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CHAIRPERSON: Good morning. Can you ask the witness to confirm that he is still under oath.

MR VERMEULEN: I do.

CHAIRPERSON: Okay.

5 ADV LEBALA: Thank you Chairperson, Commissioner Musi. Just to refresh you for matters of hygiene, we are confident that at this stage we have the declassified bundle in front of you, you have the slide bundle in front of you, you have the statement, the sworn statement of the witness in front
10 of you and you have the Criticism bundle in front of you. I see the chairperson is nodding, I'm waiting for the approval of Commissioner Musi. I see Commissioner Musi is nodding. Before we adjourned yesterday Mr Vermeulen we were about to take you to back to your statement, do you remember?

15 MR VERMEULEN: Yes Chair, I remember that.

ADV LEBALA: But before we go back to your statement I would like us to take stock and this will assist us so that we should appreciate where we would be going. Let's look at where we are in relation to where we come from in the process
20 of gravitating towards producing the submarine product. Just to summarise, is it true that the whole process ... Let's shorten it, it started with the RFI and complemented with the RFI Value System that assisted in eliminating some of the invited countries?

25 MR VERMEULEN: That's correct Chair, to be specific it

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eliminates one of the invited countries.

ADV LEBALA: Then came the RFO, complemented by the RFO Value System and that value system was used to evaluate the RFO responses as prepared by Mr Muynk.

5 MR VERMEULEN: That's correct, that was the purpose of that value system for the RFO.

ADV LEBALA: And we know that that value system that was used to evaluate the RFO's was approved by Commander Reed, Admiral Simpson Anderson who was the Chief of the
10 Navy and Mr Shamin Shaik around the 12th of May 1998.

MR VERMEULEN: Yes Chair, those were the three officials that approved the document.

ADV LEBALA: Let me refresh you, do you remember that Mr Griesel told us that the value system gets locked as it gets
15 given to ARMSCOR Procurement Secretariat, waiting or the RFO's to come?

MR VERMEULEN: That is the procedure that's followed Chair.

ADV LEBALA: Now let's pause and remind ourselves what
20 we have, taking stock, the value system that evaluated the RFO's was approved around the 12th of May 1998. Now would it be fair to say the RFO's wouldn't have arrived before 12 May 1998?

MR VERMEULEN: That's correct Chair, that's the date in
25 which the value system was handed into Procurement

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Secretariat and the offers arrived thereafter.

ADV LEBALA: Now the RFO's arrives, it's four countries, they have to be evaluated, utilising the value system that was dated 26 March 1998 that we know it was approved on the
5 12th May 1998.

MR VERMEULEN: That's the self-same value system Chair.

ADV LEBALA: When we look at the value system we kept on referring to three important indexes that play a role in the evaluation of offers. Now to summarise them we look at the
10 RFO responses which relates to the engineering, it has been demonstrated that only contributes 6.54%.

MR VERMEULEN: Correct Chair.

ADV LEBALA: The second index that we look at is the Integrated Logistics Systems, you've demonstrated to us, simplify that we look at spares, what keeps the submarine
15 product going during and after it is produced and we noted that it contributes 67.51%.

MR VERMEULEN: Yes Chair.

ADV LEBALA: And then we look at the submarine
20 product, that is the technical performance, which constitute 25.95%.

MR VERMEULEN: That's right Chair.

ADV LEBALA: Then we went to the *modus operandi* of how the value system for the evaluation of the RFO's function,
25 do you remember?

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MR VERMEULEN: Yes, I remember that Chair.

ADV LEBALA: That's where we were, the parameters, and we noted that this has been done by various teams where the Integrated Project Team in which you serve as a programme manager plays a critical role.

MR VERMEULEN: I can confirm that Chair.

ADV LEBALA: We also note that your team deals with the technical military value that keeps on encapsulating these three important indexes, the RFO responses, the Integrated Logistics Systems and the submarine product, am I right?

MR VERMEULEN: Yes Chair, those three categories form an integral part of the value system.

ADV LEBALA: And your team prepared the basic scores, those basic scores were given to the moderation team consisting of Commander Reed and Rear Admiral Howell.

MR VERMEULEN: That would be correct Chair, except that Commander Reed had been promoted to Captain Reed at that stage.

ADV LEBALA: And we know that the Moderation Team prepared an evaluation report dated, the original issue is the 25th June 1998, it was compiled by Commander/Captain Reed, permit me to say, on the 30th June 1998 and it was moderated by Rear Admiral Hall on the 30th June 1998.

MR VERMEULEN: That's correct Chair.

ADV LEBALA: Now here comes the issues, let's refresh

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ourselves, let's look at what the evaluation process considered, I think we need to take the Commission with us, we are quickly going to run it because we are at the critical stage where we want to show the Commission that the successful bidder is identified, negotiations start, that's why we will go back to your statement, but before we go there let's refresh the commissioners. Look at page 122 of the declassified bundle. We are looking at what the evaluation process considered, you can see on that page evaluation, the methodology, the value system, do you agree?

MR VERMEULEN: Yes, I agree.

ADV LEBALA: Let's refresh ourselves what the performance results were, they appear on page 123 and what we know, what has become clear is that in as far as the performance results came out Italy was number 1, France was number 2, Sweden was number 3 and Germany was number 4, is that correct?

MR VERMEULEN: That's what's reflected in the table in this document, yes Chair.

ADV LEBALA: Let's look at page 124, the next page, page 124 is headed "Costing", I don't want us to waste time on it but what is significant is it has got results, even costing. If we look at the table on costing we see that the Germans had the lowest price in terms of billions which is R4 333.70 billion, Italy are the second with R5 132.28 billion, and the French

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were the third with R5 241.33 billion, and the Swedes were the last with R5 567.68 billion. Here we look at from high to low, do you agree?

MR VERMEULEN: Yes, I agree with that Chair.

5 ADV LEBALA: And then on the self-same page the Military Index Performance comes in, we'll come back to it now. That's where SOFCOM comes in, am I right?

MR VERMEULEN: What appears in this document this is before SOFCOM comes in, the authors of this document appear
10 to have performed the military value which is ..., and then that would have been submitted to SOFCOM, so SOFCOM come in just after that stage.

ADV LEBALA: But please refresh us, when you talk of formulas in line with the slide that you demonstrated on the
15 three tiers, I think the commissioners have started appreciating why we have to go back to the three tiers with the upper tier being the political executive players. We noted that there's a formula which is being calculated at the middle tier where SOFCOM plays a role.

20 MR VERMEULEN: Yes, I recall that Chair.

ADV LEBALA: Now look at this formula that we see on paragraph 124, a get your pardon, page 124 paragraph 15, the MPI which stands for the Military Performance Index which is equal to which is equal to factor x performance score + factor x
25 logistics score + factor x engineering management score divide

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by costs. Now this formula is the same formula as the one of the military value which is being used at SOFCOM.

MR VERMEULEN: From what I recall, the explanation provided by my general manager Mr Dawie Griesel there appears to be a discrepancy in that Mr Griesel described that
5 the basic scores would be divided by the total cost, the total basic score would be divided by the total basic cost driving out a normalisation index of a 100 for the highest ratio.

ADV LEBALA: Please do not agonise what I'm going to
10 ask you to calculate, just refresh me, I missed that part, Mr Griesel said the total basic score divided by the total basic?

MR VERMEULEN: Chair, just bear in mind I'm relying on memory here.

ADV LEBALA: Fair enough, fair enough.

MR VERMEULEN: What I would recommend if you want the
15 accurate description provided by Mr Griesel is to refer to his statement, so based in my memory which may not be correct I understood that Mr Griesel said you would take the total basic score of each bid and you would divide that by the total price
20 for each respective bid. The one with the highest ratio would then receive 100 points as a normalisation index and the remaining three would then be a percentage against that winning score, that is according to my recollection which may not be one hundred percent accurate.

ADV LEBALA: Actually that statement is correct, we did
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look at that part of the testimony, the principle is the total basic score of the bid divided by the total basic price for each reflected bid and the one that has the highest ratio receives 100, that's correct. Do not agonise about it, I repeat Mr Vermeulen just to assure you, please be self-assured that we are not going to what occurred yesterday. Now let's pause here, just for your memory assist us.

The formula that was being used for the military value at the SOFCOM middle tier, how does it differ, if it does, and if you don't know, you do not know, if it does from this formula that we see on page 124, the Military Performance Index.

MR VERMEULEN: Chair, I don't know the background to the philosophy applied in this document, however, it's plain to see that it does differ slightly. One can read that in that the author would have divided the separate categories by the separate costs, the background to that I couldn't comment on.

ADV LEBALA: Fair enough. Let the record reflect the following, that you are confirming that according to Mr Dawie Griesel the total basic score of the bid is taken and it's divided by the total basic price for each reflected bid and when the highest ratio receives 100, but in here on page 124 paragraph 15 the Military Performance Index takes these three indexes that we are talking about, it takes the performance score, it takes the logistics score, it takes the engineering score and

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divide it by cost and there' s a difference there, am I right?

MR VERMEULEN: Yes, that would appear to be correct Chair.

ADV LEBALA: For the sake of completeness performance score relates to the submarine product, am I right?

5 MR VERMEULEN: Yes, you are Chairman.

ADV LEBALA: Logistics score relate to the Integrated Logistics Systems isn't it?

MR VERMEULEN: That's correct Chair.

ADV LEBALA: Engineering management score relates to
10 the RFO Responses, is that right?

MR VERMEULEN: Quite right Chair.

ADV LEBALA: And that's divided by cost as can be seen.

MR VERMEULEN: That's correct.

ADV LEBALA: Remember we are refreshing the judges
15 because this is very technical and yesterday we just took them through the scores, who had the highest score, but we were just refreshing ourselves and I'll appreciate this when we go to the last portion of your testimony at this stage. Now where the three indexes are factored in and they are divided by costs as
20 seen on page 124 something remarkable happens there, Germany becomes number 1, am I right?

MR VERMEULEN: In the table reflected under paragraph 16 that is correct.

ADV LEBALA: Sweden becomes number 2.

25 MR VERMEULEN: Confirmed.

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ADV LEBALA: Italy becomes number 3.

MR VERMEULEN: That's right.

ADV LEBALA: France becomes number 4.

MR VERMEULEN: That's correct Chair.

5 ADV LEBALA: Now the Commission has to know the following at this stage that there was a formula that Mr Griesel told us about that considers the total basic score of the bids, divided by the total basic price for each reflected bid and only the highest ratio receives 100. Now we did not want you to
10 calculate that, we'll leave it, but there's also another formula of the Military Performance Index where we take the three indexes and divide them by cost and that formula makes Germans to be number 1. You agree?

MR VERMEULEN: Yes, I do Chair.

15 ADV LEBALA: Now for the sake of completeness we do not know what would happen if we were to calculate what Mr Griesel told us about where we take the total basic score of the bids and divide by the total basic price for each reflected bid.

MR VERMEULEN: That's correct Chair.

20 ADV LEBALA: Now I would like you to look at page 125 of the self-same Declassified bundle paragraph 17, I would like you to read it for the Commission at the top. Now we, in all fairness to you Mr Vermeulen you did not prepare this, that part has become clear, and the importance of eliciting this
25 testimony is just to shed light to the Commission to make them,

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to make it appreciate the processes that were involved before we got the successful bidder, that's all.

MR VERMEULEN: Paragraph 17 reads as follows:

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“For comparative purposes the results of the RFI round held in November 1997 are tabulated in the table below”.

Shall I read the content? The content of the table reads as follows:

<u>COUNTRY</u>	<u>PRODUCT</u>	<u>PERFORMANCE</u> <u>SCORE %</u>	<u>NORMALISED</u> <u>SCORE %</u>
GERMANY	Class 209 Type Submarine	69%	100%
SWEDEN	Type 192 Celsius Kockums	66.3%	94.2%
ITALY	S1600 Sauro Submarine	65.5%	73.7%
FRANCE	Scorpene Submarines	62.5%	75.6%

10

ADV LEBALA: Now what has become clear at this stage is that the Germans are number 1, the Swedes are number 2, Italy is number 3, the French are number 4.

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MR VERMEULEN: Chair, just bear in mind that this paragraph refers to the RFI round and not the RFO round.

ADV LEBALA: Yes, we are aware. Actually something

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that is very critical, and I'm happy that we've already refreshed the commissioners about it. Now would you know as to whether are we referring to the RFI Value System at this stage?

MR VERMEULEN: No, this document per se refers to the RFO Value System.

ADV LEBALA: Now I'm looking at paragraph 17, we know that the document refers to the RFO Value System but paragraph 17 refreshes that, it recognises that before you get to the RFO Value System you study the RFI. That's all that the paragraph 17 is telling us.

MR VERMEULEN: Correct Chair.

ADV LEBALA: And paragraph 17 is telling us that there were RFI results and it's telling us that even before we deal with the RFO there were results of the RFI and it appears that the Germans were number 1 in as far as the RFI results are concerned.

MR VERMEULEN: Reading from this table it would certainly appear to be so.

ADV LEBALA: And I like the fact that you are on record as saying with the RFI we are not adjudicating, we are not making a decision, we were eliminating.

MR VERMEULEN: That's correct Chair.

ADV LEBALA: So when you eliminated the Germans were number 1, I don't know whether we eliminated the Russians, I don't know whether we eliminated the Czechoslovakians, I don't

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know whether we eliminated the Brazilians, but when we eliminated what's stubborn before the Commission is the Germans were number 1.

MR VERMEULEN: That would appear to be correct Chair.

5 ADV LEBALA: Now am I right to say the RFI Value System, remember there's an RFI which has become clear to the Commission, there's an RFI Value System, it's where the RFI Value System was applied.

MR VERMEULEN: That's correct Chair.

10 ADV LEBALA: Is it fair to say the RFI Value System plays a role in assisting towards the RFO Value System.

MR VERMEULEN: No Chair, numerically it doesn't play a role, it merely, the RFI, the main purpose of the RFI is to provide information regarding the submarines which is non-
15 binding to give the project team an idea of which submarines should be pursued further in terms of the effort required to go into an RFO, so it's a market survey, it's basically for the Navy and the project team to gain more information about modern submarines, so they can finalise a functional specification. At
20 the same time it also provides insight into which bidders did not have the potential to meet the ultimate requirement so that we can eliminate it, obviously more work would go into having a lengthy list of bidders, so you want to ensure that the listed bidders there have the potential to get through the next RFO
25 round.

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ADV LEBALA: Now with that in mind let's look at what is standing to be before the Commission. Once we were at the RFI stage trying to satisfy ourselves or the team trying to satisfy itself who to eliminate posing the following questions
5 which submarines should be pursued, which submarines would meet the potential requirements the Germans were number 1.

MR VERMEULEN: Based on information contained in this table, yes.

ADV LEBALA: Am I right to say it informs us that at that
10 stage there was all the reasons to pursue the Germans?

MR VERMEULEN: No Chair, I wouldn't say that. For one what's difficult to analyse in this table is I don't know the background to what formula they used here. If you recall the SOFCOM provided a formula for use in the RFO evaluation, I
15 don't know the background to the figures here, I don't know how they arrived at these normalised performance costs because the same formula that was used in the RFO was not necessarily applied here.

