

SABS



Update on the SABS Turnaround Plan Presentation to the Portfolio Committee on Trade and Industry 26 November 2019

- **Delegation details**
- **Brief overview of the SABS**
 - Legislative mandate and SQAM Institutions
 - SABS service offering and funding model
 - Understanding the competitive landscape
- **SABS turnaround plan**
 - Key events which shaped the SABS
 - Reflecting on the financial challenge
 - Approach taken, key achievement and planned initiatives
 - Update on progress made on findings from external auditors and forensic investigations

DELEGATION's DETAILS



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BRIEF OVERVIEW OF THE SABS

[Executive
Authority]



the dti

Department:
Trade and Industry
REPUBLIC OF SOUTH AFRICA

- The SABS was established by the Standards Act, 1945 (Act 24 of 1945)
- The SABS exists as a public entity under the Standards Act, 2008 (Act 8 of 2008)



[Accounting
Authority]



Standardisation

- To develop, promote and maintain **South African National Standards (SANS)**
- To **promote quality** with respect to commodities, products and services for the domestic and export markets
- **Providing conformity assessment services** – certification, laboratory testing and local content verification

Regulation

Administers **regulation** to ensure compliance and protect human health and safety

Accreditation

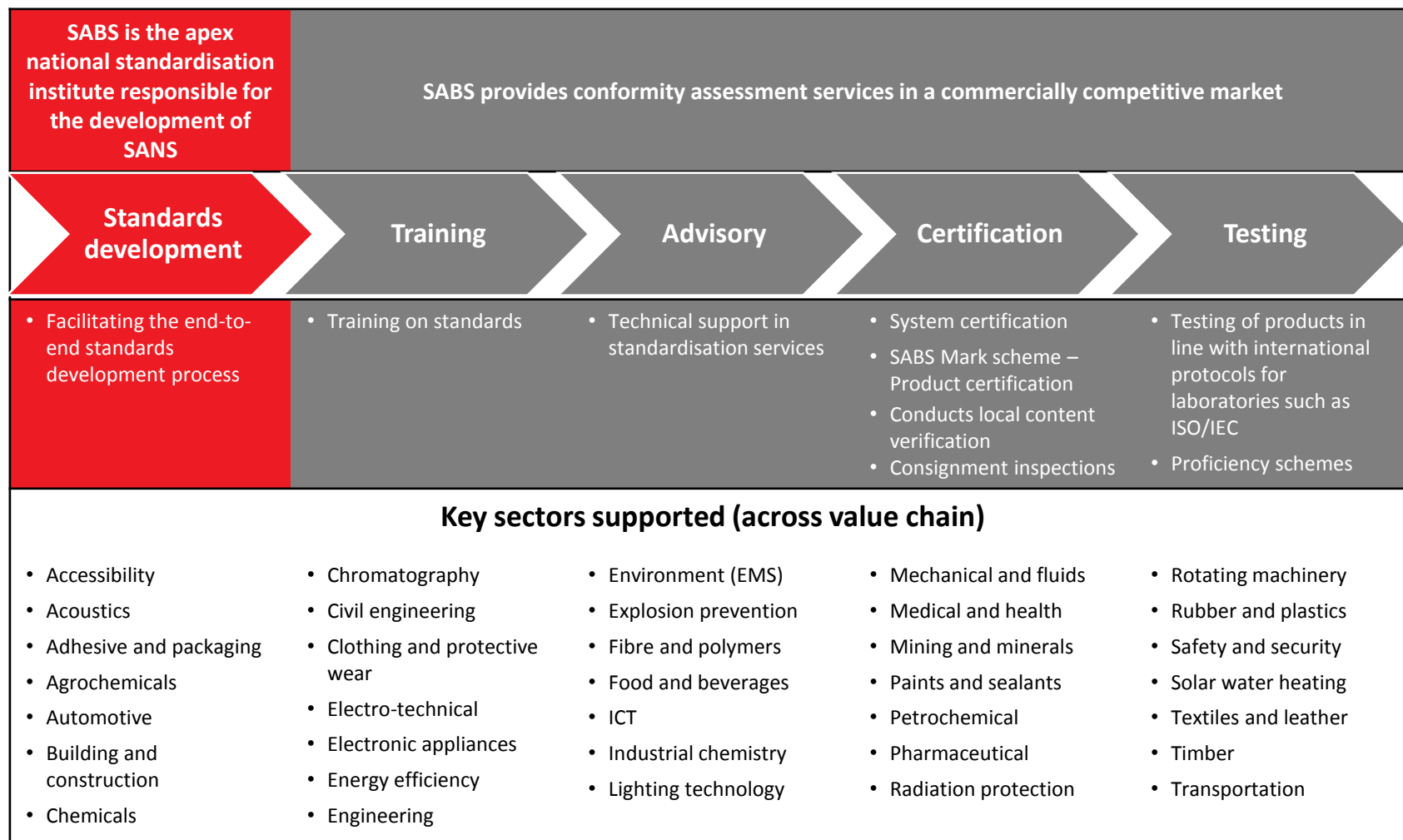
Provides **formal recognition** to carry out specific tasks

