FREE STATE HIGH COURT, BLOEMFONTEIN
REPUBLIC OF SOUTH AFRICA

Case No.: 1719/2010

In the matter between:-

NATIONAL ASSOCIATION OF WELFARE ORGANISATIONS AND NON-GOVERNMENTAL ORGANISATIONS	First Applicant
N G SOCIAL SERVICES FREE STATE	Second Applicant
FREE STATE CARE IN ACTION	Third Applicant

and

THE MEMBER OF THE EXECUTIVE COUNCIL FOR SOCIAL DEVELOPMENT, FREE STATE	First Respondent
HEAD OF THE DEPARTMENT OF SOCIAL DEVELOPMENT, FREE STATE	Second Respondent
NATIONAL MINISTER OF SOCIAL DEVELOPMENT	Third Respondent

HEARD ON: 5 MAY 2011

JUDGMENT BY: VAN DER MERWE, J

DELIVERED ON: 9 JUNE 2011

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[1] This is a sequel to the judgment delivered in this matter on 5 August 2010 and it must be read with that judgment.

[2] On 5 August 2010 *inter alia* the following orders were made:

"1. It is declared that:

1.1 the Free State Policy on Financial Awards to the Nonprofit Organisations in the Social Development Sector of August 2003 ("the policy") is inconsistent with the constitutional and statutory obligations of the first and second respondents in terms of sections 26, 27 and 28 of the Constitution, section 4(2) of the Children's Act, 38 of 2005, section 3(2) of the Older Persons Act, 13 of 2006 and the provisions in respect of statutory services referred to in this judgment, in that it fails to recognise as a fundamental principle of funding that nonprofit organisations that care for children, older persons or vulnerable persons in need or provide statutory services, fulfil the obligations of the first and second respondents.

1.2 the policy is not a reasonable measure as envisaged by the aforesaid provisions to the extent that it lacks a fair, equitable and transparent method of determination of the contributions that the aforesaid nonprofit organisations should make from own resources or sources of income in respect of provision of the aforesaid care and services.

2. The first and second respondents are ordered to adopt and to implement a redrafted or revised policy in order to remedy the abovementioned shortcomings.

3. The first and second respondents shall within four months

of date of this order deliver a report under oath stating what steps have been taken to comply with this order.

4. The applicants may within one month of delivery of the report, deliver a commentary under oath on the report.

5. The first and second respondents shall within one month of delivery of the commentary, deliver a reply thereto under oath.

6. The matter shall be enrolled on a date to be fixed by the registrar in consultation with the presiding judge for consideration and determination of the aforesaid report, commentary and reply."

[3] The department and the applicants filed papers in terms of paragraphs 3, 4 and 5 of the order. The department's papers in terms of paragraph 3 of the order consist of an explanatory affidavit by the second respondent, to which is attached a report by KPMG Services (Pty) Ltd ("KPMG") and a draft revised version of paragraph 11.6 of the policy.

[4] In this affidavit the second respondent states that although this may not have been expressed clearly in the policy, the

department, from the MEC down to the officials tasked with the implementation of the policy, has at all times been acutely aware of the fact that the department is obliged to provide the funding concerned and was obliged to do so as a matter of constitutional and statutory duty. The second respondent added however that as far as the finding that the policy does not contain a fair, equitable and transparent method of determining which NPO's are able to and should make a financial contribution towards the provision of social welfare services by them is concerned, "... that particular aspect of the ... policy is not so easy to remedy...". It is further stated that both the relevant national policy and the policy are in the process of being revised overall, but that neither could be completed by the time that the department had to file its affidavit in terms of the order. For this reason the department instructed its legal representatives to formulate a draft revision only of that part of the policy which would enable the department to comply with the order. The department also appointed KPMG to, *inter alia*, develop a model for the costing and distribution of the funding available to it for the provision of social welfare services in the Free State Province and to develop a draft implementation plan for the incorporation of the model into operational use. The result hereof is that KPMG produced its aforesaid report and the department's legal representatives drafted a revised version of paragraph 11.6 of the policy. The second respondent states further that these two documents have to be read together and submits that the proposed revision of paragraph 11.6 of the policy together with the processes the department intends to employ pursuant to the KPMG report will remedy the problems identified in the judgment and will comply with the order.