ADV LEBALA: Mr Vermeulen assume I agree with you, full
20 square I agree everything you say, but the underbelly that makes what you say vulnerably is as follows; the Commission has been taken through number 1, number 2, number 3, number 4, if the RFI Value System is not important then why do we rank them? This might sound unfair but we are ranking them
25 still.

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MR VERMEULEN: Chair, I don't see any significance in this ranking because at RFI level you are not selecting any of these bidders, that's why you have to go to the effort of going to an RFO where you rank them. I honestly don't see the value in ranking these bidders.

ADV LEBALA: Then answer the following question, what's the logic of making the Germans number 1, the Swedes number 2, the Italians number 3, the French number 4, and you have seen why in other indexes we make them number 1, number 2, number 3, number 4.

MR VERMEULEN: Chair, I would have a concern in placing significance on these results namely for the following reason, if you recall when you go out on RFI the offers, the pricing, the information per se in that RFI is not binding. Any one of those bidders quite rightly reserves the right between the RFI phase and the RFO phase to refine his offer, so you can't set any store [sic] on the values and the information and data you obtain in an RFI offer as opposed to an RFO offer which is formal and binding, so to go and put effort into analysing the results in an RFI to me is a fruitless effort.

ADV LEBALA: I'll leave it to the Commission to make its mind, hence I'm posing the following question, why are they ranked in line with all those other indexes?

MR VERMEULEN: Chair the best way to answer that, to get an answer on that is to ask the author of this document that

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question.

ADV LEBALA: Fair enough. Now let's look at the essential documents that helped us to come to the conclusion we reached in ranking these. I beg your pardon, I think the
5 Commissioners are conferring, probably they have a concern. Let's pause.

CHAIRPERSON: Okay, you can go on.

ADV LEBALA: Mr Vermeulen you will note that it's appropriate when I sense that the commissioners are conferring
10 not to go on because they could be raising probably an aspect where they want to inform each other, probably they would like to ask you a question but we proceed now. Let's look at the essential documents that helped us to come to the conclusions we reached yesterday. Let's quickly go through page 99 to 100
15 of the self-same bundle, the Declassified bundle. Page 99 and page 100. We know that this document is the value system for the evaluation of the RFO. Am I right to say that this document assist us in appreciating the scoring guidelines and denoting the names of the team members?

20 MR VERMEULEN: It does that Chair.

ADV LEBALA: What we know also is that the date of its original issue was the 26th March 1998 and it was signed on the 12th May 1998.

MR VERMEULEN: Yes Chair.

25 ADV LEBALA: It is that document that was approved by

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Mr Shaik.

MR VERMEULEN: I can confirm that.

ADV LEBALA: Let's look at page 118 and 119 of the self-
same bundle Commissioner Musi and Chair. This document is
5 the Submarine Evaluation Report dated 25th June 1998. We
know it was compiled by Commander Reed and it was
moderated by Rear Admiral Howell on the 30th June 1998.

MR VERMEULEN: That's correct Chair.

ADV LEBALA: Please go back to page 110 paragraph 9.5.
10 We know that it's a document that assist us to appreciate the
scoring and the team members, now we note something in page
110 paragraph 9.5 that there was a team which was the
Evaluation Team for Submitted Offers, something remarkable is
happening here. You were a member of that team, am I right,
15 you are number 4?

MR VERMEULEN: I was a member of that team, yes Chair.

ADV LEBALA: Rear Admiral Howell is a member of the
self-same team.

MR VERMEULEN: Yes, his name appears here Chair.

ADV LEBALA: Is this the team that assisted in the basic
20 scores that were taken to the Moderation Team?

MR VERMEULEN: This team consisted of members who had
participated in the basic scoring, quite correct, that also
consisted of two members, Admiral Howell and Commander
25 Reed who did the normalisation of those basic results as well,

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so it was a mix to answer your question.

ADV LEBALA: But of significance it is the team that prepares the basic scores that were taken to the Moderation Team.

5 MR VERMEULEN: Yes Chair.

ADV LEBALA: Now something remarkable is happening here. Mr Howell is a member of this team and he also moderates, do you want to comment, and this might sound unfair to you.

10 MR VERMEULEN: Unfortunately I'm not really in a position to comment on that Chair.

ADV LEBALA: Would you agree with me if I were to say there's no way in which you can be a referee and a player at the same time?

15 MR VERMEULEN: I understand your concern Chair.

ADV LEBALA: Is it a concern to you that Rear Admiral Howell was a member of the Evaluation Team that prepared the basic scores and he also moderates?

MR VERMEULEN: No Chair, and I'll tell you why it was not a
20 concern. At the time this value system was compiled there was no mention of Admiral Howell performing a function subsequent to this document as a moderator, I didn't know such a document would materialise, so taking this at face value at the time my assumption was that a senior submariner was participating in
25 the scoring.

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ADV LEBALA: And Mr Vermeulen, I'm sounding unfair to you because Rear Admiral Howell must come and answer this question, but let me ask you this question, ordinarily let's take an exam, you are learned, you went to school, when you wrote
5 your technical engineering exams there was an examiner, am I right?

MR VERMEULEN: Correct.

ADV LEBALA: That examiner cannot be the moderator of your script isn't it?

10 MR VERMEULEN: I understand your problem and I agree with you.

ADV LEBALA: So you agree with me that the function of an examiner and moderator are different?

15 MR VERMEULEN: They are different. I just want to reiterate again that when this document was written there was no talk of a moderator being put into place thereafter.

ADV LEBALA: Fair enough, hence I say only Mr Howell should come and explain and this question sounds unfair to you, albeit it must be recorded, they make us to raise
20 eyebrows. With a view to achieve the goal of trying to explain these processes, remember your testimony is so critical to explain to the Commission what happened from the beginning before this product submarine, especially the German Submarine Consortium, submarine the Type 209 arrived in
25 South Africa, do you understand where we are going I suppose?

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MR VERMEULEN: I understand.

ADV LEBALA: Let's soldier on.

CHAIRPERSON: Advocate Lebala let me just try and find out something from the witness, I understand that at the time
5 when this Evaluation Team was announced and you realised that Mr Howell is one of them, at that time you were not aware that he will later on be appointed a moderator. Now the question is were you surprised when later on you learned that
10 Mr Howell who was on the team with you is now a moderator of the same scores that were prepared by the team to which he was a member, were you surprised by that or you felt that was normal?

MR VERMEULEN: Chair I was surprised, I was in fact more surprised to learn of the RFO Evaluation Report in my
15 statement yesterday or in my testimony yesterday, I actually stated the fact that I only learnt of that RFO Evaluation Report during the course of preparing my statement in these last few weeks. I was unaware of that document up until this time.

ADV LEBALA: Thank you Chair. Let's look at the page
20 123. We have the performance results, we are refreshing ourselves. With the Performance Result we note that the Italians were number 1, the Swedes were number 2, the Germans were number 3, the French were number 4.

MR VERMEULEN: Correct Chair.

25 ADV LEBALA: Page 124. We've dealt with it

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demonstrating the costs and we know the answer that on the cost side the Germans were rated number 1 because we were going to pay less money if we considered their price, am I right?

5 MR VERMEULEN: Chair, quite honestly I don't know how these results are arrived at because as you can see in that Military Performance Index the costs are separated according to the three categories, I'm not sure how those specific costs for those categories were arrived at, so it's very difficult to
10 analyse this in its entirety, you have to have that information to be able to confirm the accuracy of these figures and unfortunately those figures allude me, those costs, those individual costs allude me.

ADV LEBALA: You could be rest assured that if I asked
15 you a question to tell us how these figures were computed Mr Solomon would object, that's not my question. My question is when it comes to costs the Germans were number 1 because we were going to pay less money for this submarine if we considered them, that's my question because costs were a
20 consideration. In South Africa, I have to be careful not to testify, you see in South Africa we have a Constitution and procurement principles that emphasise a number of five elements, amongst them it's competitiveness and cost efficiency, transparency, so costs are significant and you
25 testified about it yesterday, you remember?

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MR VERMEULEN: Yes Chair I do, I just have a bit of difficulty in confirming what you are saying in that I showed you the approach that ARMSCOR would have followed yesterday where cost obviously is vitally important where we showed you that the four submarines met the requirement and then the next step would be to consider the cheapest price, however, this doesn't necessarily follow that path. If you look at the previous table in page 10 it doesn't follow that path because you will see there the Italians are normalised at 100. Now we all know, as I showed you yesterday they're in fact a lot more expensive, so if you see my difficulty in concurring with what you are saying.

ADV LEBALA: But that's the point. Isn't it true that yesterday you testified that we took the Germans cost-wise or considered them because we were going to save R800 million-odd had we taken the next price which was higher than this?

MR VERMEULEN: Chair can I put that graph back on the wall?

ADV LEBALA: There's no need, there's no need, I think here Mr Vermeulen I'm going to beg you, there's no need. Yesterday you demonstrated to this Commission that one of the reasons why the Germans cost-wise were better in that graph, for instance let's look at the ... The Commissioners have got it?

CHAIRPERSON: Just hold on Advocate Lebala. Mr

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Vermeulen the question is simple, according to your evidence yesterday the Germans were offering on their submarines at a much cheaper price compared to the others, according to your own evidence yesterday, is that correct or not?

5 MR VERMEULEN: Chair, you are a hundred percent correct and I emphasised it yesterday, they were in fact 18% cheaper, significantly cheaper, however, because of the SOFCOM guidelines we couldn't follow that approach, we didn't automatically say the Type 209 Submarine meets the Navy
10 specification, it's by far the cheapest, let's select them as preferred supplier, that would normally be the case and this is what I always explained yesterday, that would normally be the case in ARMSCOR's procedures, however, that normal procedure was deviated from and then the cheapest price in
15 fact was not the major consideration and that's what I'm trying to express here.

ADV LEBALA: Just to anchor on the heel of the chair's question, assume I agree with you that SOFCOM could have considered other things but let's look at what we have in front
20 of us and what you demonstrated yesterday when you look at the slide bundle. Please go to page 7 of the slide. You could even project it on the screen if you want to. Now do you remember yesterday you testified demonstrating the percentage of 60.20% in relation to the figure of R4.333 billion?

25 MR VERMEULEN: I did Chair.

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ADV LEBALA: You compared it with the Italian figure of 74.17% at R5.132 billion.

MR VERMEULEN: Yes I did Chair, that was the second cheapest of the four bidders.

5 ADV LEBALA: You concluded by saying if we took the Germans we were going to spend R800 million-odd less.

MR VERMEULEN: I did say that Chair.

ADV LEBALA: And you remember I asked you whether was price a factor in as far as awarding the Germans to be the
10 successful bidder.

MR VERMEULEN: Yes I did Chair and I replied to you by saying that under normal circumstances the prices is paramount, that's the word I used, it's paramount, it is vitally important and taking into account the factor that the German
15 Submarine Consortium submarine met the minimum requirements of the specification without hesitation, and I said this to you yesterday as well, under normal circumstances if ARMSCOR was doing this adjudication I would recommend in the submission to my board of directors on those key factors
20 the bid meets the requirement and it's the cheapest, I would recommend to my board of directors that I be granted authorisation to enter into a negotiation phase and they get selected as a preferred supplier. That's under the ARMSCOR process, however, when you bring industries and normalising
25 into the account the price does not enjoy that same paramount

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importance and that's what I tried to reflect yesterday.

ADV LEBALA: Yes, you did. Let's pause, I think the commissioners are conferring.

CHAIRPERSON: Okay sorry, you can continue.

5 ADV LEBALA: Mr Vermeulen I don't know today but as a programme manager you might be privy to, actually this is ubiquitous, lawyers use this term, it's a known fact, I think we are the only country in the world that constitutionalise procurement, are you aware?

10 MR VERMEULEN: I don't know if that is true Chair.

ADV LEBALA: Now well for your own edification this is very significant and then you understand its relevance and I see that Solomon SC might like to object. I just want the record to reflect the following, that cost is a consideration in
15 our country when we procure services, especially when our government or its organs of state procure services.

MR VERMEULEN: Chair I'm slightly confused here, I fully agree with you and ARMSCOR endorses that fully. Cost is of paramount importance when making the selection of a bid,
20 there's no question of that and I certainly am not attempting to contradict that in any way.

ADV LEBALA: Thank you. Remember we are still looking at the ...

JUDGE MUSI: Can I jump in Advocate Lebala without
25 interrupting you, I just want to make sure and understand what

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the witness is actually saying and I understand him to say that if you were following the ARMSCOR process, as long as all those bidders meet the minimum requirements you would go for the cheapest?

5 MR VERMEULEN: That's exactly what I'm saying Chair.

JUDGE MUSI: But then you say that because this was not, that process was not followed here you don't know what, precisely what process the SOFCOM followed in arriving at the winning bidder.

10 MR VERMEULEN: Chair, the approach SOFCOM followed, and you were given tier guidelines of it, is that you would take each one of these scores and associated prices, you divide them. When you divide them you will find that the Fincantieri Italian bid actually gets a higher score, it's called a figure of merit
15 where you take their score and you divide it by price, then that philosophy is not followed. You equate that then to a 100 and the others are a percentage of that and it is reflected in this slide in paragraph 10 where that in fact happens. If I could ask, if I could point you towards that Chair it's page 123 in the
20 Declassified bundle.

In that paragraph 10 Chair you will see that the Italians, notwithstanding the fact that they are more expensive than the GSC they are normalised to 100, in other words they are reflected as coming first, the others are then a percentage
25 of that. Now that is in accordance with the SOFCOM

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procedure, so there's a distinction here between the normal process that would be followed and the process that was adopted by SOFCOM.

JUDGE MUSI: Thank you.

5 ADV LEBALA: Commissioner Musi, I beg your pardon, the chair wants to probably ask a question?

CHAIRPERSON: No, no, I just want to make an note.

ADV LEBALA: Oh, the chair wants to make an important note, let's wait.

10 CHAIRPERSON: Thank you.

ADV LEBALA: Commissioner Musi's question ignites some thoughts on my mind and I think we need to close this by asking you the following question. Is it true that ARMSCOR is represented at SOFCOM?

15 MR VERMEULEN: Yes, they are represented Chair.

ADV LEBALA: It's correct to say actually SOFCOM is chaired by two chairpersons and we know that during the SDPP's it was chaired by Mr Shamin Shaik, the Chief of Acquisition for the Department of Defence and Mr Esterhuyse,
20 the General Manager of Acquisition from ARMSCOR.

MR VERMEULEN: Quite correct Chair, they were representatives of SOFCOM.

ADV LEBALA: Thank you. Now remember we are looking at the essential documents that helped us to come to the
25 conclusions we reached in choosing the successful bidder.

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Let's look at page 141 and 142 dealing with the logistic evaluation of the offers, the self-same bundle Chairperson, Commissioner Musi. At page 141 the title of the document is "The Logistic Evaluation of the Offers". In simple terms what
5 does this mean?

MR VERMEULEN: Chair, this was a report that singled out, I think I mentioned the three categories, there was a RFI Response, there was a Submarine Product System Category and there was an ILS, the Integrated Logistics Support
10 Category. This report addresses the ILS category.

ADV LEBALA: Thank you. We see that the date of its issue just below there is 28 June 1998, can you see on the page 141 Chairperson, Commissioner Musi?

MR VERMEULEN: Yes Chair, I note that.