Metrology

Underpins testing and calibration through **measurement, accuracy and measurement traceability**

ROLE OF THE SABS IS DISTINCT FROM OTHER SQAM INSTITUTIONS, ESPECIALLY NRCS. NRCS ADMINISTERS REGULATIONS FOR COMPULSORY SPECIFICATIONS, WHEREAS SABS DEVELOPS VOLUNTARY STANDARDS WHICH MAY BE REFERENCED IN REGULATIONS

SABS provides services across the standards development and services value chain, supporting 35 economic sectors and sub-sectors



Funding sources

**Annual grant from
the Fiscus**

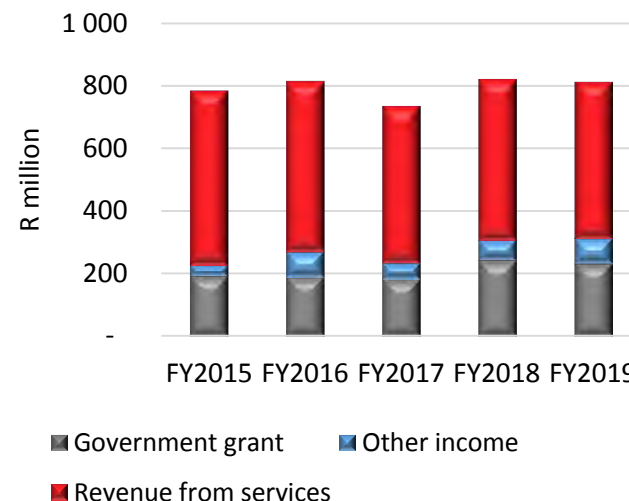
**Revenue generated
in a commercial
market**

SABS business funded

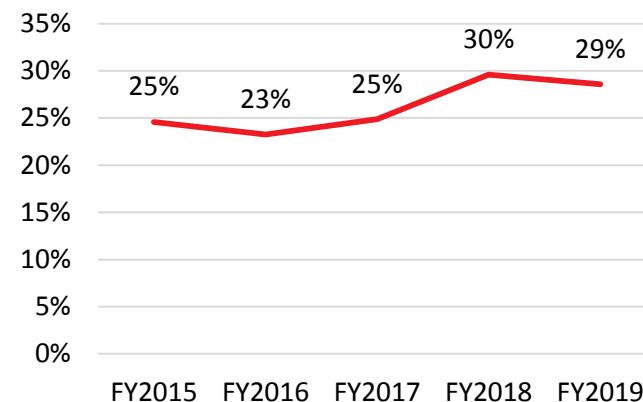
- Standards development and promotion activities
- Operations and support services of the SABS
- Maintenance and investment in infrastructure especially testing laboratories

Conformity assessment services including certification, testing, training and local content verification