[5] In respect of the way forward, it is stated in this affidavit that KPMG still has to perform a number of tasks which could not be completed in the time available. These tasks include the finalisation of the social welfare service sectors contained in the first schedule to the proposed revised policy given that these must represent homogenous costing groups, the determination of the reasonable annual cost per case (or beneficiary) and the finalisation of an implementation plan. A further revision of the draft reformulation of paragraph 11.6 of the policy may be necessitated by further inputs received from the department and KPMG. It is stated that it is not

possible for the policy as it is proposed to be revised to be implemented in respect of the 2011/2012 financial year. The department however intends to implement the costing model and recommendations in the KPMG report. As the budget process for any year commences in June of the preceding year, it is anticipated that the costing model and recommendations in the KPMG report will be used in the department's budget process for the 2012/2013 fiscal year. Finally, the court's approval of the amendment to the policy, as set out in the revised version of paragraph 11.6 thereof together with the report of KPMG, is sought.

[6] The KPMG report states that it describes a conceptual costing model, in the sense of determination of funding requirements based on standardised costs of servicing beneficiaries, that would lead to a fair, equitable and transparent method of allocating funding and determining the contributions that the NPO's should make from their own resources. The methodology that is proposed in the report for the costing model seeks in the first place to determine the cost of providing a welfare service programme to a typical beneficiary for a year. Once this annual service cost per

beneficiary has been determined, it is multiplied by the number of beneficiaries serviced by a specific NPO to determine that NPO's annual service cost. In order to more accurately apply the general methodology explained above, factors that have an impact on the cost of providing welfare services should be identified and is referred to as costing factors. The total caseload of an NPO is then subdivided in such a way that cases within each group have the same costing factors. These are referred to as costing groups. As a starting point the eight sub-programmes within the department's programme two - social welfare services, referred to in paragraph [8] of the judgment of 5 August 2010, are each regarded as a costing group. It is stated that the NPO's will be invited to make representations in respect of the finalisation of the costing groups.

[7] The annual service cost per case for each costing group, will then be determined. It is stated in the papers that these costs will be determined through a costing study to be carried out by KPMG and that there will be objectively justifiable data to justify the amounts and that these will be reasonable unit costs. These costs will also be determined

by taking into account representations of the NPO's. The annual service cost per case belonging to a specific costing group is multiplied by the number of cases in the caseload of an NPO within that costing group. The result is the annual service cost of the NPO for that costing group. This calculation is repeated for all other costing groups that make up the NPO's total caseload. The annual service cost for all the costing groups are then aggregated to determine the total annual service cost for the NPO.

[8] Having determined the total annual service cost per NPO, the aggregate of the funding cost of all the NPO's can be determined. The next step is to determine which NPO's can reasonably contribute to their funding costs and to what extent. On the basis that the total NPO funding costs exceed the budget available to the department to fund the NPO's, a formula is proposed which in its simplest form can be stated as:

$x = (A – B) \div C$

[9] In this formula A is the total annual costs of the services provided by the NPO's calculated as described above, B is

the total annual budget available to the department for the funding of these services provided by the NPO's and C is the total own funds of the NPO's reasonably available to contribute to the services provided by the NPO's. When x is multiplied by 100, it provides the percentage that each NPO that is able to contribute to the cost of the services provided by it, is to contribute from the amount reasonably available from own funds to contribute thereto. Thus, if A is R100 million, B is R60 million and C is R50 million, x will be 0.8. When multiplied by 100 the result is 80%. Therefore an NPO that has funds reasonably available to contribute to the cost of the services provided by it, will be required to contribute 80% of those available funds.