15 ADV LEBALA: Let's go to page 142. We see that it was compiled by Mr FH Zietsman, it was accepted by, is it Commander Reed?

MR VERMEULEN: Yes it is, it is accepted by Captain Reed yes.

20 ADV LEBALA: It was also moderated by Admiral Howell.

MR VERMEULEN: I note that Chair.

ADV LEBALA: Now let's look at the scores that would be coming out of that evaluation. At this stage we are only looking at the Integrated Logistics Systems, am I right

25 MR VERMEULEN: Yes Chair, that's correct.

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ADV LEBALA: If you look at page 151 the scores are as follows; there's a graph at the top saying "The Overall Score", the scores are as follows, the Italians are number 1, the Swedes are number 2, the French are number 3, the Germans
5 are number last.

MR VERMEULEN: I note that Chair.

ADV LEBALA: Let's look at page 152 and 153, the Product Evaluation of the RFO. If you look at page 152 the document is titled "Product Evaluation of the RFO", simply in
10 simple terms just tell the commissioners what are we looking at.

MR VERMEULEN: Yes Chair, again I just draw your attention to the three categories that are contained in the value system, the RFO Response, the ILS value and the Submarine Product
15 System value, this is the RFO Response.

ADV LEBALA: Thank you. We realise that the date of its issue is the 28th of June 1998 on the self-same page 152, are you with me?

MR VERMEULEN: Yes, I am.

ADV LEBALA: Page 153, its compiled by Mr Zietsman, it's approved by Commander Reed and it's the person responsible, now what does responsible in that column mean, we see that there is a signature, it's a signature of Rear Admiral Howell, do
20 you agree?

MR VERMEULEN: I agree that it is his signature, I'm not
25

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sure how to describe “responsible” in this context.

ADV LEBALA: Would it mean, moderate, would responsible mean responsible for moderation?

MR VERMEULEN: I would have to speculate, I don’t know.

5 ADV LEBALA: Now back to my question and this I think might sound unfair to you, is it strange for you at this stage that Rear Admiral Howell was playing a role in significant teams, all of them almost and at the same time he ends up moderating at this stage? Now I’m taking you through this
10 documentation for a purpose, I’m eliciting your comment at this stage of your testimony before the Commission, is it strange to you?

MR VERMEULEN: Chair, Admiral Howell was appointed Director Naval of Acquisition, I’m not sure what his Terms of
15 Reference are, I don’t have that information, so I couldn’t comment as to whether it’s strange or whether it’s normal, I really don’t know, I don’t know what his Terms of Reference and his portfolio consisted of.

ADV LEBALA: Now that’s not my question as to what his
20 portfolio consisted of and because that part you can’t answer, you were not part of it, we don’t know what was in the mind of those who deliberated that he should be appointed but my question is do you find it strange?

MR VERMEULEN: I can’t comment on that Chair.

25 ADV LEBALA: Fair enough. Look at page 160, that’s the

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outcome of the scores for the product evaluation of the RFO Responses, we note that the Italians are number 1, the Swedes are number 2, the Germans are number 3 and the French are number 4.

5 MR VERMEULEN: Yes, I take note of that.

ADV LEBALA: Now at this stage we had a successful bidder, am I right?

MR VERMEULEN: Yes, we did.

10 ADV LEBALA: Now we took the Commission through the process of demonstrating what made the Germans to be the successful bidder and you put it well on your statement. Please look at your sworn statement page 9 paragraph 3.21. We are going back to the Vermeulen bundle paragraph 9. I beg your pardon, page 9 Commissioner Musi, Chairperson,
15 paragraph 3.21. It seems to have been a very long journey to come here and I'm, it's a passionate thinking in our mind that we hope the Commission appreciates why we had to go through these twists and turns to come to paragraph 3.21. Are the Commissioners with us? May I take the liberty to read it:

20 *"In November 1998 Cabinet announced that in the case of the submarines the ..."*

I beg your pardon, Commissioner Musi is not with us. It's the Vermeulen bundle Commissioner Musi, page 9 paragraph 3.21. Is Commissioner Musi with us? Thank you.

25 *"In November 1998 Cabinet announced that in the*

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5 *case of the submarines the German Submarine Consortium had been selected as the preferred supplier. Also during November 1998 Cabinet mandated the International Offers Negotiation Team (IONT) to negotiate with each of the preferred bidders in respect of the SDPP in order to finalise equitable and affordable contracts”.*

MR VERMEULEN: Correct Chair. Chair, could I just go back to your previous point, a minor correction. When you were
10 discussing this RFO Response Report the preferred supplier had not been selected at that stage.

ADV LEBALA: I think that has become clear. What seeks to advise us, we just want to demonstrate the link as to, remember we took you through the scores, there’s a reason why
15 we took you through the scores, you discussed the graph, we debated some of the points, moderation, that’s why the three tiers were very important. That connection to fit the jigsaw puzzle is going to come now. At this stage after all these processes were done we know that, and that’s why we had to
20 demonstrate that at a certain point you cut off, that is why we took you through those three tiers and in all fairness to you it accredits you because you want to demonstrate to the Commission that they don’t play a role from a certain point going up, do you appreciate it?

25 MR VERMEULEN: Yes, I do Chair.

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ADV LEBALA: Now is it true that what we went through up to so far, the scores, the debates that we had had, had played a significant role to explain why the German Submarine Consortium was appointed as a preferred bidder?

5 MR VERMEULEN: Yes I do Chair, it all built up to an eventual outcome.

ADV LEBALA: The scores played a significant role in the results that rendered the German Submarine Consortium being the successful bidder.

10 MR VERMEULEN: Yes, I would concur with that Chair.

ADV LEBALA: Here's an unfair question. You remember those three tiers we showed you? Please go back to that slide. It's on page 8, we call it the Slide bundle Commissioner Musi and Chairperson. We wanted you to explain the slide by starting below-up, this time we'll start up, going down. Do you have an idea as to whether any party in the upper tier played a role irrespective of the scores because we know the underbelly that makes some of the conclusions and the scores vulnerable and questionable, that part has become clear, it's not for you to debate, I think the commissioners will make their own minds.

20
25 Would you say the players in the upper tier who we demonstrated, remember Cabinet, the President, the Minister's Committee, did they play a role in the announcement and appointment of the German Submarine Consortium as the preferred supplier?

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MR VERMEULEN: To the best of my knowledge they would have played a role in that they accepted the findings of the SOFCOM, SOFCOM would have made a recommendation to Cabinet and presumably on the strength of that
5 recommendation Cabinet under due consideration would have made a decision in favour of the German Submarine Consortium.

ADV LEBALA: Here's an evaluative question. Do you have an idea how much role they played?

10 MR VERMEULEN: No Chair, apart from what I had just surmised I couldn't comment further, I can only make assumption that that was the process that was followed.

ADV LEBALA: Thank you. Remember I'm asking you this question in the context of the underbellies of the vernacular
15 that demonstrated that some of these scores make one to raise eyebrows, am I fair?

MR VERMEULEN: I couldn't really comment on that Chair.

ADV LEBALA: Well it's for argument I think and I shouldn't have asked you this question in actual fact Mr
20 Vermeulen, I sound unfair now, I beg your pardon. Now here's that the process where you start to be engaged again as a programme manager, the negotiation phase. Now the Commission is starting to appreciate what happened from the RFI, RFI Evaluation, RFO, RFO Evaluation, you punching, your
25 integrated team punching the basic scores, the Moderation

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Team pitching them high to SOFCOM, you confirm now that SOFCOM pitched that high to the upper tier, you say the upper tier did play a role to an extent as you surmise. Now we know who the preferred supplier is, (indistinct) the process.

5 Paragraph 4 "Negotiations", page 9 paragraph 4.1:

"The negotiation phase was entered into with the German Submarine Consortium which commenced in November 1998 and concluded in June 1999. Given my role as the programme manager I was directly

10 *involved with the negotiation phase of the process at the technical level, specifically with regard to the Submarine Product System".*

The Commission appreciates why we spend time at the lower level explaining to them that you were involved at a technical

15 level, the military value of the submarine, now everything changes now. Why were the negotiations important?

MR VERMEULEN: Chair, what makes a negotiation phase necessary is that if you recall yesterday I mentioned one example was some draft plans were provided with the offers,

20 we also received a technical specification, what we call a product specification or build-specification. Each of the respective bidders provided that. We would then now have to take that a step further so that we could achieve a contract baseline which would enable us to place contracts. That would

25 entail the establishment of all the contractual terms and

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conditions, It would have entailed finalising the technical specification. If you recall at this stage we haven't, we have not been able to deal directly with the supplier, we received their bids, we reviewed them, now the preferred supplier had
5 been selected, now we can talk directly to the preferred supplier, so we would start negotiating a number of issues.

My responsibility during the negotiation phase was to arrive at a contract baseline which essentially is what the negotiation phase drives out. You get to a mutually accepted
10 technical specification, you are going to obviously fine tune or calibrate the specifications provided in the offer, in some respects you customise those specs to the Navy's unique requirements.

One of the issues that we would have to discuss
15 and it comes out here, is contractual milestones, the offers don't necessarily allude to contractual milestones, it's only when you are able to go down to a lower level with the preferred supplier do you finalise all that level of documentation. You would be looking at for instance a master
20 production plan.

The contractor provided for what he saw as a production plan, we would take it to a lower level and we would tailor that together with the contractor, at that stage the preferred supplier, not a contractor yet, so we would finalise
25 all those levels of documentation, we had finalised the quality

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assurance plan, we had agreed on the acceptance test procedures, all of that level of detail you would do during the negotiation phase.

5 There are some more and I have got them, I'm just going from memory right now, I have listed further ones here, but essentially that is the main objective of a negotiation phase to arrive at a mutually acceptable contract baseline, mutually acceptable to ARMSCOR, to our board of directors normally and of course also mutually accepted to the preferred supplier,
10 you've both got to agree to how this project will go forth from here because from there on you enter into a production phase, so obviously all the documentation you need has to be in place.

Once that contract baseline is achieved it's a formal baseline, if there are any changes that occur after that they get
15 changed through formal processes, if they are technical changes it would mean engineering changes would have to be put into place, if they're contractual changes you would have to do a contract amendment, so from there on it's a very structured approach you always measure back to the baseline,
20 and that's what I strived to achieve during this negotiation phase.

ADV LEBALA: Chair, I note that it's almost 11h30. I don't know whether this is the right time for adjournment.

CHAIRPERSON: We'll take a tea adjournment for about 20
25 minutes or so. Thank you.

(Commission adjourns)

(Commission resumes)

CHAIRPERSON: Thank you.

NOTE: Witness confirmed to be still under oath.

5 CHAIRPERSON: Thank you. Thank you.

ADV LEBALA: Mr Vermeulen, I just want to fast track your testimony, in actual fact I had an ambition to make it a point that we are done with you before 14h00. You have testified about your role in the negotiation phase with your cap
10 on as a programme manager and as a member of the Integrated Project Team, is that correct?

MR VERMEULEN: It's correct Chair.

ADV LEBALA: Now quickly take the Commission through the slide where you demonstrate the levels of negotiations
15 having laid the basis why there had to be negotiations and that will be on page 9 of the Slide bundle Commissioner Musi, Chairperson, page 9 of the Slide bundle. You've explained it so well that now that the successful bidder has been identified to engage the bidder for the first time there's got to be
20 negotiations and that's why we kept on trying to explain what the contract baseline is, we've explained it, that's where you have the challenge of bringing documents that will form the basis of the contract and control comes in, there must be accountability, you've got to negotiate with the German
25 Submarine Consortium, you've got to conclude negotiations,

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you end up signing the main agreement, the industrial participation elements come in there, am I right?

MR VERMEULEN: Yes Chair, you are right.

5 ADV LEBALA: So the contract baseline is not only a set of free floating documents, am I right?

MR VERMEULEN: No Chair, it's a suite of documents.

ADV LEBALA: Yes, but it's a significant document that are important during the submarine life cycle that form the basis of that contract.

10 MR VERMEULEN: Quite right Chair, the documents address the production phase specifically, the further acquisition process and yes, it addresses the through-life support of the submarine as well.

15 ADV LEBALA: Now please take the Commission through the agreement hierarchy having explained that there were two tiers where members of the Integrated Project Team negotiate with the German Submarine Consortium where you also are part of that team as a programme manager, am I right?

MR VERMEULEN: That's correct Chair.

20 ADV LEBALA: Now explain to the Commission the two tiers of the negotiating teams.

MR VERMEULEN: Yes Chair, the first tier was managed by the International Offers Negotiation Team, the "IONT", and their responsibility was to arrive at a completed umbrella agreement with the contractor, and the umbrella agreement as

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you can see in that slide that I present consists of a number of lower level documents, the supply terms, the DIP terms, the NIP terms and the financial terms, in other words all the facets that make up the entire contract. The lower level tier ..., can I
5 proceed?

ADV LEBALA: Yes.

MR VERMEULEN: The lower tier in the case of the submarine project is whether the Integrated Project Team comes in. We would typically address the Supply Terms Agreement which is a
10 contract, a speciality-type contract that addresses the Submarine Product System and then it's got a number of annexures and I'll mention a few of those as an example, the most, or one of the most important being the technical specification, so that has to be finalised during the negotiation
15 phase, the contractual terms and conditions associated with the submarine and a number of other annexures as well.

For instance one example is what sort of equipment and services would the client, the Navy provide. There are a number of annexures, I think there were over 20 all-in-all, it
20 would be a confidentiality agreement, it would be the trafficking arms requirements that would have to be brought into account, so a wide array of annexures were included in the supply terms and these all had to be finalised during this negotiation phase.

25 ADV LEBALA: Now at this stage we know that there are

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two negotiating teams, the International Offers Negotiation Team discusses with the German Submarine Consortium about what are they bringing to South Africa in as far as the DIP component is concerned, am I right?

5 MR VERMEULEN: Amongst others, correct.

ADV LEBALA: Now with the DIP component is that where we seek to benefit about the Defence Industrial Participation negotiating with the German Submarine Consortium as to what could the South African Government leverage in as far as the benefit that would arise from those negotiations are concerned.

10 MR VERMEULEN: Exactly that Chair.

ADV LEBALA: Does it inform us that at that level the International Offers Negotiating Team had a specialist component that deals with the DIP component?

15 MR VERMEULEN: I'm not hundred percent sure Chair, I don't know if the IONT would rely on the expertise at a lower level of the DIP specialists who finalise those terms.

ADV LEBALA: But we also know that at that level also the NIP, National Industrial Participation terms were also negotiated.

20 MR VERMEULEN: That is correct, and the Department of Trade and Industries would have been involved with that exercise.

ADV LEBALA: Of course as far as the DIP is concerned
25 the Department of Defence would be involved with that

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exercise.

MR VERMEULEN: ARMSCOR was specifically involved in that exercise Chair.

CHAIRPERSON: Excuse me, I missed that.

5 MR VERMEULEN: Sorry Chair, in terms of the DIP terms the conditions surrounding that would have been negotiated by ARMSCOR.

ADV LEBALA: The negotiations that were effectuated by the International Offers Negotiating Team also included the
10 negotiating financial options with the German Submarine Consortium?

MR VERMEULEN: Yes, there was a team of specialists involved in that exercise as well.

ADV LEBALA: Just simplify for the Commission if you can
15 what financial options were being discussed.