Total income



Government grant as % of total income



Source: Latest published SABS annual financial statement

UNDERSTANDING THE COMPETITIVE LANDSCAPE

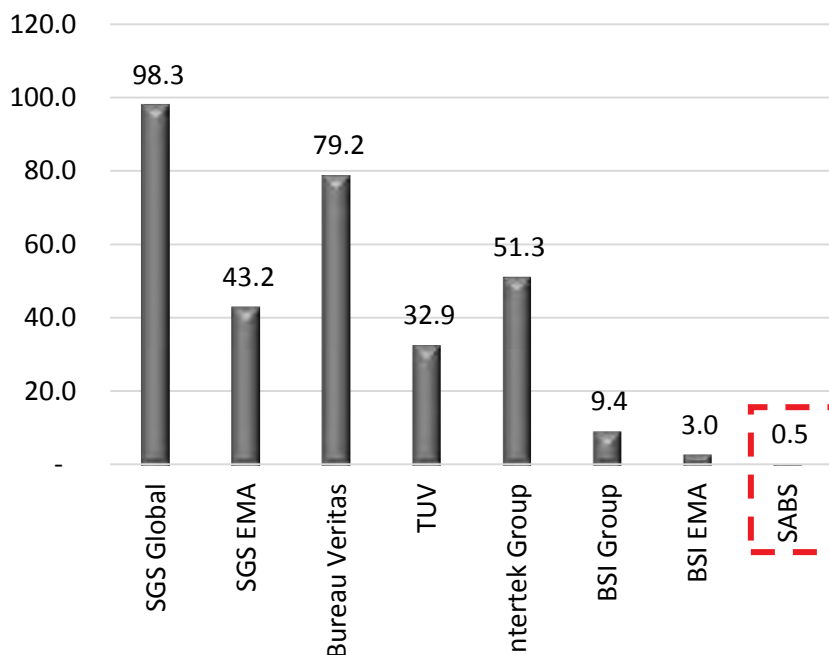
SABS

SABS operates in a highly competitive environment

- Conformity assessment services globally is big business
- SABS faces strong competition from foreign and local companies targeting niche industries and market segments

27
SANAS
accredited
certification
bodies in RSA

Group revenue (in R billion)



Company	Quick facts	Presence in RSA?
SGS Group	<ul style="list-style-type: none"> +97 000 employees +2 600 offices and laboratories 	Yes
BSI Group	<ul style="list-style-type: none"> Operational in 193 countries 117 years in operations 4 784 employees 	Yes
Bureau Veritas	<ul style="list-style-type: none"> 75 428 employees Operational in 140 countries 	Yes
TUV Rheinland	<ul style="list-style-type: none"> Established in 1872 20 450 employees 	Yes
Intertek	<ul style="list-style-type: none"> +3 000 auditors +1 000 laboratories +44 000 employees 	Yes

Source: Latest published company annual reports

EMA: Europe, Middle-East and Africa

SABS revenue, excludes grant from the dti and other income

SABS TURNAROUND PLAN

KEY EVENTS WHICH SHAPED THE SABS

SABS

Pre-1999

Followed a technology / product based structure

- SABS established in 1945
- Sector focus e.g. Chemicals
 - Standards
 - Regulatory
 - Mark scheme
 - System certification
 - Testing
- Mark scheme/permit- evergreen (no renewal)

1999-2001

Ring-fenced standards development and regulatory duties. Commercial business - move towards profit focus and cost-cutting

- Three separate “businesses” created
- Standards
 - Regulatory
 - SABS Holding Company with five subsidiaries
 - Product certification (SABS Mark) transferred from Testing to Certification
 - Mark scheme – changed to 3 year validity, leading to expiry of permits not renewed

2005

SABS Commercial restructured towards sector/industry view with system certification, Mark Scheme and testing services allocated to each sector cluster

- All subsidiary companies collapsed into one entity (SABS Commercial SOC)
- Loss of critical technical skills
- Project Hannibal initiated to improve SABS productivity, review processes and systems. Embedding the principles throughout SABS was a challenge

2012-2017

Significant events

- Central bargaining unit – increased benefit – Additional R65 million per annum unfunded cost to company
- SANAS suspension of certification accreditation – reputational damage
- Discontinued partial testing and requirement to only test to SANS standards – loss of customers
- Cancelled permits/certificates led to loss of annual fees of approximately R19 million in FY2017, R61 million in FY2018 and R57 million in FY2019

2010

Certification and testing activities split into two separately managed business divisions

- Management structure changed from sector/industry to product focus i.e. certification and testing divisions (created silo's)

2008

SABS Act amended and regulatory duties removed from SABS

- NRCS established and all regulatory responsibilities and income (levy) removed from SABS
 - Loss of skills especially from the labs, (test officer and inspectors) to join NRCS.
 - NRCS determined that SABS Mark not adequate proof of compliance and not exempted from levy. As Mark is voluntary, customers elected to discontinue Mark and comply to regulatory requirements – significant loss of revenue
 - Part of lost levy historically used for testing equipment investment.
- SABS not repurposed.