[10] The KPMG model therefore essentially calculates the costs of the services to be provided by the NPO's in terms of the costing model and makes use of the formula to determine the distribution of the budget available for this purpose. Two very important aspects of the model must however be kept in mind. The first is that in no instance will the annual cost of providing the service by the NPO be subject to reduction in calculating the allocation to it by the department. In the case

where an NPO is unable to make a contribution to the cost of the services provided by it, it will be allocated the full cost of the services as calculated above. Also, in the case where an NPO can contribute to the cost of the services provided by it, it will only be required to make a contribution to the total cost of the service provided as calculated, so that the balance will be provided by the allocation by the department. The second is, as is expressed clearly in the KPMG report, that the formula is subject to the constraint that x is equal to or less than 1. This will be the case only if B + C is equal to or more than A, that is if the total budget available for transfer to NPO's and the NPO funds available to contribute to the services provided by them, equal or exceed the total costs of provision of the services by the NPO's. In these respects the KPMG model is inconsistent with the revised version of paragraph 11.6 of the policy, as will be shown below.

[11] As a result of suggestions made during argument and at the invitation of the court, both the applicants and the department subsequently filed proposed revisions of paragraph 11.6 of the policy. The revised version filed by the department, referred to as "the revision", is the following:

"11.6 **Financial assessment of service plans**

11.6.1 Applications for state funding of social welfare service programmes (service plans) will only be considered if they pertain to one of the recognized social welfare service sectors (sub-programmes) identified in the first schedule.

11.6.2 The financial appraisal of all service plans which qualify for funding in terms of this policy will be performed in accordance with the principles and procedures set out in paragraphs 11.6.3 to 11.6.14 below.

11.6.3 The appraisal will be based on the reasonable annual cost per case of providing the applicable social welfare service, which the Department has calculated having regard to the reasonable unit cost ("benchmark cost") of each of the items of expenditure that is normally and ordinarily incurred for that purpose.

11.6.4 The appraisal will be conducted in accordance with the costing models contained in the second to ninth schedules, each of which:

11.6.4.1 the Department has compiled, having regard to the normal and ordinary items and expenditure that are incurred for that purpose;

11.6.4.2 is applicable to one of the recognized social welfare service sectors identified in the first schedule.

11.6.5 The appraisal will be conducted in two stages.

11.6.6 The first stage will be the provisional determination of the financial award done by:

11.6.6.1 firstly, determining the benchmark amount, which is done by multiplying the benchmark cost as determined in accordance with the applicable costing model, by the number of beneficiaries to whom the relevant programme will deliver social welfares services;

11.6.6.2 thereafter, deducting from the benchmark amount that which the service provider is reasonably able to contribute towards the costs it will incur in rendering the services it has applied to perform. The amount which the service provider cannot itself contribute will be determined by the Department after consultation with the service provider concerned and will take into account, inter alia the service provider’s service plan (submitted in accordance with paragraph 10 of this policy) and its financial statements for the preceding fiscal year. At the time of submitting its application for funding and its service plan and financial statements, the service provider may make representations in writing in support of its application.

11.6.7 The second stage will be the final determination of the financial award.

11.6.8 The financial award so determined will be commensurate with the costs which the service provider concerned will incur in rendering the services it has applied to perform as determined in accordance with the applicable costing model or models.

11.6.9 The provisional awards so determined will further be subject to adjustment by an appropriate percentage, if necessary, to provide the final awards of all programmes to which subsidies have been allocated to ensure that the aggregate of the approved financial awards do not exceed the funds allocated to the Department for transfer to the service providers rendering the relevant social welfare services.

The appropriate percentage will be determined in respect of each service provider separately, taking into account the prioritization of services or activities within the service after consultation with the relevant service providers.

11.6.10 The financial appraisal performed in terms of paragraphs 11.6.2 to 11.6.9 will be based on the principles set out in paragraphs 11.6.11 to 11.6.14 below.

11.6.11 The Department has a statutory and constitutional obligation to achieve, within its available resources, the progressive realization of the applicable socio-economic rights, which it must fulfill by striving to progressively increase the resources available for the provision of social welfare services.

11.6.12 The costing model in relation to each application may be based on the specific requirements of the services to be rendered, and that part of the income available to service providers to contribute towards the costs of rendering the service.