MR VERMEULEN: From what I understand, and I have a very limited knowledge of that, obviously the outcome of it impacted me, but that would typically address the loan agreements, the period in which payments would commence and the timeframe
20 for payments amongst others but I'm talking outside my line of expertise here totally. I could just, however, say that during the negotiation phase of the supply terms there was a correlation there in that I had to negotiate contractual milestones and that obviously had to fall within the timeframe
25 within the constraints that were finalised under these

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agreements, so my milestones had to fit in with that.

ADV LEBALA: Now the International Offers Negotiating Team, was it negotiating on behalf of the Government of South Africa or on behalf of the Department of Defence?

5 MR VERMEULEN: Chair, I'm not familiar with their terms of reference, I can assume that they were operating on behalf of the Government of South Africa.

ADV LEBALA: Is this informed by the fact that it was a government-to-government procurement?

10 MR VERMEULEN: I would hesitate to agree fully with that Chair, I understand it to have been a government in the case of South Africa to a shipyard agreement.

ADV LEBALA: Okay it's not within your expertise, don't bother about it but we know what the SDPP's were all about.
15 Now that's the first tier. The second tier where you played a significant role you guys were just as specialists, you were involved with what I would call a unique type of contractual negotiation that has to make it a point that this submarine product is brought to South Africa, there it was a technical
20 speciality isn't it?

MR VERMEULEN: Chair it encompass more than technical conditions in isolation, if I could give an example, to get the ball rolling with the negotiations I requested the German Submarine Consortium to provide me with a draft contract,
25 sanitised with another of their foreign clients so I could gage

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their approach towards contract, and one of the first things I learned when I evaluated their draft contract was that they didn't incorporate milestones into their payments, they had standard financial draw-downs each year, and that was immediately totally unacceptable.

In ARMSCOR we work with contractual payment milestones so we can leverage the control we need during the production phase, in other words we don't just release payments automatically during the course of the project, we release them conditionally. I can give you an example, when all the sea trials of the first submarine are completed it's a contractual milestone, we have conditions associated with that and we would release payment on the successful conclusion of that specific effort.

So, I went through a lengthy period where I had to negotiate contractual milestone payments with the contract, so just to get back to your question it didn't, it wasn't relegated only to the technical specification itself.

ADV LEBALA: Now let's try a fine line here, the International Offers Negotiating Team focused on discussing the technical side, the military value, they focused on discussing the industrial participation which looked at NIP and DIP, and they also looked at the financial option, am I right?

MR VERMEULEN: You are correct Chair. I could just add in a very limited sense to talking only about the supply terms, I'm

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not sure exactly the extent of their involvement with respect to the other categories. With respect to the supply terms they relied very much on the product team to arrive at a conclusion in that regard.

5 ADV LEBALA: In as much as the Integrated Project Team focused on other areas I can imagine you wanted to demonstrate that you know the, you'd be a prudent programme manager, you didn't allow the German Submarine Consortium to take ARMSCOR and South Africa for granted, you'd bargain
10 better, you'd negotiate better, you'd leverage where you have to leverage which means that you touch on finances, but honestly speaking the side of your negotiation team was to focus on the speciality-type of making the point that this submarine product meets the technical specifications, am I
15 right?

MR VERMEULEN: Yes Chair, and in so doing if I could just elaborate a bit, one of the concerns, and it was discussed at length yesterday, was the fact that the German Submarine Consortium did not offer a substantial integrated logistic
20 support package as you are aware, and as such they were penalised in the scoring of the value system.

Once it was announced that the German Submarine Consortium was the preferred supplier my strategy then was to try and bolster that ILS component, it was obviously
25 unsatisfactory and I set about trying to improve on that within

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the financial ceiling approved by Cabinet, in other words my limitations were as such I couldn't go and try and negotiate additional items into the scope of supply and thereby increase the price, however, I could work within that price and try and leverage, if I could say, use the term arm-wrestle further elements, deliverables into that price and that's what I set out to do especially in the area of integrated logistic support.

ADV LEBALA: Well, you did that as a member of the Integrated Project Team?

10 MR VERMEULEN: Yes Chair, I did that in my capacity as programme manager.

ADV LEBALA: And the task was to focus on the supply terms, that you qualified that not only were they confined to the speciality-type of making it a point that the Submarine Product System meets the technical specification but it also went beyond where you could even leverage money, make it a point that we pay lesser costs, you get more spares, things like that, am I right?

20 MR VERMEULEN: Yes Chair you are quite right and in that specific regard again within the price, the ceiling price set by Cabinet I also leveraged, and a big concern again going back to integrated logistic support the Germans offered a ceiling price within their offer for spare parts which we considered inadequate, so I set about negotiating during the course of this period a much improved spare parts supply to the effect that

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initially, and I got the figures here, initially in the German offer they offered \$12.4 million US worth of spare parts, we managed to push that up to €26.1 million as the contract was finally placed in Europe.

5 The way we did that was, the strategy I used was I told the GSC that there's huge risk in the offer with respect to integrated logistic support and I would have no choice but to report to my principals that that was a risky project in terms of logistic support, unless we can set about improving it within
10 the price they offered, and that's what I did to the effect that spare parts were increased within the price, within the price set by Cabinet from the \$12 million US-odd to €26.1 million. And there were other integrated logistic support elements that we also managed to incorporate into the scope of supply within
15 the set price when, I can elaborate on it if you wish to and I have some slides just to try and portray that a bit clearer to the Commission when you are ready.

ADV LEBALA: We know the role that you played in the negotiations that you exercised your prudence as the
20 programme manager as part of the Integrated Project Team. You referred to your principals, who are you referring to?

MR VERMEULEN: In my case I report to a divisional manager, I was then in the Maritime Division of ARMSCOR, it's now named the Naval System Division, I have a divisional
25 manager that I report to but more specifically in the case of the

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negotiation phase I reported to the Project Control Board together with the project officer.

ADV LEBALA: I see that you told us about where you negotiated with the German Submarine Consortium in as far as the Integrated Logistics Systems are concerned in the light of the spare parts that were needed. In that case I would like to draw your attention to page 11 of your statement, paragraph 4.6.2.1, is that what you are referring to, and please read it for the record?

10 MR VERMEULEN: Yes Chair, this is one of the examples I'm referring to where the ceiling price for spares provisioning was increased from \$12.4 million US, which was reflected in the offer, to approximately €25 million, to be exact it was, when we placed the contract it was €26.1 million.

15 ADV LEBALA: Now when does this happen, does it happen when the production phases started or during a time when the contract baseline was being negotiated?

MR VERMEULEN: Chair, the actual discharging of that money takes place during the production phase, it's a ceiling amount, the production phase has two main activities running concurrently, the one is the production of the submarines and the other is the completion of the integrated logistics deliverables. Now one of those deliverables would be spare parts. The philosophy used was a ceiling amount of R26.1 million [sic] was established within the contract.

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During the production phase we would have a series, and I'll discuss it when I talk about the production phase, a series of what we called spare parts conferences, there were a number of subcontractors involved with the submarine, the German Submarine Consortium was a prime contractor, there were a number of subcontractors, we would have technical discussions with each respective subcontractor to determine the needs, the spare parts requirements for that specific subsystem.

If I can give you an example, the navigation radar, we would talk to the original equipment manufacturer directly in connection with his spare ..., he would recommend spare parts for that particular subsystem, we would make a decision to accept. When I say "we" it was obviously facilitated by the project team but we also drew in expertise from the Navy, we would get specialists from the Navy to participate and help us make those decisions on their behalf, so, and we would slowly go through the process, it was over a number of months in which we would finally commit the full extent of that €26.1 million to spare parts, including onboard spare parts and depot-based spare parts.

ADV LEBALA: Let's quickly run through paragraph 4.5 just to confirm what your mandate was, paragraph 4.5 on page 10:

"My mandate during the negotiation phase was to

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establish a contract baseline in which amongst others the following objectives were to be met”.

Page 11, 4.5.1:

5 “A mutually acceptable set of contractual milestones”.

You keep on talking about contractual milestones, please simplify by way of an example.

MR VERMEULEN: Yes Chair, if I could try and simplify that it’s a number of events and activities that take place during the course of the production phase where costs are allocated to these activities and cost is released, payment is released in accordance with the completion of these milestones and you would agree upfront exactly how these would be accepted. I will elaborate a lot further and I’m sure this will come clearer in the pages to come Chair where I discuss a number of these contractual milestones and I give pertinent examples of it.

ADV LEBALA: 4.5.2 page 11:

“An agreed upon technical specification addressing the entire Submarine Product System”.

20 I think that we know you have qualified that it was part of the supply terms because you guys were technical as the Integrated Project Team, am I right?

MR VERMEULEN: Yes Chair, you’re correct. And this specification, if you recall with the RFO we included a functional, a Navy functional requirement specification. This

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takes it down to a lower level, it's what we call a build-specification in Navy terms where, and you have to have a deeper level of specification because you are going to use the specification to implement tests. This specification will drive
5 out further lower level test specifications for each subsystem onboard that submarine, so you've got to have a good level of detail in the specification and once both parties agree to the specification any change from there on to this specification has to be implemented by means of an engineering change, it's a
10 formal process, so you keep what we call configuration management of that specification during the entire production phase, so if there's any change you've got full traceability to that change and that specification, so it's a very structured
approached.

15 And each, if I could sorry, just to finalise on that engineering change process we mentioned yesterday a Navy project engineer, we would take each of those engineering changes, and there were a number of them and it's normal practice during a project of this magnitude to downstream have
20 certain changes that come about, you might find a piece of equipment that was originally offered becomes obsolete, so you need to change, I'll use the same example again, navigation radar, a newer one comes about, bearing in mind this is a lengthy project.

25 To change that you would have to do an engineering

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change, and what we would do within the project team we'd have all our specialists, we evaluate that changed proposal, we would all, we would discuss that internally and our project engineer would be brought in because it could impact a number of areas and he would preside over that and agree on the change in the specification.

Following that I would have regular meetings with a project steering committee and I would report on those changes to them and I would give them the background to those changes so that they at all times were appraised of the situation of any changes which occur to the contract baseline.

ADV LEBALA: Now I know that you overwhelm us with a lot of technical information but the theme of what you say is that there were activities during this stage, you are doing your best to leverage where you can, you are doing your best to negotiate better for your principals where you can. Of significance you had your cap on with a view to make it a point that you achieve the best for the South African Navy, am I right?

MR VERMEULEN: That was my objective Chair.

ADV LEBALA: Then comes 4.5.3 page 11:

"A detailed master schedule which incorporated all production related activities as well as the inclusion of the integrated logistics deliverables".

I'm certain that the commissioners are realising how important

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this integrated logistic system deliverables are, at one time we wanted to sway you to make you appreciate that in actual fact the performance of the submarine is important, more than the Integrated Logistics Systems deliverables but this keeps on coming back time and again. Are you confirming that without the ILS you wouldn't have done a better negotiation job?

MR VERMEULEN: Yes Chair, the Integrated Logistics Support is very important because as we concluded yesterday the submarine cannot perform without those ILS elements. Could I just say in this regard the significance here and the word "integrated" is important because it's got to be integrated with the whole production process, so we would have a master schedule which identifies all the production activities and you would have to have the integrated logistics support elements delivered at appropriate times throughout that process.

In other words as an example one of the ILS elements would include technical manuals, we would make sure those manuals were delivered at the right time before training took place, so there has to be a logical sequence in your production schedule to make sure that each deliverable is delivered as and when it is required and that's where term "integrated" is emphasised.

ADV LEBALA: Yes, I would like you to simplify it. You say that for instance an example that you give of the integrated logistics system is a technical manual that relates to the

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training before training takes place. Just simplify it in this context.

MR VERMEULEN: Yes Chair. The technical manuals do form an important facet for training, you base your training on the technical manuals, however, obviously the technical manuals play another important role. Those manuals stay with the submarine during the course of its life cycle, technicians will use those manuals to effect repairs on equipment post-delivery, so the manuals are a very important ILS deliverable.

5
10 ADV LEBALA: Just draw a correlation between training, the manual and the Integrated Logistics Systems.

MR VERMEULEN: Sorry Chair, could you repeat that?

ADV LEBALA: You talk of the training manual and then the technical manual and then you talk about training, I understand it. And then you talk about before training takes place. Now I would like you to show the connection between the technical manual, the training and the Integrated Logistics Systems. Remember you are trying to show the Commission the following, that the submarine, it's not only performance, it's delivered or it's in the process of being delivered, it has to take a voyage, it has to go and do exercises. Now how does the integrated logistics system play a role at that stage when it's delivered in relation to the technical manual and training?

15
20
25 MR VERMEULEN: Yes Chair, the relationship between those two elements which are both ILS elements is the sequence

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would be as follows; the contractor would deliver a full set of draft manuals and not the completed version, and this is why the sequence is so important. We would then effect the training programme, all the training courses would take place and the candidates that were receiving the training would utilise those draft manuals. There were two reasons for that, we obviously, there would be mistakes in those manuals. Remember, these manuals have been drawn up by non-English speaking personnel, these are the German Submarine Consortium, so we had used the candidates in two ways and these are obviously all Navy personnel, they would help us improve those manuals and at the same time they would learn from those manuals.

So, we had a space of time where the draft manuals would be delivered, the training would be effected, we would then instruct all those candidates receiving training to mark up any mistakes or inconsistencies or errors they find, we'd feed these back to the shipyard and they would then produce a final version of technical mandates, so the two are very interlinked. Following the training of course those ticking the manuals play another important role in that they provide the backbone for maintenance, all the maintenance information would be contained in those manuals.

ADV LEBALA: Can I simplify it further by saying it's the training of the following, the technicians who will be in the

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submarine, the electricians who will be in the submarine, the crew who is in the submarine, the mechanic crew in the submarine, am I right?

MR VERMEULEN: That would be one element. Another
5 element in terms of maintenance which is more important is the shore-based personnel. Staff onboard the submarine would provide a high level of maintenance, however, the more detailed a diagnostic related maintenance would be done when
10 the submarine is alongside, in other words in the workshops, so the manuals have to provide that level of technical detail as well, so you have operator maintainer training for the onboard personnel and you have shore-based maintainer training, which is a far greater level of depth.

ADV LEBALA: Thank you. In actual fact Admiral
15 Schoultz, the commander of the Naval Base in Simonstown explained that part to us so well about the training that goes in, the courses that are being given. Of course those are typical examples that make these submarines function, it's not only the performance I mean, the submarine must function and
20 you correlate that with the spare parts and that's what makes the submarine to turn around.

MR VERMEULEN: Correct Chair.

ADV LEBALA: Thank you. 4.5:

"A Supply Terms Agreement".

25 You've explained that, let's get going now. 4.6:

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“A strategy was implemented so as to bolster the initial German Submarine Consortium offer”.

You explained what you did during the negotiations, how you made it a point that the spare parts are increased, I mean it has become clear that the German Submarine Consortium was not strong at the Integrated Logistics Systems. Of significance is what you say in paragraph 4.6.2 where you say:

“Concentrate on improving the ILS, emphasising its importance as opposed to enhancing the functional performance. The outcome of this strategy resulted in the scope and supply being extended without any resulting overall price increase”.

Now the question of costs was significant during the negotiations, am I right?