2018

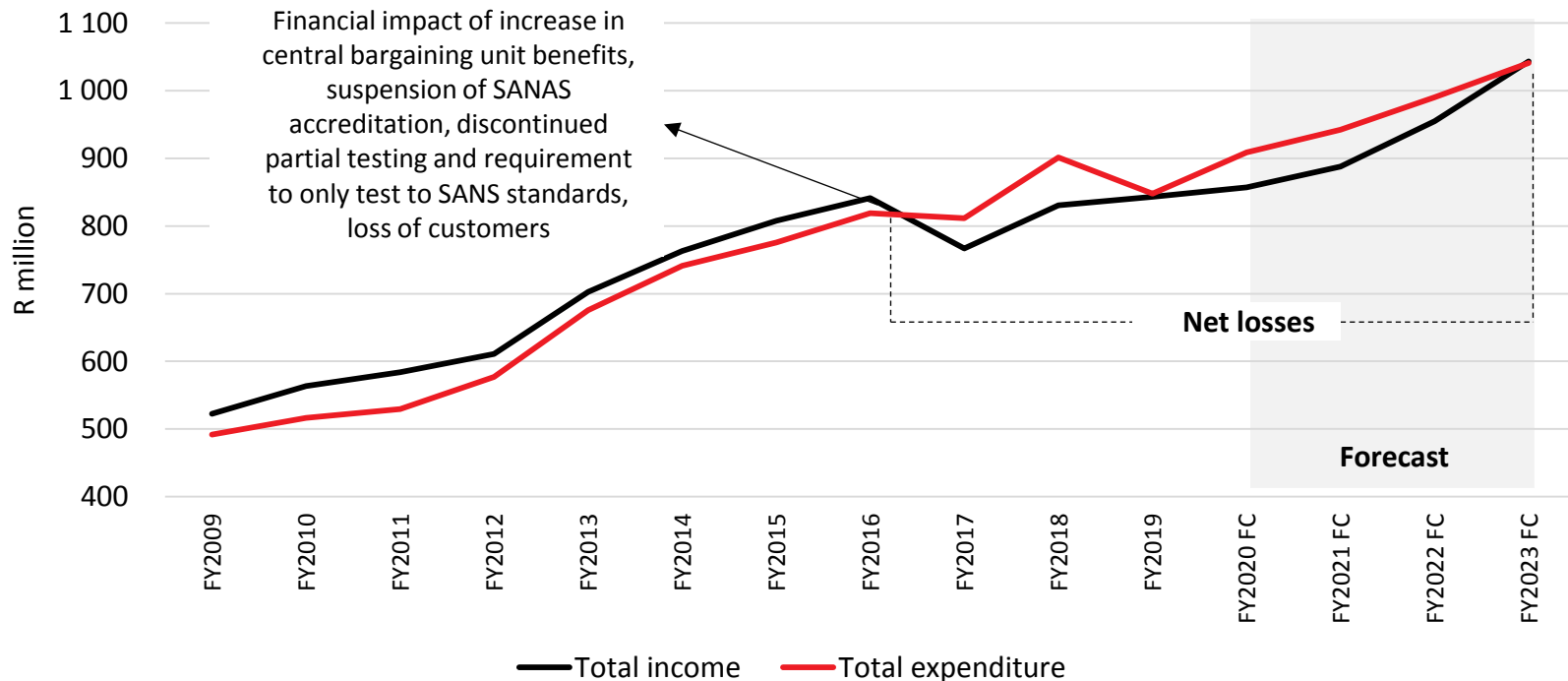
SABS placed under administration and co-administrators appointed

REFLECTING ON THE FINANCIAL CHALLENGE

Broadly two challenges

- Generating **insufficient revenue** from conformity assessment services to cover operational expenditure:
 - Employee expenditure account for ~70% of administrative and operating expenditure
 - Increased benefits awarded to central bargaining unit employees (additional R65 million per annum) without corresponding increase in competitiveness and output
 - National footprint and costly infrastructure
 - SABS provides a broad range of “public good” services in a competitive market
- Unless significant additional revenue is generated and cost cutting achieved, **cash resources will be depleted** by ~March 2021

Financial performance (actual and projected)