11.6.13 It is recognized that whilst the Department strives and will continue to strive to fund the provision of social welfare services to the maximum extent possible, its objective being to ensure that its financial awards will eventually cover the full cost of service, the limited resources at its disposal presently preclude it from covering the full cost thereof.

11.6.14 Financial awards will, in order to facilitate forward planning and budgeting, be approved for a minimum period of three financial years, with the approval in respect of the second and third years being provisional.

11.6.15 The costing models and benchmark unit costs contained in schedules two to nine will be reviewed, and if necessary revised, annually by the Department's provincial office (Public Private Partnership Sub-directorate), pursuant to it having considered inputs received from the sub-directorates responsible for each of the identified social welfare service sectors and service providers."

[12] The revision is clearly work in progress. The first question is whether what is envisaged by the revision complies with the judgment and order. I do not concern myself with issues of proper language and logical sequence of sub-paragraphs of the revision. I do however constantly remind myself that it is not for the court to devise a policy.

[13] Upon analysis of the revision, with the exclusion of paragraph 11.6.9 thereof, the following is apparent. In paragraph 11.6.11 it is recognised that the department has a constitutional and statutory obligation to achieve within its available resources the progressive realisation of the

applicable socio-economic rights, which it must fulfil by striving to progressively increase the resources available for the provision of social welfare services. In paragraph 11.6.13 it is stated that whilst the department strives and will continue to strive to fund the provision of social welfare services to the maximum extent possible, its objective is to ensure that these financial awards to NPO's will eventually cover the full costs of the services provided by the NPO's. Furthermore it is clear from paragraphs 11.6.3, 11.6.4, 11.6.6.1 and 11.6.8 that the idea is to determine as benchmark amount, the reasonable total cost of provision of the particular service, in other words, an amount that will enable an NPO to actually provide the social service concerned from this source only. It is proposed that from this amount should be deducted the amount that the NPO is reasonably able to contribute towards the benchmark amount. This reasonable contribution will be determined in consultation with the NPO during which process the NPO will be able, for instance, to show that certain funds available to it are earmarked for other purposes or for one or other reason not reasonably required or available to contribute towards the provision of the particular social service. The provisions that applications for state funding of social welfare service programmes will only be considered if they pertain to one of the recognised social welfare service sectors (para 11.6.1), that the costing model in relation to an application may be based on the specific requirements of the services to be rendered and that part of the income derived therefrom available to the NPO to contribute towards the cost of rendering the service (para 11.6.12), that in order to facilitate forward planning and budgeting, financial awards will be approved for a minimum period of three financial years albeit that the approval in respect of the second and third years will be provisional (para 11.6.14) and that the costing models and benchmark unit costs will be reviewed annually having regard *inter alia* to inputs by the NPO's (para 11.6.15), appear to me to be eminently practical and reasonable.

[14] So far so good, one could say. The NPO's that fulfil the constitutional and statutory obligations of the department will be funded on the basis of the reasonable actual cost of providing the services, less what they can reasonably contribute to the cost thereof. This accords with the KPMG model, on the basis that the NPO's contribute 100% of the

funds that they have available for this specific purpose. But then follows paragraph 11.6.9.

[15] This provision is expressly intended to ensure that the aggregate of the approved financial awards do not exceed the funds allocated to the department for transfer to the NPO's rendering the relevant social welfare services. The operation of the policy as proposed to be amended is as follows: The service plans submitted by the NPO's in response to the service specifications are regarded as applications for funding. The department approves all the service plans that comply with the objective requirements stated in the policy. This necessarily results in the available budget being less than the cost of the execution of all the approved service plans. This in turn becomes a vicious circle because the more qualifying NPO's apply for funding by submitting service plans, the greater the deficit. However, in terms of the revision the total cost of the provision of these services by each NPO is calculated and from that is deducted the amount that can reasonably be contributed to that cost by the NPO. Having thus meticulously calculated which amount is actually needed by each approved NPO

(total cost less own contribution, if any), this amount is then reduced by what is termed "an appropriate percentage". This may result in a very substantial reduction. The KPMG report points out that in the 2010/2011 financial year the actual awards made were 49% less than those recommended.

