PUBLIC AFFAIRS RESEARCH INSTITUTE

STATE REFORM

The Case for Encouraged Whistleblowing in Public Procurement in South Africa

POLICY BRIEF

NOVEMBER 2020

ABOUT THIS BRIEF

This policy brief is one of a series developed by the Public Affairs Research Institute (PARI), intended to contribute to a strategy for state reform. The series focuses on specific interventions to achieve integrity, democratic control and effectiveness in the public service. It is designed to provide reform-minded politicians, public servants and civil society actors with a programme for constructive change upon which they can agree and act.

AVAILABLE ONLINE AT

www.pari.org.za

SUGGESTED CITATION

Brunette, R. and J. Klaaren (2020) 'The Case for Encouraged Whistleblowing in Public Procurement in South Africa'. State Reform Policy Brief. Public Affairs Research Institute.

Introduction

South Africa has descended into an unprecedented socio-economic crisis. Even before the Covid-19 pandemic, the country had entered its second recession in as many years. Gross domestic product per person had returned to 2008 levels. Unemployment, already at five times the global rate, was rising. So was the poverty rate, with more than half of South Africans living on less than R1,183 a month and a quarter living on less than R547. Early data suggests that, with the pandemic, South Africa entered its deepest, quickest economic contraction on record. By the end of June 2020, 3 million jobs were lost and the expanded definition unemployment rate had risen to 42 per cent. Thirty-seven per cent of households had run out of money to buy food. Job and income losses are concentrated among poor people, black people and women, worsening what were already the highest levels of inequality in the world.

South Africa will need an active and capable state to lift itself out of this crisis. Corruption in public procurement is a major impediment to this. The Covid-19 procurement scandals that have shocked the country vividly illustrate this problem. Ethics are important. Ethical government, however, rests on establishing institutions, checks and balances that prevent public servants from doing the wrong thing and that encourage them to serve the social and economic interests of the people of South Africa. In this policy brief we present a simple reform that will help to achieve this in public procurement. It consists of a mechanism that encourages whistleblowing and the recovery of civil damages arising in the course of fraudulent transactions perpetrated against the state.[1]

1 For a fuller discussion, see the PARI position papers on state reform, available online at www.pari.org.za. The theme of this policy brief, public procurement, is dealt with more broadly in R. Brunette and J. Klaaren (2020), Reforming the Public Procurement System in South Africa. Position Papers on State Reform.

Public procurement in South Africa

Public procurement, which in 2017 accounted for 19.5 per cent of gross domestic product, is a significant component of state operations and of the South African economy. It is, unfortunately, beset with serious problems of inefficiency, ineffectiveness and corruption. There are a number of reasons for this.

The legal framework for public procurement is too fragmented and complicated. It is sometimes self-contradictory. The central regulatory authority of public procurement, the Office of the Chief Procurement Officer, has had inconsistent political backing. It lacks the staff numbers, budget, and technological infrastructure needed to secure control convincingly and drive efficiencies. The procurement system is opaque. It does not provide adequate public access to information. Its personnel are generally-speaking insufficiently specialised and professional. South Africa expends considerable resources through public procurement to promote the emergence of new businesses, but it discourages the formation of durable business capacity by offering small, short-term, vaguely specified and uncertain contracts and relationships. South African public procurement suffers from widespread non-compliance, lack of enforcement and few or no consequences for wrongdoers. The new Public Procurement Bill aims to consolidate the legal framework and establish a strengthened Public Procurement Regulator. It is characterised, however, by inadequate promotion of transparency, professionalisation, developmentalism and enforcement.[2]

South African public procurement suffers from widespread non-compliance, lack of enforcement and inadequate consequences for wrongdoers.

In this policy brief we focus on the last problem. The legal framework and broader reform of South African public procurement requires robust disciplinary mechanisms. These are currently lacking. We lay out a policy to change that.

Oversight and enforcement

South Africa's oversight and criminal justice institutions have been undermined by politicisation and often deliberate incapacitation. Although there are indications that this is changing, efforts to discipline, prosecute and convict transgressors, and to recover financial damages from them, have been slow and limited.