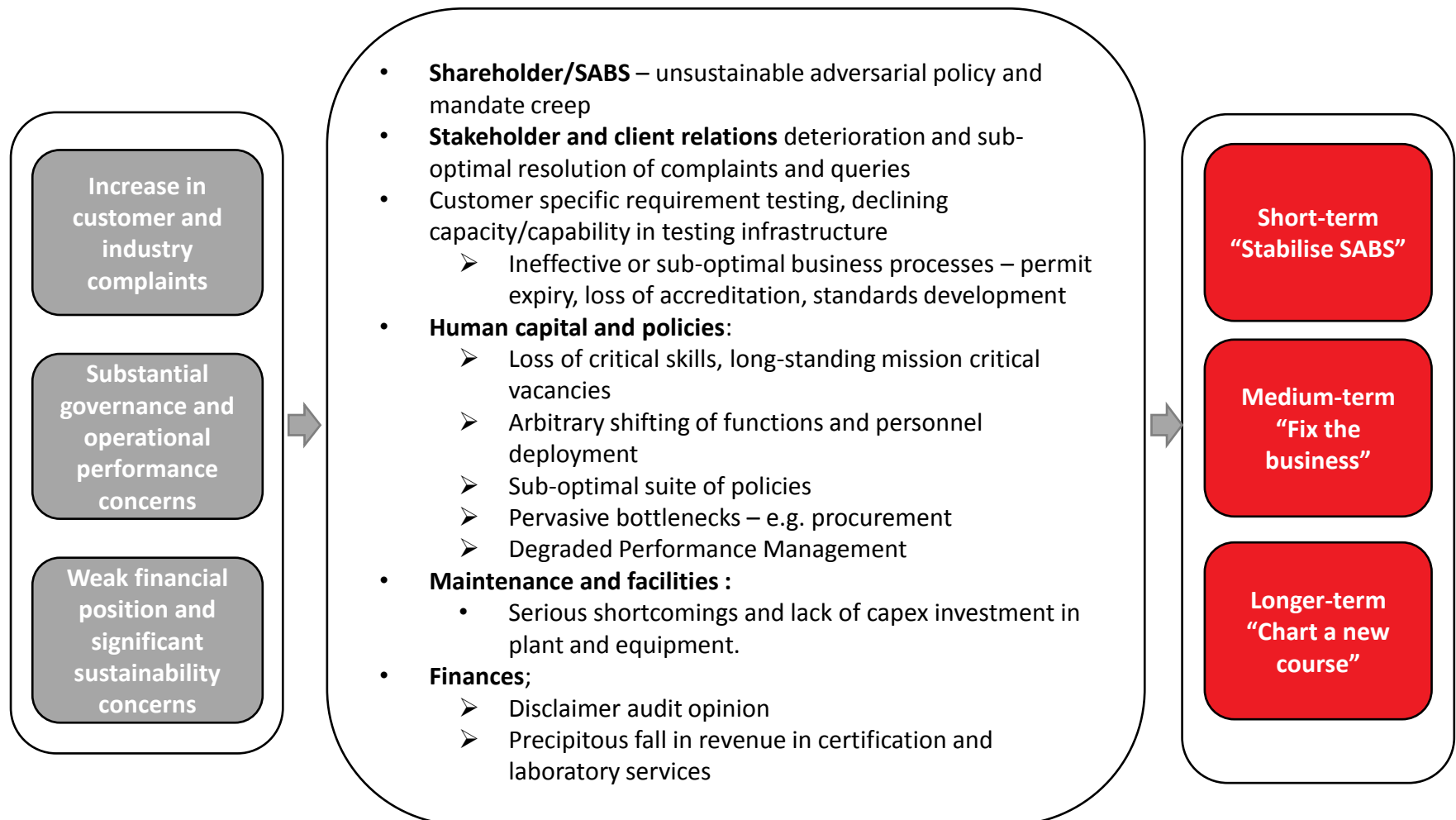
Total income includes revenue from services, government grant, other income and net finance income
Forecast numbers for FY2021 to FY2023 currently in draft

The need for turnaround
plan driven by ...

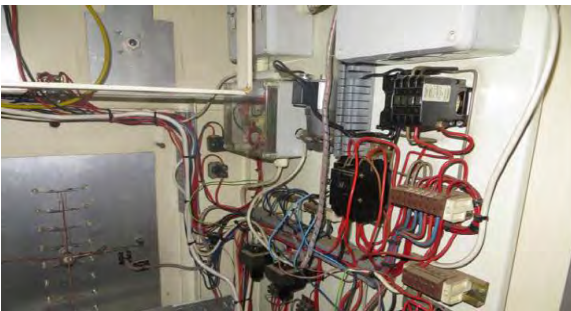
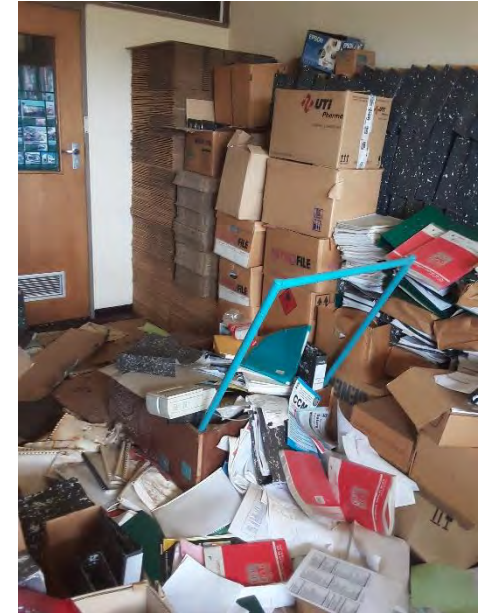
SABS placed under administration in July 2018