[16] I appreciate of course that the policy should contain a mechanism to allocate an insufficient budget. This mechanism must however be reasonable. Paragraph 11.6.9 as presently framed is not a reasonable measure. It appears to me to be illogical and irrational.

[17] This may be illustrated by the following example. An NPO operates a registered child and youth care centre for 20 children in a poor section of the community. It will be remembered that all children in child and youth care centres are children found by a children's court to be in need of care and protection and placed in a child and youth care centre by order of the children's court. In terms of section 193 of the Children's Act the MEC of a province must provide and fund child and youth care centres. The sub-programme child care

and protection services is by far the largest sub-programme in the department's programme two: social welfare services. These children are therefore constitutionally and statutorily the charges of the department. Say the appropriate benchmark cost amounts to R4 000,00 per child per month and that the benchmark amount per month is therefore R80 000,00 per month. The NPO has no funds available to contribute to these costs. Imagine now that the financial award allocated to the NPO is 49% less than the amount of R80 000,00 per month which the department itself calculated as the reasonable cost to care for these children. This gives rise to many questions. What is the NPO to do in the circumstances? How will the human dignity of the children be maintained? And what about their rights to equality, because they may suffer solely as a result thereof that they happened to be referred to the NPO's child and youth care centre and not, for instance, to one of the department's own institutions? Will this not result in the failure of the NPO's programme and resultant effective waste of the financial award to it?

[18] In terms of the policy the service specifications must be published by not later than 30 September of each year. The

deadline for submission of service plans by NPO's in respect of the service specifications for the 2010/2011 financial year commencing on 1 April 2010, was 6 November 2009. In terms of paragraph 11.2.5 of the policy the appraisal of the service plans must be finalised within 60 days after the closing date for submission of service plans. The appraisal process must therefore be concluded by say the middle of January of the following year.

[19] By that time the department will for some time have had a very good idea of the budget that will be allocated to it for the fiscal year commencing on 1 April. The budget process commences already in approximately June of the preceding year. Its departure point is the so-called "Blue Book". The Blue Book contains details of the actual budgets for the previous three financial years, details of the budget of the current financial year and estimates of what the budgets will be for the ensuing three years.

[20] What happens then can be illustrated by what transpired in respect of the department's budget allocation in respect of the 2010/2011 fiscal year. Against the background of the

Blue Book the department made detailed submissions to both the provincial and national treasuries calling for and explaining the need for an increased budget allocation to it. In a letter dated 21 August 2009 the provincial treasury communicated to the department its initial allocation for the 2010/2011 to 2012/2013 financial years. This was regarded by the department as a "significant indication". Following further submissions by the department a further preliminary allocation for the same period was made to the department by letter dated 4 December 2009. Upon receipt hereof the department had the opportunity to adjust its allocations in order to fit its programmes within the parameters of the funds it was likely to receive. The department was advised of the final allocation for the 2010/2011 financial year on 25 February 2010. This document again not only contained the final budget allocation to the department for the 2010/2011 financial year but also contained estimates thereof for the ensuing two years. The final allocation for 2010/2011 was approximately 2,6% more than the initial allocation of 21 August 2009.

[21] During the appraisal process it will be determined what the

contributions are that could be made by the relevant NPO's. There is in any event no reason why the time frames in respect of service specifications or service plans could not be suitably adjusted. In the affidavit in terms of paragraph 6 of the order the department said that the appraisal process must be finalised by 1 April annually.

[22] The department should therefore be able to do proper planning and prioritisation in respect of publication of service specifications and/or appraisal of service plans. The draft new national policy states in this regard that service specifications will determine priorities for service delivery at either national or provincial level and will be informed by, amongst others, government priorities, relevant research, statistics, relevant community needs and priorities, the relevant demographics, including population, poverty levels, migration patterns and other social development indicators and integrated development plans and that service specifications will therefore determine where, to whom and for what purpose funding will be allocated. The department's constitutional and statutory obligations require planning and prioritisation. In so doing, even though this may require

some tough decisions, the department could justify in a manner consistent with the Bill of Rights as a whole, the effective funding of the prioritised services required from the NPO's, in accordance with paragraphs 11.6.6.1 and 11.6.6.2 of the revision. There is therefor no reason for the senseless procedures of approval of service plans that cannot be fully funded (albeit with the assistance of reasonable contributions by NPO's) and payment of palpably insufficient amounts to all approved NPO's.