MR VERMEULEN: Yes and no Chair, what we did was we didn't try and negotiate the price down with the German Submarine Consortium, the price had been accepted by Cabinet and what we did instead of trying to negotiate that price down, we tried to pack as much into that price as possible, that was the approach we followed. Cabinet was satisfied with the overall price and we worked and we got, if I can put it crudely, an expression we used is we got as much bang for our bucks as possible.

ADV LEBALA: Of course you also had to make it a point that the price didn't increase, am I right?

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MR VERMEULEN: Correct Chair, I had to work within the ceiling price of the price indicated by Cabinet.

ADV LEBALA: Now demonstrate to the Commission the ambidexterity of your negotiation skills, what you did. Let's go
5 to the slides just to shed light to the Commission what you have achieved during the negotiation items that form part of the ILS that benefited the South African Navy. You may take the commissioners directly to the slide and project it but they have copies, I think we are looking at pages 10, 11, 12 and 13.
10 Just explain to them what is the significance of this diagram in relation to the negotiations.

MR VERMEULEN: Yes Chair. Chair all the elements, as I said to you our strategy was to bolster, to improve the offered integrated logistics support package and you will see that
15 these examples that I'm going to show you are all with respect to integrated logistics support. If you recall I mentioned integrated logistic support includes training, that would also include training equipment and expensive simulators as well. What you see in front of you here is a Containerised Combat
20 Information Centre Simulator.

Essentially what this piece of equipment does, and the second slide shows the inside of that container, what this container does is you place it alongside a submarine that's in harbour, you connect it to the submarine and the operators
25 onboard the submarine have got consoles and you would

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generate scenarios using this, by scenarios I mean activities which would test the proficiency of the onboard submariners without having to take them to sea, so a simulator, although it's an expensive piece of equipment initially it proves, it becomes very cost effective over time because it allows you to train personnel under realistic conditions without actually having to be in the operating environment which obviously is costly.

So that's what this sets out to do, it essentially trains the sonar operators, and while training the onboard operators you also have youngsters receiving training here because what they are observing on these large flat panel displays is the response from the sonar operators onboard the submarine. You will have an instructor here which will, and he will explain the scenario being used and the individuals here, these candidates will see exactly how the operators onboard are reacting to those tasks, so that's the one simulator.

Another simulator which we negotiated, and if you could bear in mind that these items were not initially included in the scope of supply of the GSC, this is a Diving Simulator or Platform Simulator, it's got three degrees of movement, it essentially is there to train, if I can call it the drivers of the submarine, the helmsmen and the plainsmen, the individuals, the personnel who are responsible to keeping that, the submarine stable. So, here again you would put all sorts of,

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and these, the people inside this simulator actually have to be strapped in, it gets pretty hectic inside there.

The submarine again, you put it through very difficult scenarios, you simulate emergency situations where you will suddenly lose ballast of a submarine and these trainees, you put them under stressful conditions and they have to keep that submarine stable and they get tested on this and this is part of their ongoing training, this is post-delivery training which takes place after the submarines and this equipment is delivered. This equipment for instance is located in the Naval Base at Simonstown at the Submarine School.

So that was negotiated in as well, and a lot of effort had to go into those scenarios that go into this because they had to simulate our sea conditions and they also had to simulate the Type 209 submarine's reactions to those conditions.

What I'm showing here Chair is a Fifth-Scale Model, it's a 20% sized model of the submarine, it's a replication of that submarine and it indicates every pipe, every cable, you can see the level of detail hopefully in this slide. Now this is one section, there were five sections of this, you can appreciate the number of man hours, this is a plastic model, that would go into replicating each piece of equipment onboard this, inside this model.

Just some background regarding this model, the

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Germans would have had to produce this model because they use it as a production tool. The negotiation was such that we convinced the Germans that following the build of the submarine they would have no use for this model, so we negotiated that they include it, that they agree to give us this model, so we, that was included in the scope of supply and it's a very useful training tool in Simonstown because you can take a young trainee who is unfamiliar with the submarine and this could be one of his first steps to learning the intricacies and the equipment layout of the submarine, so it was a very useful piece of equipment and notwithstanding the fact that it was not included in the original scope of supply we nevertheless also negotiated that it would have to undergo a qualification, we qualified this product, we made sure that it replicated the submarine in its entirety, so that was also included.

Okay, that's as far as what we managed to achieve. There were other items we managed to achieve in the negotiation phase as well but these were the significant ones Chair.

ADV LEBALA: We are now gravitating towards the product. We know the following; you did not affect the contract price, Cabinet gave a mandate that we'll not spend more than, how much, R4.-what-what-what billion, you were doing your best to stay within that line, you were trying your best not to make it a point that it is increased, you were not trying to

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shortchange the Germans, you are achieving simulators, there's a scale model section which was not part of the initial original scope, you managed to achieve all this during negotiations.

MR VERMEULEN: That's correct Chair.

5 ADV LEBALA: Page 14 paragraph 4.7:

"Following the conclusion of the negotiation phase which culminated with the establishment of the contract baseline the contract pertaining to the acquisition of the three submarines was initialed on 10 12 June 1999. The parties who initialed the contract were members of the IONT and the preferred supplier".

Why were you not allowed to initial because you were part of the negotiation team? I know that your focus was supply terms, the International Offers Negotiating Team was the umbrella agreement, why were you not allowed?

MR VERMEULEN: Chair the contract was negotiated, the formalising of the contract was negotiated at higher level. I did initial the actual pages in the Supply Terms Agreement.

20 ADV LEBALA: What does "initial" mean in this context?

MR VERMEULEN: In this context it is acknowledging the content of each page within the document.

ADV LEBALA: 4.8, this is very critical, you will appreciate that when we go to the other Terms of Reference 25 you might not be here, it's going to come up time and again:

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“The contract was formally signed on the 3rd December 1999 between the Government of the Republic of South Africa and the German Submarine Consortium for the acquisition of three Class 209 Type 1400 MoD submarines”.

Were you present when the contract was signed?

MR VERMEULEN: No Chair, I wasn't present. I heard the news on the same day though.

ADV LEBALA: Are you alive as to who signed the contract on behalf of the Government of South Africa?

MR VERMEULEN: I believe the contract was signed by the Minister of Defence.

ADV LEBALA: Do you know who was the Minister then?

MR VERMEULEN: Mr Joe Modise.

ADV LEBALA: Let's go to the production phase. In actual fact it might refresh you, I think literature and the documentation informs us that it's Minister Lekota who signed it. Nothing turns around it at this stage, please do not agonise.

MR VERMEULEN: Thank you for that correction Chair.

ADV LEBALA: Now we go to the production phase. Now the submarine has to be produced. Now negotiations are done, we scored, everything starts to fit in a jigsaw puzzle. 5.1, that's the process:

“Certain members of the IPT including the project

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officer ...”.

That includes yourself:

5 *“... and the ARMSCOR programme manager were
deployed to Germany and based at the two German
Submarine Consortium shipyards situated in Kiel
and Emden for the duration of the production
phase”.*

That’s very clear. 5.2:

10 *“During the production phase and in accordance
with established contract (indistinct) baseline ...”.*

Are you talking about the contract baseline that you negotiated,
am I right?

MR VERMEULEN: Correct Chair.

15 ADV LEBALA: Those are the terms, the contract and the
control that you want to regulate.

MR VERMEULEN: Yes, as per those documents that I
explained earlier on which make up that baseline.

20 ADV LEBALA: *“The three submarines were constructed
and onboard equipment was installed, integrated
and set to work”.*

That’s very clear. 5.3 page 15. Now your ability to play a
significant role comes again here:

25 *“During and after each respective submarine’s
production factory acceptance tests onboard setting
to work, harbour acceptance tests and sea*

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acceptance trials were conducted in accordance with the approved test specification”.

Let's pause there. Was this part of what was included in the contract baseline?

5 MR VERMEULEN: Chair, you will notice in the previous paragraph I mentioned contract baseline/product baseline. We take it a step further, during the negotiation phase we arrived at a build-specification, a detailed product specification. That document had to contain enough information for us to take it a
10 step further during the production and drive our test specifications, so following the deployment to Germany, commence with the process of drawing up low level, at subsystem level test specifications for acceptance test procedures, in other words each subsystem would have to be
15 qualified against a test specification and contract payments are, form a part of that as we'll see later on.

So, in other words ... Perhaps if I could just explain, you would have a contract baseline for the completion of harbour acceptance tests for the first submarine, you would
20 measure that against the test specification, you would have to have something concrete to accept that the contractor has fulfilled his obligations and that would be the basis for that and you would both agree upfront this was the manner in which each piece of equipment would be tested and qualified before
25 actually initiating that process.

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ADV LEBALA: Now let's recapitulate and simplify the Commission, we know that the submarine is being produced now, probably is it at Kiel or Hamburg, it's in that area where they are constructing it. At what stage are we talking about
5 the factory acceptance test and what is it, is it when it's at the factory, is it when they take it out of the factory, they put it in the ocean?

MR VERMEULEN: Chair, as soon as the contract was placed with the GSC they would in turn place subcontracts on the
10 equipment manufacturers of all the equipment that they don't produce, all the electronic equipment they place a subcontract on that. In some cases the factory acceptance test took place in South Africa. For instance the external communications system onboard the submarine was manufactured in South
15 Africa, so we would have part of our project team, as I mentioned earlier on, not all the project team relocated to Germany, some would remain here in order to effect those factory acceptance tests at the local industries facilities before those items were shipped to Germany for integration.

20 And then of course a number of where the German or other foreign suppliers provided equipment factory acceptance tests would be executed at those premises before delivery to the shipyard, if that makes it clear.

ADV LEBALA: "Onboard setting to work", simplify it, give
25 an example.

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MR VERMEULEN: Yes Chair. Once the individual equipment had been factory tested they would be delivered to the shipyard, they would be integrated into the submarine and so that's what onboard setting to work, and they would be set to work, in other words they would have to be compatible with one another, they couldn't interfere with one another, they'd have to function and function correctly.

ADV LEBALA: At this stage is the submarine at the harbour or is it still in the factory?

MR VERMEULEN: At this stage the submarine would have been constructed in order to accommodate those equipment, so you would have the cables would be installed, your ventilation, the submarine would be fitted out at that stage or in the process of being fitted out. In some cases it would be a sequential thing. The seven areas of the submarine where you don't have equipment installed, that would carry on. In other areas where compartments were finished you could install equipment and do factory acceptance tests, that's why a master schedule, a production schedule is crucial because once the process starts you have to order your lengthy deliverable items, all has to fit in with the production schedule so that you can meet the timescales, it's quite an intricate procedure and that's why you need a very experienced shipyard to work with in this regard.

ADV LEBALA: Thanks for the additional information. At

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this stage when we do the onboard setting to work, is it at the factory or is it at the harbour?

MR VERMEULEN: It's at the harbour onboard the submarine Chair.

5 ADV LEBALA: Thank you. The harbour acceptance test is obviously at the harbour?

MR VERMEULEN: Yes, that's just the next stage. Basically the equipment gets installed and sent to work and then you do formal qualifications in accordance with the test specification,
10 you will do a harbour test, you will make sure that equipment functions within its operating environment onboard the submarine.

ADV LEBALA: And sea acceptance trials, it's on a voyage now, it's in the thick of the ocean.

15 MR VERMEULEN: These are the final acceptance tests you do where the submarine actually goes to sea and in this case it's a very expensive exercise for the shipyard, it's included in the price. The submarines were produced in Kiel which is in the Baltic Sea, it's very shallow, the submarines plus an escort
20 vessel had to transit into deep water off Norway and what's called the Skagerrak Sea, to obtain the required depth to dive the submarine and carry out the sea acceptance tests. There were a total of 41 sea acceptance tests for the first submarine and 40 respectively for each of the following submarines.
25 These were carried out by a team of people from the shipyard,

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bearing in mind the submarine still belonged to the shipyard.

We did include project team members and we also managed to include Navy people as well, bearing in mind a submarine is very constrained in size, it can only take typically
5 a maximum 45 people, it's designed for a crew of 30, it can carry 15 passengers.

ADV LEBALA: Now at this stage we do know the names of the submarine, by the way the first submarine was Manthatisi, am I right?

10 MR VERMEULEN: SAS Manthatisi was the first submarine.

ADV LEBALA: Is it the one that did 41 sea trial tests, or is it 41 all-inclusive of Manthatisi, Charlotte Maxeke and Queen Modjadji?

15 MR VERMEULEN: No, that refers purely to Manthatisi. Charlotte Maxeke had had 40 sea trials and Queen Modjadji had 40 sea trials as well.

ADV LEBALA: Now who pays this cost of the sea trials or were they negotiated during the contract baseline or is it your acumen as you keep on negotiating who managed to squeeze
20 these 41 sea trials, I can imagine, is it the limited number that has to be done of the sea trials?

MR VERMEULEN: Chair, to answer your first question it's included in the price of the submarine. What we did during the negotiations, it was quite a tough negotiation, what the GSC
25 wanted to do was provide us with a total of 41 sea days for

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5 trials. Sorry, let me reword that. There were a total of 41 trial events, they wanted to do it over a specific period and they tried to invoke the following condition that should the environmental conditions or sea conditions prevent those trials from taking place they would be written off because they had a production schedule to keep to, it's a fair argument.

10 We insisted that irrespective of the weather conditions we wanted those 41 trials done, they had to be completed and it turned out that it resulted in some delays, often the submarine would have to go back to harbour because there were incremental weather conditions, we couldn't carry out certain exercises, but they relented and they provided us with that. So, we completed the full scope of sea trials for each respective submarine.

15 ADV LEBALA: I think the rest becomes what we can read without asking you questions. Page 15 paragraph 5.3, the last from line number 4:

20 *"The extent of these acceptance tests, all of which required individual test specifications and were witnessed by the Integrated Project Team appointed personnel were quantified as follows:*

- *240 Individual factory acceptance tests were conducted per submarine.*
 - *126 Individual harbour acceptance tests were conducted per submarine, and;*
- 25

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- *46 Sea acceptance trials were conducted for the first submarines and 45 sea acceptance tests for the remaining two submarines”.*

Is it 45, 45 or 45 for both?

5 MR VERMEULEN: Chair, I've actually made an error previously, I said 41, it was 46 sea trials for the lead submarine SAS Manthatisi and 45 per submarine for the next two submarines.

ADV LEBALA: 5.4:

10 *“A total of 71 engineering changes were approved during the course of the production phase. Each of these engineering changes had to be evaluated by various specialists within the IPT and approved by the appointed IPT and Navy project engineer. All*
15 *affected technical documents such as drawings, manuals, specifications had to be revised so as to ensure that the As-Built Data Pack was all times aligned to the product system configuration”.*

What is As-Built Data Pack? The theme there speaks for itself
20 what was achieved even during negotiations, additional things but what is an As-Built Data Pack?

MR VERMEULEN: Chair, the procedure is you have a product specification prior to the commencement of the production phase. During the course of the production phase a number of
25 drawings have to be compiled, detailed technical drawings,

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interface control documents, all the manufacturing related details of that submarine and those drawings get compiled into what we call an As-Built Data Pack and you have an As-Built Data Pack for each respective submarine.