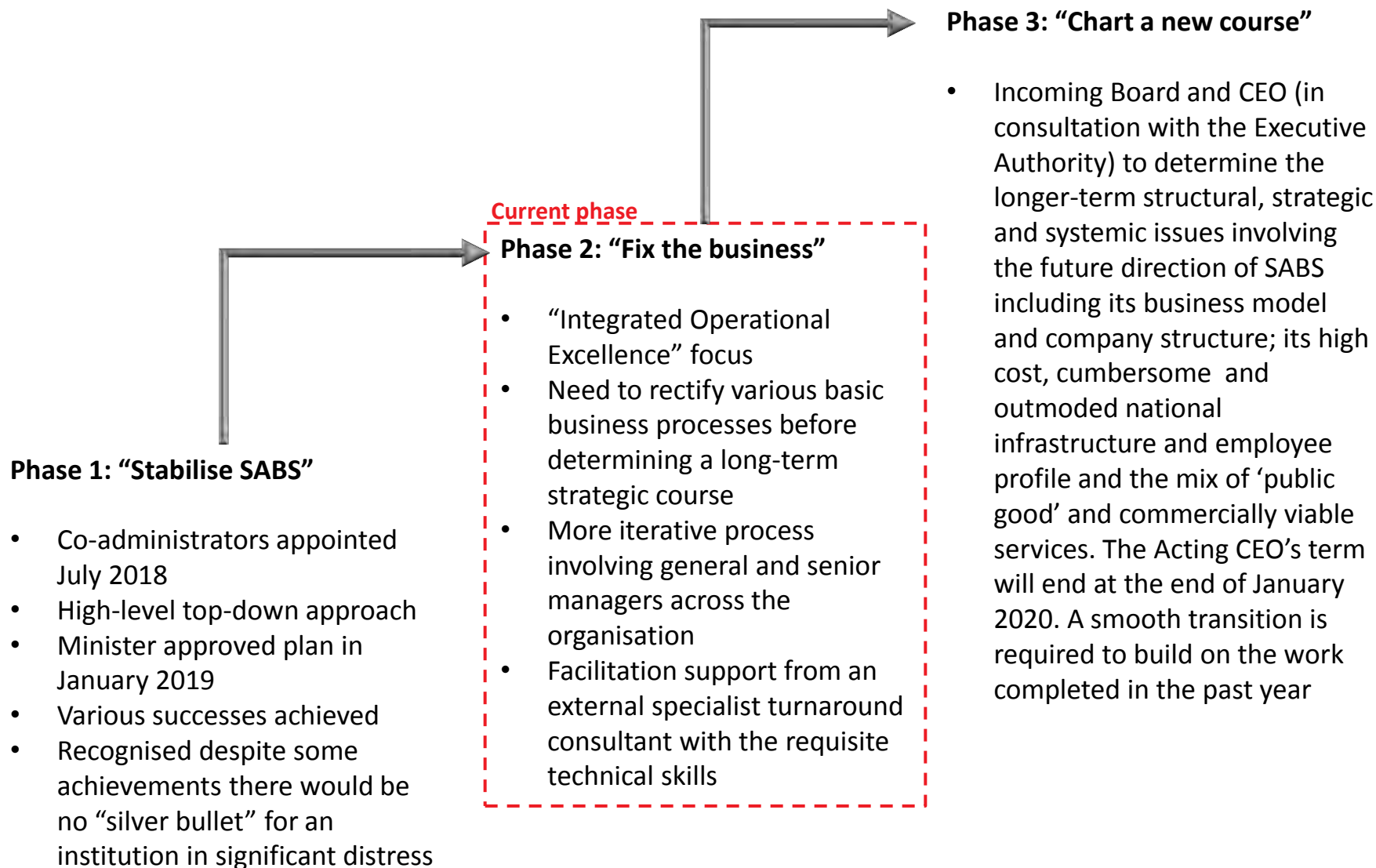
Turnaround plan
developed with ongoing
refinement

Diagnostic process – highlighted....