[23] It follows that in my judgment it is irrational to deal with an inadequate budget as proposed in paragraph 11.6.9. Parapraph 11.6.9 in any event suffers from the deficiencies set out below.

[24] First, the determination of an adjustment by appropriate percentage in terms of paragraph 11.6.9 must be consistent with the Bill of Rights as a whole and must be fair, equitable and transparent. This is not at all the case at present. It is not possible to ascertain from the policy how the (downward) adjustment will be done. It intends to differentiate between NPO's in a manner that is altogether vague and uncertain.

The department says that the revision must be read with the KPMG report and that the department intends to implement the costing model and recommendations in the KPMG report. If this means that the model contained in the KPMG report is intended to be used, then the policy must say so. But paragraph 11.6.9 is inconsistent with the KPMG model as the KPMG model requires that the total own NPO funds available in respect of services delivered for the department together with the budget allocation for this purpose must at least be equal to the total amount of approved costs. In terms thereof no deduction is to be made from the benchmark amounts of the NPO's, so that NPO's that cannot make a contribution will receive the benchmark amount and NPO's that can, will within their means make contribution to the benchmark amount.

[25] Second, it is not difficult to see that because of paragraph 11.6.9 the whole process of funding of NPO's may culminate therein that the NPO's are unable to provide the services that the department requires them to do, properly or at all. That is precisely the uncontested evidence of the applicants. In order for a measure such as paragraph 11.6.9 to pass

muster, it must ensure that it is not self-defeating and that the reduction or appropriate percentage does not result in the service required by the department not being provided. In short, it must not result in merely paying lip service to the fundamental principle of funding that NPO's that care for children, older persons or vulnerable persons in need or provide statutory services fulfil the obligations of the department.

[26] I conclude therefore that the revision does not comply with the judgment and order of 5 August 2011. Counsel for the applicants proposed that in the event of such finding, the department should be directed, after consultation with the applicants, to table within 90 days a revised policy which meets the requirements of the judgment and order of 5 August 2010. The department raised no objection to this proposal as such and it appears to me to be sound.

[27] Intertwined in the affidavits filed by the applicants in terms of paragraph 4 of the order, an application for what was termed emergency relief is found. As I understand it, the relief claimed is that this court should order the department to pay

specific amounts of increased financial awards to specific institutions operating under the auspices of the applicants. At the hearing on 5 May 2011 this application was not moved. The temptation to consider whether this claim for relief has any prospect of success must therefore be resisted. But for the same reason the costs wasted as a result of the application for emergency relief, must be paid by the applicants. Costs of more than two counsel are not justified in this regard.

[28] The following orders are issued:

1. It is declared that the revised policy presented by the respondents in purported compliance with the judgment and order of 5 August 2010 in this matter, does not comply with that order.
2. The first and second respondents are directed, after consultation with the applicants, to within 90 days of this order file a revised policy which meets the requirements of the judgment and order of 5 August 2010.
3. Any party hereto may enroll the matter after a revised policy was filed.

4. Save for paragraph 5 below, the first and second respondents shall pay the costs of the application incurred since 5 August 2010, including the costs of two counsel.
5. The applicants shall pay the costs wasted by the deferment of the applicants' application for emergency relief, including the costs of two counsel.

C.H.G. VAN DER MERWE, J

On behalf of the applicants: Adv. J. Gauntlett SC
With him:
F. Pelser
Instructed by:
Phatsoane Henney Inc.
BLOEMFONTEIN

On behalf of the first and second respondents: Adv. C.G. Marnewick SC
With him:
N. Singh SC and C. Human
Instructed by:
The State Attorney
BLOEMFONTEIN

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