5 Chair, if I could just elaborate on the tests if I may? I've mentioned in my statement that the Integrated Project Team witnessed all the tests but we had further support as well. ARMSCOR Quality Division had negotiated a cooperative agreement with the equivalent NATO ARMSCOR Organisation
10 known as BWB. This organisation also assisted us with the acceptance of factory and harbour acceptance tests. It's just something to bear in mind, we didn't just rely on the expertise within our project team and within the Navy, we solicited additional help as well.

15 ADV LEBALA: Who carried those costs?

MR VERMEULEN: ARMSCOR negotiated a cooperative agreement with the BWB which is a NATO-based organisation in which they did not charge us for man hours. We had to pay a cost for the use of facilities at times but they provide us with a
20 very fair arrangement which we made the most of, so it didn't in fact cost us that much extra.

ADV LEBALA: To be specific did it affect the Cabinet price?

MR VERMEULEN: No it didn't, it was in the framework of the
25 costing.

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ADV LEBALA: 5.5 the ILS comes back again:

“In parallel with the production of the three submarines all Integrated Logistics Systems deliverables had to be reviewed and accepted. This included, but were not limited to the following; ...”.

5

You’ve addressed some of them.

“5.5.1 The reveal of the full set of draft and final version technical manuals.

5.5.2 Participation with the spare part selection process.

10

5.5.3 Acceptance of training course curricula and overseeing of training courses to the extent as follows; ...”.

15

That’s clear, that’s clear. Page 17, do you want to take the Commission to the slide that is reflected on page 17 and please address it.

20

MR VERMEULEN: Certainly Chair. In the previous page we provide an indication of the training, the scope of training that this contract included. It was a huge training effort which occurred throughout the production phase. Again this falls within the ILS, within the ILS element, this was merely to show one of the many training courses that was conducted where we see a crew member undergoing emergency escape training in Germany. There was a huge effort placed into the training of Navy personnel and ARMSCOR personnel under this contract

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Chair.

ADV LEBALA: By the way, as at that stage were you alive to as to how many countries were using the German Submarine Consortium submarines?

5 MR VERMEULEN: Yes Chair, it's an impressive number. There are approximately 40 countries apart from South Africa that make use of various versions of the Type 209 submarine. It's one of the world's most successful export submarines ever produced.

10 ADV LEBALA: As at that stage were you alive to the number of countries that used the Italian submarines who were the competitors of the German Submarine Consortium?

MR VERMEULEN: Chair, to the best of my knowledge it was only the Italian Navy that used their submarines, but I stand to
15 be corrected.

ADV LEBALA: As at that stage were you aware of the number of countries that used the Swede's submarines that was the competitor of the German Submarine Consortium during the bidding process?

20 MR VERMEULEN: Chair I know obviously the Swedish Navy used that submarine and there was a variant, it was a big variant submarine that was produced for the Australian Navy as well, but it wasn't the same submarine that we would have obtained, it was a much larger submarine.

25 ADV LEBALA: Now are you saying as at that stage there

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were other countries that were using the Swede's submarine?

MR VERMEULEN: The particular submarine the T192 that was offered to South Africa I don't, I'm not aware of any other country that uses that specific submarine.

5 ADV LEBALA: We know historically we used the French submarines and the French were the competitors with the German Submarine Consortium. As at that stage were you alive to the number of countries that were using the French submarine?

10 MR VERMEULEN: Yes Chair, the Scorpene submarine that was offered in the bid was a new submarine. We did know that Chile was about to place an order for that submarine but it was a new submarine, they were the first client to ever use that Scorpion submarine. Subsequently now at this stage it has
15 been sold to other countries as well.

ADV LEBALA: Now are you saying ... I see that it's time for lunch. This is my last question before we break for lunch, we are left with two pages and then you go to DIP if need be, you promised the Commission that you will talk to DIP, you
20 could talk about the damages to demonstrate, if need be, how you negotiated better for those who were not keeping time introducing this product, how you dealt with them and how you infused it in the contract baseline, and then you can talk about the Auditor-General's finding and then we conclude. But before
25 we part ways for lunch ... My train of thought is gone, I'm not

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on the right track. I will address this question after our adjournment, lunch adjournment Chair, it's 13h00, I take it this is an appropriate time for adjournment.

CHAIRPERSON: We'll adjourn.

5 ADV LEBALA: Thank you.

(Commission adjourns)

(Commission resumes)

NOTE: Witness confirmed to be still under oath.

CHAIRPERSON: Thank you.

10 ADV LEBALA: Thank you Chair, Commissioner Musi. We are on page 17 of your statement, paragraph 5.6:

“Throughout the production phase the Integrated Project Team and the German Submarine Consortium Team members participated in regular progress and technical meetings”.

15

Was this part of the contract baseline that was negotiated from the onset?

MR VERMEULEN: Yes, it was Chair. If you recall I referred to an engineering management plan which formed part of the RFO Response and that specifies or details the necessity for holding regular progress meetings with the prime contractor.

20

ADV LEBALA: So members of the Integrated Project Team were hands-on throughout the production phase?

MR VERMEULEN: Yes, they were Chair.

25 ADV LEBALA: 5.7:

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*“The Integrated Project Team’s project executive,
the project officer and programme manager ...”.*

We’ve heard about the project executive:

5 *“... was also required to report on a quarterly basis
to an established maritime project steering
committee”.*

What is that?

MR VERMEULEN: Chair, Maritime Project Steering
Committee is established, it’s co-chaired by the ARMSCOR
10 senior manager for Naval Systems in the case of Navy projects
and it’s also co-chaired by Director Naval Acquisition and it’s
essentially a report-back on the progress of the projects. I
mentioned earlier on if there were any engineering changes, if
there are any risks that we identified, progress of milestones,
15 that sort of level of detail, we’re reporting back. We’d have to
prepare a quarterly report and we’d present against that
quarterly report on a three-monthly basis.

ADV LEBALA: Let’s look further at the role played by the
project executive.

20 *“Apart from reporting on detailed milestone
progress ...”.*

Which you have explained and simplified:

*“... the project executive was also required to report
on aspects such as project risks and the abatement
25 thereof as well as engineering changes”.*

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You explained engineering changes. What is project risks?

MR VERMEULEN: Chair, an important facet that we follow during the acquisition process is the management of risks, a lot of importance is attached to that, to the effect that the programme manager has to compile each project a risk management plan. It's equitable to a non-negotiable mandatory document. Whenever risk is identified we have a kind of an approach towards the abatement of that risk, there were a number of risks that were identified during the course of the project and we had to explain the means by which we were going to contain and alleviate those risks, and that would be ongoing throughout the project. It's one of the standing agenda items to the Steering Committee being these risks.

ADV LEBALA: Well, you've explained abatement in that context. The Maritime Project Steering Committee was jointly chaired by the Director Naval Acquisition and Senior Manager ARMSCOR Naval Systems Division. Were the representatives of the German Submarine Consortium not represented at that forum?

MR VERMEULEN: No Chair they weren't, we had a separate programme management review with the contractor, also on a three-monthly basis, and shortly thereafter we would time our Project Steering Committee meetings with DAPD and with ARMSCOR, so to answer your question it was an internal meeting that involved the Navy and ARMSCOR representatives.

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ADV LEBALA: Now we are addressing the milestones. In the context in which you talked about milestones and in this context in paragraph 5.8 page 18 of your sworn statements what are you referring to when you talk about milestones?

5 MR VERMEULEN: Chair, a milestone, it's a contract payment point, it's a hold-point if you like, it can address a deliverable, for instance if you mentioned technical manuals, if the technical manuals had been completed and accepted we would, there would be a certain amount attached to that, financial
10 amount. It could also entail an event, it wouldn't necessarily have to be a deliverable, for instance you will see one I've got for keel laying that's not a deliverable as such, it's an event that happens during the production phase, and we would have a specific way of going about accepting those milestones and
15 we'd agree upfront on how we were going to accept them, and we would in the project team, we'd involve the following process, we'd get the contractor to draw up a certificate of conformance which he would have to sign and his project engineer would have to sign, then it gets submitted to myself.

20 I would make sure, depending on the nature of the nature of the milestone, for instance if it's a harbour acceptance test we would make sure there are specialists involved with those harbour acceptance tests, sign that certificate of conformance, we would always make sure our
25 quality assurance representative who was permanently

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allocated to our project signed and stamped that, and what he would do is he would check all the documentation associated with that milestone as well as (indistinct) the completeness of the milestone from a quality point of view.

5 **NOTE: Note that the witness is not speaking into the microphone.**

MR VERMEULEN: And then lastly the programme manager and the project officer would sign that milestone off and we would then submit that to ARMSCOR Finance Division for the
10 release of payment for that specific milestone.

ADV LEBALA: Now appreciating that the milestones are inclusive of contract payment, address the deliverables, address the events. Were there instances when you had challenge with the way the German Submarine Consortium
15 addressed payment?

MR VERMEULEN: Addressed payment or completion of the milestones Chair?

ADV LEBALA: Milestones are inclusive of the following, contract payments as an example, deliverable as an example
20 and events. Now were there, I'm breaking those three down, were there instances when the German Submarine Consortium had a problem in addressing contract payments?

MR VERMEULEN: Sorry for that Chair. Yes, yes, there were some instances where the German Submarine Consortium failed
25 to meet the deadline for the completion of the milestone and

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our contract made provision for that. We had to work to a strict production schedule as I explained and you have to finish certain things in time otherwise there would be consequences, so we had a clause in our supply terms contract which made provision for late delivery and this involved liquidated damages or penalties and where necessary we invoke that and there is a calculation which works on the basis of for every day a milestone is late you would, there would be a calculation against that specific value for that milestone and that would be deduced from payment to the contractor and we had to invoke that on certain occasions.

ADV LEBALA: Now other than demonstrating that the Integrated Project Team, including yourself, were very prudent in the negotiation process and accountability leading to the production of the product system, the submarine, we note that there were also liquidated penalties and damages that arose because the German submarine company was not sticking to the strict production schedule.

MR VERMEULEN: Correct Chair.

ADV LEBALA: No you referred to page 85 of the indexed and paginated papers, your statement page 85, it's Annexure "RMV5" Commissioner Musi, Chairperson, page 85. I would like, I would like you to quickly take the Commission through this document, let's identify whether the Commissioners are on the same page. The commissioners are on the same page.

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Please identify this document.

MR VERMEULEN: Yes Chair, this specific Annexure "RMV5" refers to the status of liquidated damages or penalties that occurred during the course of the production phase of the project.

5

ADV LEBALA: Now explain it to the commissioners as to in relation to what in as far as the production of these submarines was it?

MR VERMEULEN: Yes Chair, in what you see in front of you actually involved three penalties for each of the respective submarines coincidentally. In the first one S101, that's the first, the lead submarine penalties ...

10

ADV LEBALA: Is that Manthatisi?

MR VERMEULEN: Correct Chair, it was subsequently, once it was commissioned it was named SAS Manthatisi.

15

ADV LEBALA: So let's start naming them, S101 would be Manthatisi, S102 would be Charlotte Maxeke, S103 would be Queen Modjadji, am I right?

MR VERMEULEN: Yes, you are right Chair.

20

ADV LEBALA: You may proceed.

MR VERMEULEN: With respect to SAS Manthatisi penalties had to be levied because the contractor failed to complete his harbour acceptance tests and his sea acceptance tests on time, so based on the formula contained within the Supply Terms Agreement this resulted in a penalty of €66 030.00 because

25

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those milestones were not completed on time.

ADV LEBALA: Now you say the contractor failed to complete the harbour acceptance tests and sea acceptance tests, who are you referring to?

5 MR VERMEULEN: The German Submarine Consortium.

ADV LEBALA: And the penalty was €66 030.00, is that correct?

MR VERMEULEN: Correct, for that specific non-completion date.

10 ADV LEBALA: Now I see below there's "EDC 60 months with grace period". Would you like to explain that?

MR VERMEULEN: Yes Chair. Basically what EDC stands for is effective date of contract, in other words once the contract is signed the clock starts ticking in terms of the production phase, so in this case these milestones had to be furnished within 60 months after the effective date of contract. The grace period, what that refers to is, just taking you back to the negotiation phase, the German Submarine Consortium was very averse to us including these contractual payment milestones as I explained, they wanted annual draw-downs that happened automatically.

We explained to them that that is not how we do business, we enforce contractual payment milestones as a measure of controlling production phase and they eventually relented and they agreed that we include contractual payment

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milestones. The compromise here was the grace period, they said they can't at that stage assure, be assured of completing that specific milestone within 60 months, so they said they will agree to us including the contractual milestones provided we
5 just at least allow a grace period and eventually through my legal services we negotiated that we made a compromise. We felt that we had done pretty well, we had forced them to accept the contractual milestones which was a breakthrough for us.

ADV LEBALA: I understand the effective date of contract,
10 I understand the grace period, just simplify it, what is the difference in your thinking in as far as payment is concerned, let me understand. The Germans wanted to, you to pay after the completion of the whole contract or within a month, irrespective you wanted to pay monthly or you wanted to pay
15 daily, please simplify it.

MR VERMEULEN: Certainly Chair. Chair, what the Germans wanted, and it's quite obvious why because they are also concerned about alleviating risks from their side, this is obviously both parties had interests. What they wanted was to
20 have automatic draw-downs or automatic annual payments delivered to them, irrespective of their progress, so at a given date, 12 monthly-period they requested that payment would go automatically through to them based on the financial restriction allocated for that particular year. We had a different approach
25 to that, we said no, we don't, it's not necessarily a monthly or

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a yearly payment, we pay on the basis of completion of milestones. In this particular case these milestones had to be finished 60 months after, in other words five years after the effective date of contract.

5 ADV LEBALA: I think that has been clarified. Now if you convert €66 000-odd, how much is it in Rand?

MR VERMEULEN: At that exchange, I think we had a base rate in the contract of 6.4, so you would have to multiply the €66 000 by 6.4, that was the rate of exchange that was fixed
10 for this contract at that time.

ADV LEBALA: I beg your pardon Chairperson, Commissioner Musi. How many years did it take in terms of the milestone contract to complete one submarine?

MR VERMEULEN: It was five years per submarine, so this,
15 these two milestones HATS would have shortly after that, the first submarine would have been completed, and likewise with the SATS, they didn't all run concurrently, you had the first submarine starting, then the second and then the third in a staggered approach. So it was a total of 84 months for the
20 entire three submarines to be produced and qualified.

ADV LEBALA: Yes, the Naval officers did explain that. By the way did you mention how much are we talking in conversion of €66 000?

MR VERMEULEN: Yes Chair, the rate of exchange was 6.4,
25 so you would have to multiply that €66 000 by 6.4 and you will

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have the Rand equivalent at that stage.

ADV LEBALA: Now let's look at the second submarine, the penalties. Before you even go there was this amount paid by the contractor?

5 MR VERMEULEN: Chair, how it works is they would submit an invoice for the full amount and we would deduct the €66 000 from payment.

ADV LEBALA: So, in other words it was expiated or paid, one way or the other it was compensated?

10 MR VERMEULEN: Precisely Chair.

ADV LEBALA: Now let's look at the next submarine Charlotte Maxeke, the penalties.

MR VERMEULEN: Yes Chair it was a similar case here, there was a milestone for the integration of the first data link system, you will see there it's sub-milestone 11.3. We have an elaborate milestone plan which indicates all the milestones and the payment amounts for each milestone. In this case the milestone amount was €514 000 and the penalty amounts to €47 399, and likewise here it was the same rate of exchange.