Main plant room and general housekeeping weak





Financial

- **Cost containment measures implemented**

- R53.5 million saving in total operating expenditure (FY2019: R847.8 million versus R901.3 million in FY2018):
 - Review of all expenditure contracts
 - Implemented a new cost allocation model
 - New pricing model developed for implementation.
 - All vacancies reviewed and only critical positions filled. Since December 2018, total headcount, including permanent and contract workers, reduced from 908 to 879 at the end of October 2019.
 - Total number of Executives have reduced from 8 to 5 in the past year due to natural attrition. A review of the Executive management team structure is currently underway
 - No performance bonuses paid for FY2019
 - Executive’s salary increases limited to 2.8% for FY2020.
 - Proposal for the implementation of a long-term incentive plan was not approved

- **Funding**

- Secured additional funding from the dti to support capital expenditure over the short-term. Additional short-term funding is required for operational expenditure.

- **Procurement**

- Interventions to overcome significant bottlenecks, improving turnaround times from ~60 days to between 50 and 55 days in the past few months, and cost savings

- **Roll-out of ICT strategy**

- Cancellation of R300 million digitisation plan in favour of cost effective integrated model

Operational

- **Certification**
 - Maintained SANAS and RvA accreditation
 - Reduction in expired permits following interventions to secure management, systems and oversight improvements
- **Local content verification (LCV)**
 - SABS has established a local content verification capacity. To date 63 verifications has been completed out of a portfolio of 84 projects within the furniture, textiles, valves, transformers, steel structures, locomotive and vessels industries. Activities were funded from the grant allocated by the dti.
 - SABS has been granted a further R12 million per annum over the MTEF by the dti for LCV. A more comprehensive funding model for LCV has not yet been finalised by government.
 - LCV under the Mining Charter process has been delayed owing to uncertainty related to legal processes currently underway.
 - SABS is working on a methodology and plan involving the use of a digital platform for item identification, standards and LCV in the mining value chain. This will be a pilot with enormous potential benefits for local content and supplier development in the public and private sectors with spill over potential for other industrial sectors.'
- **Laboratory services**
 - Roll-out of sequenced investment in laboratory services. Lack of technical capacity for tender specifications a significant hindrance.
 - Sequential reinstatement of “customer specific requirement” / “partial” testing

Operational (continued)

- **Facilities**
 - Critical maintenance completed on plant room and related infrastructure.
- **Human capital**
 - Review of the full suite of SABS policies; occupational health, safety and environmental management plans as well as training, learning and development plans
 - Put in place a new organisational structure
- **Stakeholder engagement**
 - Ongoing improvement in customer, government and stakeholder engagement
- **Internal audit**
 - Restructuring and resourcing of the Internal Audit department is nearing completion
 - Various forensic investigations have been completed (see later in presentation for more feedback)

Upgrade of sub-plant in C-block



Upgrade of the testing capability for centrifugal pump



Significant work is underway to ensure that the SABS moves from a qualified audit in 2018/19 to an unqualified audit in 2019/20

- Technical accounting matters
 - Assets – componentisation and useful lives of old assets (land; buildings and investment property) (Group and separate financial statements) – **technical experts appointed to assist in componentising the assets of the SABS and reassessing the useful lives**
 - Completeness of revenue within the Laboratory services division (Group financial statements) – **system enhancements to ensure that a report is generated showing all samples received (completeness). Review of all reports underway to ensure there are no gaps in the report**
 - Split between the current revenue and income received in advance for subscription fees (Group and separate financial statements) – **manual review of all subscription contracts and update of dates on the system to ensure correct calculation of revenue vs income received in advance**
 - Expected credit losses relating to loans to group companies (separate financial statements) – **options for settlement of intercompany loan underway**
- Irregular expenditure – Lack of an appropriate system to identifying all irregular expenditure (Group and separate financial statements) – **review of all policies/registers/transactions for 2019 completed. 2018 in progress.**
- Compliance with legislation
 - Some goods, works or services were not procured through a procurement process which is fair, equitable, transparent and competitive – **policy reviews to be completed by 30 November 2019**
- All other findings – 60% completed. All outstanding matters to be addressed by 31 January 2020.

- **Loss of IATF Accreditation**

- A forensic investigation was undertaken into the deficiencies which led to loss of the (International Automotive Task Force) IATF accreditation by the SABS. The investigation raised a number of organisational inadequacies which contributed to the loss of the IATF accreditation. These include: poor succession planning and resourcing; lack of the required technical skills; inadequate reporting of interventions, remedial actions and oversight by the then Executive and governance deficiencies. Remedial steps are being taken to address the weaknesses identified.

- **Irregular appointments**

- A forensic investigation into allegations by anonymous whistle blowers concerning irregularities in the appointment to various positions in the SABS spanning a period between February 2015 and 30 November 2018 undertaken. This raised a number of deficiencies in the recruitment and appointment processes to various positions. A process has been initiated to obtain further legal advice as to the possible recourse and obligations of the SABS based on the report findings and take disciplinary action against employees still in the employment of the SABS.