The Auditor General is historically the most independent and robust of South Africa's oversight institutions. The Public Audit Amendment Act is now law, giving the Auditor General power to take remedial action in cases of governmental corruption, to issue certificates of debt when accounting officers and authorities fail to take action and to refer matters for criminal investigation. Welcome though this is, even the Auditor General is unlikely to have the capacity to grapple with South Africa's corruption problem. It risks becoming a target of corrupt political actors and over the longer term it may not fully escape the kind of damage that other independent oversight and enforcement agencies have sustained.

The Auditor General also still relies on downstream enforcement agencies to follow through on its recommendations. The National Prosecuting Authority, although in the course of being rebuilt, is not currently in good condition. Among other problems it is inadequately staffed and funded, and given South Africa's current fiscal position this is unlikely to change. In the 2020 financial year, the

2 See Public Affairs Research Institute (2020), Draft Public Procurement Bill: Submission of Public Comments. https://47zhcvti0ul2ftip9rxo9fj9-wpengine.netdna-ssl.com/wp-content/uploads/2020/07/PARI_20200630_DraftProcurementBill_Submission.pdf

number of convictions of government officials for corruption-related offences actually declined to 183, which is lower than the number of potential corruption cases logged for internal investigation and referral in some large municipalities. The Asset Forfeiture Unit attained corruption-related civil recoveries of just R3-million. Clearly additional strategies for confronting corruption are required.

The history of encouraged whistleblowing

Whistleblowers in South Africa face appalling risks. Despite existing legal protections, they face being ostracised by managers, colleagues and friends. They may be subjected to contrived counter-accusations to throw their reputation and credibility into question. They lose their jobs and get blacklisted in powerful party-political, public-administrative and corporate circles. They often face physical threats to themselves and their families. The social and economic costs of whistleblowing can be severe and enduring, but why should whistleblowers have to be martyrs? In an open and democratic country like South Africa, there should be no objection to the political and economic empowerment of citizens in the face of corruption and similar wrongdoing. How can legitimate whistleblowing be encouraged when the consequences for brave individuals are often so destructive?

A notable option is what we call encouraged whistleblowing. In the legal profession, it is known as *qui tam*, from the Latin for a person who sues on behalf of themselves and the King. It is particularly appropriate when the state is overwhelmed by and unable to prosecute large numbers of supply chain corruption cases.

In an open and democratic country like South Africa, there should be no objection to the political and economic empowerment of citizens in the face of corruption and similar wrongdoing. How can legitimate whistleblowing be encouraged when the consequences for brave individuals are often so destructive?

The mechanism is ancient and versatile. It was a common feature of Roman law more than two thousand years ago. Vestiges continued into the European middle ages and it reemerged to become an important vehicle of English law from the fourteenth to the nineteenth centuries. There it was used to enforce regulations dealing with everything from religious observance to industrial production, trade, pollution and bribery.

In the United States, the modern home of encouraged whistleblowing, it goes back to the Civil War of the 1860s. President Abraham Lincoln was leading the struggle to end the secession of the southern states and abolish slavery. The federal war effort was undermined by contractors who profiteered by selling the Union Army small arms that would not fire and artillery shells filled with sawdust. At the time Washington lacked the investigative and prosecutorial capacity to deal with this threat, so in order to root out procurement corruption Lincoln introduced the False Claims Act. The idea was simple. Private individuals with information about fraudulent claims perpetrated against the federal government would be encouraged, with a sort of "bounty", to bring this information forward. They could institute a civil action in any competent court, in the name of themselves and the United States, and if successful they would receive half of a standard statutory civil penalty and half of the damages awarded. The Act mobilised whistleblowers, and their lawyers, in a way that served their interests and those of the government. It was followed up with similar legislation on tax violations.