20 ADV LEBALA: So the penalty was a percentage of the total milestone amount?

MR VERMEULEN: Correct Chair. How it works is every day that the item has been delayed penalties are calculated on a daily basis.

25 ADV LEBALA: Was it a consistent percentage?

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MR VERMEULEN: Yes, it's a consistent formula applied to any late delivery.

ADV LEBALA: Now as a data link system we know that the first penalty in as far as Manthatisi is concerned, it was in
5 relation to the completion of the harbour acceptance tests and the sea acceptance tests and what about the data link system, what is it?

MR VERMEULEN: Yes Chair, we had milestones at various levels. The first two on SAS Manthatisi were fairly high level
10 milestones, you will see they address the entire harbour acceptance tests. Then we had low level milestones as well, for instance this is a particular subsystem that's installed onboard the submarine, the contract was battling at this stage to integrate that subsystems successfully, so we held back
15 payment until we could successfully do a qualification of this system onboard the submarine. Once it had met all the requirements as contained in the test specification we could release for payment.

ADV LEBALA: The third penalty, is it a low level or a
20 high level?

MR VERMEULEN: Chair, these are also high level and this included the harbour acceptance test and sea acceptance test onboard Queen Modjadji.

ADV LEBALA: Thank you. Let's go back to page 18. It's
25 becoming manifest and palpably clear that there was

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accountability, the Integrated Team was on top of the game, you did your best, you negotiated, you expected accountability, no one was going to take this process for granted, it's very clear to the Commissioners. 5.8:

5 *"There were a 117 payment milestones ..."*.

Now we are going to payment because we know that milestones could be payment, they could be non-payment, they could be contract payment, they could be deliverables, they could be events, now we are addressing payments, and numerous non-
10 payment milestones which were required to be successfully completed during the production phase.

"Major milestone event completion dates are listed in the table".

Let's start with S101 Manthatisi. What is keel laying? Now
15 let's understand, there's a detailed design completion, we are talking about S101 the first submarine Manthatisi, there is a date July 2002. Explain the column "Detailed Design Completion" and the date July 2002.

MR VERMEULEN: Yes Chair. Chair, if I could just take you
20 back to the completion of the negotiation phase you arrive at a contract baseline. An order is placed, a contract is placed, you don't go into full scale production immediately, there's a period where you do a detailed design. There are a number of reasons for this, although it's s mature submarine you must
25 bear in mind this submarine had never fitted South African

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systems on board it before, so that integration, that aspect of the design has to be done, so there were some customisation of the submarine in terms of the Navy specific requirements, there were some changes for instance to accommodation, some minor configuration changes, all of those which are brought out during the production phase and captured in the production specification. The detailed design drawings around those specific changes has to be completed and it's a matter of interest this detailed design completion culminated with the construction of that Fifth-Scale Model, because the Fifth-Scale Model is a very good indication of the fact that that submarine has now been designed in detail related to the submarine, the South African Navy application.

You will notice though that the production does not have to commence at that stage otherwise you won't meet the overall timescales, so you will see in the next milestone which is called keel laying, and I'll explain what that's all about now, you will see that date was May 2001, so you don't have to wait until the full detailed design is done because the contractor has to order what we call long-lead items, there's certain items like the main motor, the electric motor of the submarine which can take 24 months to acquire.

That propeller that you see in the picture takes a full 18 months because what, he's faced with a dilemma, he goes to his suppliers and he'll place an order for a propeller,

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they are also dealing with other customers, essentially he has to get in the queue in some cases, so he has to in his planning, in his production planning he has to factor in all those long-lead items, all those lengthy delivery, he has to build that in, 5 so you allow him to buy, it's obviously not going to be impacted by the detailed design, those are standard items that he always uses, so he'll order those pretty quickly.

The keel laying which I mentioned, it's an old nautical term which was used when older ships were originally 10 acquired. Keel laying in this case specifies the cutting of steel, it's a major milestone event, it's when steel starts being cut for the first submarine, so that was a milestone at that stage. The one you will see it's HATS completion and we've discussed harbour acceptance tests, and just please bear in 15 mind that this is an extraction, I didn't put every milestone in, I just wanted to give the Commission an idea of what milestone, the philosophy behind the milestones for all of that. So these are the significant ones. SATS I think I've dealt with.

The contractual handover, after we did SATS we had 20 a very elaborate checklist, you would sit down with the contractor for about three days where we had apart from evaluating the sea trial results and the harbour trial results and the FATS, there were a number of other documents, you had to have to have a seaworthy certificate, has the contractor 25 given you all the keys that are used in the submarine, it was a

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very detailed, lengthy list that we would go through the contractual handover.

So that, once that had been finished, and we also got all the IPT members and the various disciplines to sign those off as well, once that had been completed that signified the contractual handover of the submarine, so the submarine in theory had then been handed over to the IPT, not to the Navy yet.

Commissioning happens next. This is a non-payment milestone in this case but it's a very important event for the South African Navy, not every day the Navy gets handed over a new vessel, so it's an important significant event for the Navy and there's a commissioning ceremony that would go with this. The ship at this stage would be named, would get a character now, we named SAS Manthatisi. That was a non-payment milestone, it was an event that took place.

Arrival in Simonstown is similar to that, the Simonstown, following commissioning transited to Simonstown with an escort ship, in this case SAS Drakensberg escorted SAS Manthatisi home. Arrival in Simonstown was a significant event and obviously the Navy had some form of recognition of this taking place, and those were the high level milestones for SAS Manthatisi.

ADV LEBALA: I see the ... I beg your pardon.

25 JUDGE MUSI: To whom was the handover done?

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MR VERMEULEN: Sorry Chair, could you repeat the question?

JUDGE MUSI: To whom was the contractual handover made?

5 MR VERMEULEN: Chair, the contractual handover was made to the Integrated Project Team, to myself and the project officer, and what we would do before accepting the submarine is we would do a lengthy check-off list, we'd make sure that all the tests, all the prerequisite requirements, contractual
10 requirements had been met before we accepted delivery of those submarines to the project team.

JUDGE MUSI: Thank you.

ADV LEBALA: Now is that the instance where you also invited the NATO equivalent of ARMSCOR to come and assist
15 you to inspect the submarine?

MR VERMEULEN: Yes Chair, they were in fact involved throughout the process, they were involved at subcontractor premises doing factory acceptance tests together with us, they witnessed them. They never participated in the sea acceptance
20 tests, it's one of their conditions, they participated in all the factory acceptance tests and harbour acceptance tests. The sea acceptance tests were, the IPT would participate in that together with the core naval team. As I said earlier on you can only on the submarine, on this particular submarine you can fit
25 a maximum of 45 people. The crew is 30, you can take 45

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passengers, we made use of those slots to take personnel to participate in the sea trials and again we would try and get the specialists.

5 If we were doing sonar trials we would get a sonar specialist from the Navy to assist us, incidentally we also used the Institute of Maritime Technology, a subsidiary of ARMSCOR to participate in specialist trials. For instance we would do the acoustic trials, we would measure the signature, the stealth signature of the, the acoustic signature of the submarine, we
10 used the Institute of Maritime Technology, specialist engineers to assist us with that, to help us evaluate the results and to help us draw up the test specification so that we can ensure the acoustic trial was comprehensively carried out, similarly with the magnetic signature of the ship we had used specialist
15 engineers from Institute for Maritime Technology to assist us in that regard.

ADV LEBALA: These experts from the Institute of Maritime Technology, were they South African or were they NATO-based in Europe?

20 MR VERMEULEN: Chair, they were South African, in fact they work as a subsidiary of ARMSCOR based in Simonstown.

ADV LEBALA: Now the contractual handover, is it symbolical?

MR VERMEULEN: No Chair, the contractual handover is a
25 technical handover. It's basically an audit of all the activities

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and requirements rolled up into a checklist, so for instance we would address all the harbour acceptance tests, have all the observations been cleared, sea acceptance test, have those all been successfully done, are all the certificates of conformance in place, is the documentation in place for that, so it was very much a technical, contractual handover.

ADV LEBALA: Now at this stage the submarine is produced and complete, you really have a product.

MR VERMEULEN: Correct Chair.

10 ADV LEBALA: Now Commissioning, we heard the Naval officers explaining “commissioned” from the Naval officers’ side, I don’t know whether it’s the same explanation, let’s hear it from the civilian technical side, what is “commissioning”?

15 MR VERMEULEN: Chair, commissioning is where the submarine is formally named, it’s a christening ceremony, it’s a high level event for the Navy, it’s an emotional event for the Navy to receive a new vessel and from ARMSCOR’s side we respect that, we understand that and we make the necessary provision to help facilitate that exercise.

20 ADV LEBALA: Where did this exercise take place, in Germany or in South Africa?

MR VERMEULEN: In the case of the first two submarines it took place in Germany.

25 ADV LEBALA: Now the product arrives in South Africa in Simonstown during April 2006, am I right, we are talking about

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SAS Manthatisi.

MR VERMEULEN: Yes Chair, that's correct.

ADV LEBALA: We note that SAS Charlotte Maxeke went through the same thing, we don't have to go back to explaining all those concepts, it arrived in South Africa in April 2007, it was commissioned during March 2007, that is it was formally named during March 2007 and it arrived in South Africa April 2007. Look at S102 SAS Charlotte Maxeke, the two last columns.

10 MR VERMEULEN: Yes Chair, those dates are correct.

ADV LEBALA: SAS Queen Modjadji same thing, the Naval officers confirmed that it was commissioned during May 2008 and it arrived in South Africa during May 2008.

15 MR VERMEULEN: That's correct Chair, that specific submarine was actually commissioned in Simonstown.

ADV LEBALA: Next page 19, there comes the integrated logistic support that we went through time and again. Now what makes it to have its own milestones?

20 MR VERMEULEN: They are distinctive milestones, you can see although it runs concurrently with the production phase they are separate in nature, for instance you know one of them you will see there's the completion of the technical manuals, nevertheless the timescales are integrated with production, so these milestones would occur concurrently with the production
25 phase.

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ADV LEBALA: Now my question at this stage is you have been helping and feeding us with the importance of the integrated logistic support, I don't see an exclusive milestone of the RFO Response, the engineering I don't see an exclusive
5 milestone of the submarine product, I see an exclusive milestone of the Integrated Logistics Systems, why is that so?

MR VERMEULEN: If I could try and explain Chair, first of all if I could take you back to the previous page you will see the milestone contractual handover, that addresses ILS elements
10 as well, all the ILS elements, all the activities and deliverables affecting a specific submarine including ILS would be covered in that checklist. They are separate milestones in that you have got different personnel who would do the acceptance and we would have for instance an ILS specialist who would do the
15 acceptance of the training, the technical manuals.

In terms of the production phase these are all contained within these milestones, like for instance keel laying is very much part of the production phase, you're starting to construct the submarine, so that would be a submarine
20 production, the product system milestone. If you look at RFO Responses those don't formulate deliverables, that was, if you recall that gave us an indication of how serious the offerers responded to our bids, so it wasn't a contractual milestone during the production phase as such.

ADV LEBALA: Paragraph 5.9, we don't have to go through

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the ILS milestone, what is significant is that they are in front
of us, what is significant is you referred to the simulator, that
during negotiations you managed to achieve without affecting
the price, without it being in the original specification, delivery
5 of the CIC Simulator, technical manuals that you
overemphasised, delivery of the Fifth-Scale Model that you
projected on the slide that you managed to achieve without
affecting the price which was not in the original specification,
and the spare parts which are the theme of the Integrated
10 Logistics Systems.

Now let's go to paragraph 5.9, the Supply Terms
Agreement concluded between page 19 Commissioner Musi,
Chairperson, the Supply Terms Agreement concluded between
ARMSCOR and the German Submarine Consortium made
15 provisions for liquidated damages, we've dealt with that. In
the case of Project Wills penalties were invoked to the value of
€272 772.62, that's the total of all those figures in Annexure
"RMV5", am I right?

MR VERMEULEN: Yes, you are right Chair.

20 ADV LEBALA: "Conclusion":

*"From the military value perspective the Type 209
submarine were the most cost-effective of the three
Submarine Product Systems on offer".*

Are you referring to cost price?

25 MR VERMEULEN: Chair in this regard I'm referring to that

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slide I produced, if you look at the basic value and the cost to that submarine I judge that to be the most cost-effective. I know that SOFCOM, because they were looking at normalised indices they had other issues to factor in and I understand that they had to apply a formula, now I'm just looking from my, shall I say simplistic view, at the basic value, that's the statement I'm making.

My contention is still that the GSC which met the requirements of the specification and was 18% cheaper than its nearest rival, was the most cost effective, but it could be a contentious issue that I'm stating there, but without continuing to the next computation of figures I think that would stand.

ADV LEBALA: *"During the negotiation phase the scope of supply was significantly extended without incurring any additional cost to the offered price"*

We demonstrated that.

"During the production phase the three submarines were subjected to an intensive regime of accepting test procedures and were delivered as qualified products".

You demonstrated that throughout.

"In conclusion I can state that my responsibility to ARMSCOR and the South African Navy was fulfilled in that the Submarine Product System which was a large and complex acquisition project was delivered

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according to the prescribed specification and within budget”.

Are you talking about the Cabinet budget?

MR VERMEULEN: Yes, I am Chair.

5 ADV LEBALA: Now let's talk about an aspect which the critics would like you to answer because you are qualified, you being a programme manager, these are, we are in the injury time of your questions. The critics would say that the Auditor-General noted that certain percentages, I need to put it
10 properly because I made a note, I beg your pardon Chair. There was a calculation of the military performance that the Internal Audit by the Auditor-General noted that it was not proper and it had exceptions, especially in the area of submarines, do you understand what I'm talking about, what I'm
15 referring to?

MR VERMEULEN: Yes Chair, I have seen that criticism yes.

ADV LEBALA: Now what do you say about this criticism?

MR VERMEULEN: Chair, that criticism could be levelled at the basic results, it's not that clear, or it could be levelled at
20 the next stage where the normalisation takes place as contained in that RFO Evaluation Report, I'm not exactly sure where that criticism lies, at the basic results contained within the value system or the subsequent phases, I'm not a hundred percent sure.

25 ADV LEBALA: I think we could simplify this by asking this

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question, was an improper conduct imputed or found on the part of the team that did the calculations in as far as the evaluation process of bringing the submarine is concerned?

MR VERMEULEN: Certainly not to my knowledge Chair.

5 ADV LEBALA: Was there ever a time when the accuracy of these calculations, remember we are dealing with those formulas. I note that we are not trying to make you to compute them, was there a stage where it was later confirmed that the accuracy of those percentage calculations was in actual fact
10 not improper?

MR VERMEULEN: Chair, I know that the critics allude to the accuracy problems and in fact the Auditor-General picked up on some of the problems and I know ARMSCOR did an internal audit on the figures and if I remember correctly, if I'm talking
15 about the same criticism those were eventually cleared. The ARMSCOR Internal Audit concurred with the results after an evaluation but I'm not sure if we are referring to that specific criticism.

ADV LEBALA: So there was an audit of the Audit-General
20 and there was also an audit of ARMSCOR Internal Audit?

MR VERMEULEN: Yes. Having read the JIT report it makes mention of an ARMSCOR internal audit as well.