- **Eskom Coal Testing**

- A forensic investigation was undertaken into allegations of irregularities by the SABS with respect to coal testing for the Tegeta Coal Mine. The investigation uncovered deficiencies in operating procedures and compliance thereto which have led to amendments in operating activities and an increased focus in the internal audit of compliance to operating procedures. The report was sent to the dti and Eskom.

Phase 2 of the ‘bottom- up’ turnaround plan, involving all of senior management to secure deeper ‘back-to-basics’ and ‘**integrated operational excellence**’ across the SABS business.

Objective: Improve resource utilisation, secure basic operational efficiencies and on-time delivery.

- **Planning, scheduling and workflow optimisation**
 - Review of **planning and scheduling systems** to assist in integrated planning and master data quality
 - **Certification division**
 - ❖ Establish a **centralised planning and monitoring function**. Ensure that delivery times are monitored and delays appropriately addressed
 - ❖ Implement a **technology-based audit management system** to assist auditors in the execution of the various audits
 - **Laboratory services**
 - ❖ Review of **laboratory processes, including sample management, densification of laboratories and testing workflow**. Pilot four labs: cement, detergents, footwear, materials and installations at NETFA
 - ❖ Review, and where appropriate, standardise and **integrate the laboratory management systems**
 - ❖ **Asset management and housekeeping**
 - Complete asset management system implementation to integrate laboratories, finance and procurement
 - Complete asset verification
 - Conduct general housekeeping – clearing of old equipment and clutter in the laboratories and adjoining workspaces.

- **Client management, sales and marketing**
 - Establish a centralized, **integrated sales and operations forum**
 - Develop capability to assess **ongoing customer needs and requirements**
 - Adopt a **new marketing and sales plan and structure**
 - Operationalise the **product development portfolio**
 - Develop, in conjunction with the operating businesses, **client engagement plans** for the top 50 best opportunities for additional sales to be followed by other business opportunities
 - **Enhance and simplify the customer journey**, focusing on a improving the customer engagement model across the organisation
- **Finance and facilities**
 - **Further cost-containment** measures
 - Develop a **cost management framework**, providing a split between direct and indirect expenditure
 - Complete **grant allocation modelling** project
 - Develop strategies and plans to secure **further funding** for the SABS
 - Upgrade of the **main plant room and adjacent infrastructure**
- **IT systems**
 - **Review core IT systems**, concentrating on Labware/LIMS and Certification solutions and enterprise resource planning (ERP) and hardware to establish critical timeline for upgrade or replacement

- **Q-Block assessment**

- Decision to construct new laboratories (Q-block), operating independently from the main plant room, was taken in 2008. Construction commenced in 2010 and partial occupancy occurred in 2011.
- Full occupancy was not achieved mainly due to the inability of the heating, ventilation and air conditioning system to provide stable environmental conditions to all laboratories. The root cause being inadequate contracted design specifications.
- Funding to the value of R300 million was provided by the dti of which R205 million has been spent.
- SABS is currently finalising the appointment of a multi-disciplinary engineering (MDE) firm, to advise the SABS on extent of the problem, proposed solutions and additional infrastructure requirements as well as potential cost to achieve full occupancy. A draft report is anticipated early in the new year.
- A technically informed decision on the best course of action will then be taken

- **Human capital**

- Complete **skills and culture audit**. Develop talent acquisition plans to fill gaps
- Review **consequence management** framework
- Investigate **incentives or disincentives measures** linked to the turnaround plan
- Consider a **fit-for-purpose organisational structure** which is less “top-heavy” and prioritises the commercial business requirements

- **Standards**

- **Prioritise standards and revenue opportunities linked to the masterplans** to be developed as part of government’s industrial development plans

Initiatives are supported by a detailed project plan, allocated project owner and delivery timeframes. All project plans are available on a shared IT portal and monitored on an on-going basis

- At the core of Phase 2 of the Turnaround plan: **secure an integrated operational and execution management plan** for SABS, with strong monitoring and oversight. The plan is based on getting all the basic ‘nuts and bolts’ operations back to acceptable levels. These plans will be supported by robust sales and marketing initiatives.
- The challenges at SABS are deep-seated and multi-layered. The **turnaround plan will take time to yield optimal outcomes** to return the institution to a competitive, professional services company which is able to compete in the certification and testing market, develop standards which are aligned with and support the industrial effort and provide a cost effective and competitive services in local content verification and training.
- The **financial sustainability and the cash position** of the SABS remains the most critical challenge over the next two years.

THANK YOU