Over the years, the British and American governments built robust apparatuses of public investigation and prosecution. At the same time, abuses crept into their encouraged whistleblowing mechanisms, so these fell into discredit and disuse. In Britain, where encouraged whistleblowing had been applied very widely, often to enforce unpopular and unjust laws, it was taken off the books in 1951. In the United States, however, the mechanism had always been applied more circumspectly. It was not abandoned, but rather increasingly refined until an ingenious 1986 amendment to the False Claims Act revived it.

Encouraged whistleblowing in action

The basic encouraged whistleblowing provision is elegant and effective. Its conditions are a law establishing a violation, such as a fraudulent transaction with the state. The remedy for this violation must involve a financial penalty, such as a civil forfeiture or the recovery of damages suffered by the state. An encouraged whistleblowing provision then creates a private right to enforce this public law. In order to assert this right, a whistleblower must be an original source, in the sense that they must have previously disclosed what is now public information or they must have new information that is independent of and adds materially to public information. If so, the whistleblower would ordinarily network with a whistleblower-protection NGO and be referred to a specialist law firm to bring an action to court. In the event of success, they are rewarded with a portion of the forfeiture or damages awarded by the judge.

The encouraged whistleblowing provision incorporates a subtle array of incentives, checks and balances. These work to shape behaviour in desirable ways and to prevent abuse.

The modern encouraged whistleblowing provision involves a number of additional features. The provision must give sufficient encouragement to whistleblowers, but it must do so in a way that also protects the public's finances and interests. These objectives are achieved, first, by enhancing the potential financial penalty, say by legislating double damages for fraud in public procurement. Second, the portion of these damages that a whistleblower might receive is then defined by lower and upper boundaries, for example (purely for illustration) between 25 and 50 per cent of the doubled damages. The presiding judge has discretion, in light of circumstances, to set the rewarded portion within these boundaries. Third, the action is lodged with a court under seal, it is kept confidential until hearings commence, and in the interim the state is given an opportunity to decide whether to adopt the action as its own. Since the state would thereby take on the costs of the action, the lower and upper boundaries would then be reduced to say 15 and 30 per cent. To illustrate how this works, Figure 1 assumes that a contractor is proven on a balance of probabilities to have defrauded the state of R10-million:

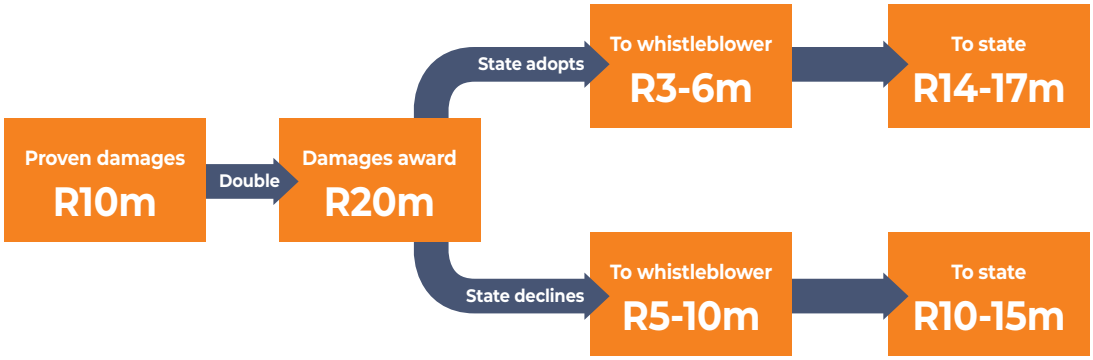

Figure 1 Illustrative calculation and allocation of damages

Formulated in this way, the encouraged whistleblowing provision incorporates a subtle array of incentives, checks and balances. These work to shape behaviour in desirable ways and to prevent abuse. Where whistleblowers and their lawyers bring frivolous and vexatious actions, a judge can order them to pay the defendant's costs. Where they have a decent case, the lower boundary provides certainty. In the example above, they can expect at least R3-million for their troubles. The upper boundary allows the presiding judge to craft decisions that encourage some forms of whistleblowing more than others. In making an award, the judge can consider whether the whistleblower was complicit in the fraudulent transaction, how they came upon the relevant information, the quality of this information, their motives and conduct in the proceedings, the risks and costs that they have sustained, and the broader public interest.