ADV LEBALA: So, both audits were found to be proper?

MR VERMEULEN: I believe in the Auditor-General reports
25 there were problems that were found with the calculations, I'm

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not sure if those calculations apply to those calculations in the normalisation of the results or in the calculations of the basic results of the value system, I can only assume that it's in the normalisation results that occurred after we achieved the basic results, that there were calculation errors which appeared in that activity, that's what I'm assuming.

ADV LEBALA: I know you are trying to be technical and I'm not trying to take you there, I'm being mechanical about it by going to the result by saying what did the Internal Audit found as against the Auditor-General's finding?

MR VERMEULEN: I think the Auditor-General did find that there were some irregularities in the military value, in the final results of the military value to the best of my knowledge.

ADV LEBALA: Does that mean that the awarding of the bid to the German Submarine Consortium had a problem?

MR VERMEULEN: Not necessarily Chair, bearing in mind that there were three indices that were addressed, there was a military value, the IP value as well as the financing value, so I'm not sure of the significance of those calculation errors that are referred to in the criticism, I'm not sure how that would impact on the final outcome of the SOFCOM result.

ADV LEBALA: Now I'm using these words cautiously, I never said improper, I never said invalid, I never said irregular, are you aware?

MR VERMEULEN: Yes Chair, you referred to a calculation

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error.

ADV LEBALA: Hence I say was there a problem in as far as the calculation of the military performance where you played the space [sic], remember we are dealing with the military value, the technical evaluation, where you played a space in that lower tier, in the third tier, are you saying that the Auditor-General and the Internal Audit established that there was not a problem?

MR VERMEULEN: Yes Chair, I'm not aware of any problems that we encountered in the calculation of the value system itself.

ADV LEBALA: Now let me ask you a last question actually, two questions. I would like you to tell the Commission about DIP, the way you understand DIP, simplify it, define it in such a manner that the commissioners are, you could be rest assured that the commissioners know DIP, but what is DIP if you had to simplify it for someone who hears about DIP for the first time and how it eloped [sic] in as far as the German Submarine Consortium success is concerned.

MR VERMEULEN: Yes Chair. Chair, DIP, Defence Industrial Offset is broken down into two components, the first applies to general Defence Industrial Participation other than the submarines, it can be in the form of ammunition for the Army or, as long as it's defence related. And then direct Industrial Participation, or D-DIP, a direct Defence Industrial

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Participation applies specifically to the submarines, so obviously whenever direct DIP initiatives come about it will have a direct impact on the supportability of the submarine itself.

5 ADV LEBALA: Now are there ... Now are you better qualified to talk about DIP or is it a specialisation territory?

MR VERMEULEN: Chair, it's a very specialised application in that offsets are calculated on the various formulas and credits that are provided to the discharging of the DIP requirements.
10 Where I can talk about it is how it impacts the submarine because that's where my role is, and there were some significant impacts in terms of the supportability of the submarine and the cost of that supportability of the submarine which came about as a result of the DIP, and those I could talk
15 back on a technical perspective.

ADV LEBALA: Now I would like you to take the Commission through a slide to explain DIP and the examples in as far as the acquisition of the submarine produced by the German Submarine Consortium. Please look at pages 15, 16
20 and 17 of the Slide bundle, let's start on page 15.

MR VERMEULEN: Yes Chair. What you see in front of you in these tables, in these slides that I'm about to show you refer to the direct Defence Industrial Participation. That is the D-DIP which impacted the submarines directly. The first one you will
25 see there, the first activity that I've listed is a company which

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is now called CASSIDIAN (PTY) Ltd., it was originally known as Eloptro which is part of the Denel Group. In this particular case CASSIDIAN received Technology Transfer as you can see there, from the original equipment manufacturer of periscopes in Germany. They also received the opportunity or an opportunity was created whereby CASSIDIAN could manufacture certain assemblies and components for their attack periscopes and Optronic Mast. This happened in-country.

Furthermore on-the-job training for onboard integration and assembly and disassembly of the Attack Periscope and the Optronic Mast was transferred to this company. The advantage here Chair, if I could summarise in this case, as it applies to most of these cases is that it's obviously very expensive to, I'm talking about post-delivery now, the support of the submarine, to place foreign contracts on companies to maintain these important systems, so it's an objective to try and get as much Technology Transfer to South Africa, so we can for all the obvious right reasons from an employment point of view and from a cost point of view it's much better to place contract, Rand value in South African contracts as opposed to foreign contracts.

So, in the case of these particular systems, that's the Optronic Mast and the Attack Periscope, which are very important subsystems onboard the submarine, these are by enlarge as a result of direct-DIP, they are now supported

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locally, the company is based here in Pretoria and their response time (indistinct) problems with the periscopes is very fast and the support contract would be placed on this company and they have the capability of supporting that product.

5 If I could go on to the next one, Siemens South Africa based in Pinetown Kwazulu-Natal, the manufacture of the switchboards for the electrical distribution system was allocated to Siemens South Africa as a result of DIP, and I could mention as well the supply to the frigates as well, they
10 did the switchboards for both of the platforms. MTU South Africa based in Cape Town, they were the recipient of Technology Transfer in order to maintain a Depth C/D maintainer capability. What I mean there by Depth C/D is a
15 level, so they received in-depth technology in order to obtain this capability.

 If I could go down to the next slide Chair. It's a company which was originally named as PERTEC, these companies change names quite regularly, it's now known as
20 IMTEC. In this case they are based in Cape Town, they were the recipient of Technology Transfer in order to obtain again a Depth C/D which is down to diagnostic and your re-engineering level, maintainer capability for the Navigation Data
25 System. The Navigation Data Management System as we know

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as the NVMC is a very important combat suite subsystem onboard the submarine, basically integrates all the non-acoustic or non-sonar senses for the combat management system, so it's a crucial system.

5 Now a significant amount of Technology Transfer was transferred from the German company, this was Rayfen based in Germany, the manufacturer of this Navigation Data Management Centre as well as the Steering Stand and both Battery Monitoring System was transferred to this company
10 based in Cape Town.

 The Council for Scientific and Industrial Research (CSIR), they've got a division known as a Materials, Science and Manufacturing Division, they received a Technology Transfer in the form of local test infrastructure, Cylindrical
15 Transducer Array adaption and production, the production of sonar array transducer elements. In fact CSIR even went a step further and improved on some of the manufacturing processes of the German-based company known as Adves Electronics, so that was a very successful Technology Transfer
20 and they are still obviously involved in the support of the (indistinct).

 The next company I have here is CYBICOM ATLAS DEFENCE company, it was newly formed, they received a lot of Technology Transfer in the form of that CIC Simulator that you
25 saw me mention the slide earlier on, they were involved in the

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software development there of what we call the Man-Machine Interfaces. The Weapon Control Unit, they were involved with software development there, Human-Machine Interfaces, they were involved in the software development and they were the
5 recipient of Technology Transfer in order to obtain the Depth C/D maintainer capability for the ISUS 90-45 Combat Management System. This is a vital system in the makeup of the combat suite onboard the submarine.

This resulted, this interaction with the foreign-
10 based company in Germany known as Adves Electronic formed a joint venture agreement with this company and it's a very successful arrangement in that this vital system is almost fully supported locally, they've got the capability here in Simonstown to maintain the system and in fact to do
15 modifications of the system, obviously with the help of their parent company based in Germany.

The next slide I show GRINTEK COMMUNICATIONS, recently acquired by the Reutech Group), they manufacture and install and integrate all the onboard External Communication
20 Systems onboard the submarines, they also provide the ILS Elements associated with the External Communications System comprising the Technical Handbooks, the training and spare parts.

Our next is SAAB AVITRONICS. This company also
25 Cape-based, they manufacture and install and integrate the

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onboard Electronic Support Measures (ESM), it's an electronic warfare system onboard the submarine, very specialised system, provision of Integrated Logistics Support Elements, again associated with this system and provided by this
5 company.

And then the SIMONS' TOWN DOCKYARD, they were the recipients of Inertial Navigation System (INS) workshop facilities. An Inertial Navigation System is a very important piece of equipment sensor onboard the submarine, it basically
10 is there to maintain the accurate position of the submarine whilst dived and on the surface. Submarine you have to have a very accurate knowledge of the position of the submarine, you need it for your computation for torpedo firing and of course to know where you are, it takes into account the drift of the
15 submarine when you are dived, so it can also be seen as a safety critical piece of equipment. The recipient of intensive on-the-job-training at the respective German shipyards, this took place over an 18-month period in which we would have in the order of six technicians and artisans at any time in
20 Germany at the shipyard receiving training, observing the production process, observing how major assembly units and systems were installed and integrated, so a considerable amount of on-the-job-training took place under the DIP initiative, the direct DIP initiative that was allocated to this
25 project Chair, and that's all I have in connection with local

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industry.

ADV LEBALA: If you could answer this, please do. From your testimony the German Submarine Consortium DIP Index materialised, am I right?

5 MR VERMEULEN: It certainly did with respect to the direct-DIP but having said that I must be cautious because I don't know the exact mechanisms of the DIP discharges of credits, you would have to discuss that with my colleague, however, I can account for the support, the direct advantages that were
10 received by the submarine in (indistinct) terms as I've tried to illustrate on these slides, that I can account for and that was certainly successful.

ADV LEBALA: You've confirmed, I mean you have been honest from the onset that you are not a DIP specialist, we
15 know that within the ARMSCOR team there are specialists who would come and address the DIP element, but back to my question, would you say given what you have told us, what you have demonstrated, let's confine ourselves to direct-DIP, it appears that from the onset the German Submarine Consortium
20 played the DIP element during the bidding stage, are you able to comment about that?

MR VERMEULEN: Yes Chair, I think it's a fair assessment to say that with respect to direct DIP the German Submarine Consortium certainly met their commitments in providing direct
25 DIP, the support to the critical systems that I've mentioned

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onboard the submarine, that certainly did manifest.

ADV LEBALA: Now I'm asking you an unfair question that could be answered up there because you see Term of Reference 1.5, 1.6 are still going to deal with this question and I'm happy that my friend Solomon SC is going to allow me to ask this question, did the DIP in your view, let's confine ourselves to direct-DIP, did the DIP influence the success of the German Submarine Consortium?

MR VERMEULEN: Are we talking about during the bidding phase Chair?

ADV LEBALA: No, I've left the bidding phase. There's a reason why I mentioned the bidding phase, now I'm coming to the DIP as an element. Confine yourself to the DIP element, confine yourself to what you have demonstrated to the Commission now about the DIP, how it was leveraged to benefit the company and it did, that's stubborn before us, now did the DIP in your view, you could look at it as direct-DIP, played a significant role in the success of the German Submarine Consortium bid?

MR VERMEULEN: I would say that the direct-DIP elements applications that I've just shown certainly played a role, in the supportability of that submarine in Simonstown it played a significant role.

ADV LEBALA: Did you learn at any stage as to what happened up there at Level 1 about how DIP was considered?

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I'm talking about, you remember the Level 1, I think it would be appropriate because we are almost done. I would like you to go to page 8 of the Slide bundle. And if you have any comment please feel free, we know where you ended, we know that you were at lower tier, from there you parted ways, the (Indistinct) team prepared the evaluation report of the RFO's lying on the very system that we know was introduced by MoD 4/147, it went higher up SOFCOM, went higher up to the upper tier, we know it did not play a role there.

10 Now as you are standing before the Commission are you alive to the fact that there are players in upper tier who used the DIP to influence the success of the German Submarine Consortium, given the challenges and the underbellies that we've seen in the scores that they've got throughout that Declassified bundle?

MR VERMEULEN: No Chair, I'm not aware of that.

ADV LEBALA: At any stage did you hear it being discussed?

MR VERMEULEN: Chair, I know that it is a ...

20 CHAIRPERSON: I'm sorry, before you answer, before you answer that question, I'm not quite sure at all, if at all the answer that the witness is going to give is going to be of any help to the Commission, so I would not allow that question. Thank you.

25 ADV LEBALA: Fair enough Chair. I think my colleague

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Mr Solomon was getting restless, I could see he was being polite. My final question is what do you say about the product system of the German Submarine Consortium that you brought back, I missed the underbellies, the weaknesses that we have
5 seen bearing in mind that you had a cap on as a programme manager ... I see the commissioners are conferring, before I ..., already you have picked up the theme of my question. I don't know whether the commissioners are still conferring, that's my final question.

10 We've taken you through testimony, very difficult, technical, we've tried to simplify it where we could, some of the concepts still confuse me, we've seen the evaluation, we've seen the scores, we've seen that the Germans only came number 1 in only one instance, the RFO Responses which goes
15 to the engineering component, which goes to performance, not the ILS, we told you what the critics say, that's the underbelly that we can't ignore, it makes vulnerability of the whole process. We know that you say in your conclusion that:

20 *"You could state that my responsibility to ARMSCOR and the South African Navy was fulfilled in that the Submarine Product System which was a large and complex acquisition project ...".*

I think you distinguish yourself there:

25 *"... was delivered according to the prescribed specification and within budget".*

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That's one thing. But this reality of this underbelly that makes this whole process vulnerable, would you say, if you are able to comment, please comment, would you say was fair and the German Submarine Consortium deserved to succeed?

5 MR VERMEULEN: Chair, if I could ... This is a comment and it's more of an observation from my side, obviously I've been very close with this project. I'm always interested in whatever literature becomes available relating to this project, I've been involved for many years in this project and obviously this is not
10 an evidential statement, it's just an observation from my side. I find it very unfortunate because this particular Submarine Product System I think is an excellent product system, I think if it's used properly and maintained properly it will certainly meet the life cycle that it has been designed for.

15 I can't talk on behalf of my Navy colleagues but I'm under the impression that they are satisfied with this product, it does the job, it lends itself to our coastal waters and the lengthy missions that are required for this submarine and its crew to perform, so it's been a very unfortunate experience
20 that this whole project has been tainted by all these allegations, whether they are true or false, from my side at my level it's been a very unfortunate experience because the project itself I think, and I hope I've conveyed this, it would be good if you agree with me that in itself it was a successful
25 product in that it has been delivered successfully according to

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budget, it's all I can say on the subject.

ADV LEBALA: Anything you want to say before you extricate yourself from that platform?

MR VERMEULEN: Not from my side Chair.

5 ADV LEBALA: That's the testimony of Mr Vermeulen. Chair, Commissioner Musi there are some aspects that I'm certain that my learned friend Mr Solomon will deal with, I think they are very critical, I did not want to traverse them for a number of reasons, I don't know whether my colleague ... My
10 colleague Ms Alan SC would also traverse it, I would like to give over to them because we've reached the evening of the testimony of Mr Vermeulen. All that we can say is we had a splendid day Chair, that's the end of his testimony as far as we are concerned.

15 CHAIRPERSON: I think maybe I should say that I was talking to Advocate Lebala because earlier on I was told that there is a meeting that they are supposed to attend at about 14h00 so I see him handing over to his other colleagues to continue the cross-examination, that is why I was trying to find
20 out from him whether is he still going to the meeting or not, and he said to me he is still going to the meeting, so that means that unfortunately we'll have to adjourn now and we will proceed with the same witness again tomorrow morning. So, we'll now adjourn. Thank you.

25 **(COMMISSION ADJOURNS)**