The involvement of multiple, independent players in encouraged whistleblowing creates an elaborate web of accountability. Bona fide whistleblowers are likely to search out trustworthy whistleblower-protection NGOs. These NGOs are more likely to want to refer them to specialist lawyers and firms who have built a reputation for integrity and professionalism. These law firms are more likely to be taken seriously by representatives of the state and the courts. Where state representatives decline to adopt the action, they signal to the courts that the case lacks merit. If they think the action flies against the public interest, they can appear before the presiding judge in hearings to make their case. If the action nevertheless succeeds, the state loses money and its legal representatives are embarrassed for their poor judgement.

Encouraged whistleblowing empowers people with integrity to act by promising they will be compensated financially for their losses and will be able to take care of themselves and their families. Investigations are a time-consuming and costly way to get at inside information. The proposal set out here encourages people with information to come into the open on their own accord. It sows distrust in corrupt combinations by motivating people around them to break ranks and come forward.

Encouraged whistleblowing is by far the most effective mechanism that the United States federal government has to address procurement fraud. In the year ending September 2019, it recovered $2-billion under the encouraged whistleblowing provision of the False Claims Act, a full 72% of all federal recoveries for false claims. Since 1988, the federal government has recovered $44.7-billion through this mechanism. Information brought to light through the provision can also be used in subsequent prosecutions.

Encouraged whistleblowing empowers people with integrity to act by promising that they will be compensated financially and will be able to take care of themselves and their families.

Encouraged whistleblowing in South Africa: a proposal

The United States has relatively low levels of procurement corruption. It has generally independent, world-class investigative and enforcement agencies. In South Africa, we have very high levels of procurement corruption. Encouraged whistleblowing will take pressure off stressed and under-resourced public investigators and prosecutors. Proportionately, the potential gains for the country's struggling fiscus are greater than in the United States.

An encouraged whistleblowing provision in South Africa need not be rolled out all at once. There are clearly political constraints on how far and quickly we can go with procurement reform. In any case, a more gradual expansion of encouraged whistleblowing will allow for practice, refinement and more systematic capacitation of the mechanism. Government could start with certain critical categories of procurement and organs of state. These could be chosen according to whether these have an identifiable reform coalition and impetus, as is currently the case around some of the state-owned enterprises and local content procurement. Initial successes with encouraged whistleblowing will provide a stronger foundation for future advances.

The legal basis for this will have to be fixed in the upcoming Public Procurement Act. An additional section should be inserted into the draft Bill. It could be structured as follows:[3]

1. Anybody who makes a false procurement claim or in some other way tries to get a false claim paid by a procuring entity violates the Act.
2. Anybody who violates this section of the Act is liable for a penalty of up to R100 000 and for damages of double the amount of the false claim. However, if the person violating this section is the whistleblower, he or she will only be liable for the amount of the false claim.
3. A whistleblower can file a complaint in confidence, submitting full information alleging a violation of this section at a High Court.
4. Such a complaint will remain in confidence for up to 120 days so that the authorities can investigate the claim.
5. Within the 120 days, the authorities will indicate whether or not they will themselves take on the case.
6. If the authorities take on the case, the whistleblower will be eligible to receive no less than fifteen per cent and up to a quarter of the damages recovered.
7. If the authorities do not take on the case, the whistleblower can proceed with it and will be eligible to receive no less than twenty per cent and up to a third of the damages recovered.
8. Whistleblowers will not be penalised for actions they take in terms of this section of the Act.
9. The Minister of Finance, in consultation with the Minister of Justice and Constitutional Development, will regulate this section, including the categories of procurement and the organs of state to which it applies.

3 These provisions, framed in the language of draft legislation, can be found in Jonathan Klaaren and Ryan Brunette, 'The Public Procurement Bill needs better enforcement: a suggested provision to empower and incentivise whistle-blowers', *African Public Procurement Law Journal*, 7 (2020): 15-25.