

July 28, 2006

To the Secretariat:

Please find attached my thoughts on the discussion document prepared by the Task Team dated July 14, 2006. I appreciate the Task Team's attentions and hope the Task Team finds them valuable.

I am not interested in making an oral presentation at this time.

Please acknowledge receipt of this email.

With respect and good wishes,

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copy to: Pat Davies, CEO, Sasol Limited

By way of introduction, I am 82 years old. Degrees from the Universities of Saskatchewan, Toronto, and Chicago. Economics specialty, but broadly educated. Taught economics at Vanderbilt University for 2 years. Entered the investment industry in 1953. Career – always as a generalist. Worked at brokerage research to 1966. Then managed 3 mutual funds (combined value \$150 million) in Montreal (1966-1970). Major experience in Japanese equities market (1967-1975). Travels – Japan, Europe, Australia, United States, and as a tourist – South Africa (1996).

Now living in Toronto since 1971. I have had mutual funds to manage for Commercial Union and Bank of Nova Scotia for a few years, always as a contractor. Investment consultant for the past 35 years. Founding trustee of The Fraser Institute and a member of the CD Howe Institute – both prominent think tanks in Canada. In the 1970s and 1980s, Associate Editor of the Financial Analysts Journal. Have published several articles and past Director of the Montreal Financial Analyst Society and the Toronto Financial Analyst Society.

Started my family Charitable Foundation in 1978. My wife and I have also supported the University of Toronto. We have both been honoured with LID's.

## **The Task Team**

I have read with keen interest the whole text of the Task Team's discussion document. The document details the history of Sasol's establishment, role, and many policies and business interfaces with government and the general public and cannot be other than confusing. The result, I believe, will mean that minds of members of the Task Team, let alone outside readers, may end up pretty much unchanged and/or confused because of the multitude of factors thrown up for consideration. Rather than getting embroiled in the detail, I will take a rather philosophical tack.

## **MY POSITION AS AN INVESTOR**

In recent years, I have believed that South Africa was generally misunderstood in many respects. It has distinguished itself in the African continent by the range of its institutions - a parliament, well managed elections, a Party in power which has been adept at recognizing and adapting to an evolving political scene – so far. The range of institutions includes a supreme court, a court system, an auditor general, and a civil service that is effectively implementing policy on many fronts –taxation, education, property rights, public works, postal system. These things are a blessing to South Africa. To its credit, the country has also in many ways assumed responsibilities in the continent well beyond its self-interest, narrowly defined.

As for Sasol, its management has taken the Company, with its 30,000 employees, to a prominent position in South African industry, plus its strong reputation with partners in diverse settings – Nigeria, Europe, Qatar, Iran, United States and now China. Many people think of the Company far too narrowly – mainly as a liquid fuels producer from natural gas and coal. Indeed, it is also a producer of a range of chemicals which find their way into many, many products and countries of the world. So, with my belief that South Africa was unappreciated for its progress on many fronts and a classy world company, I had my case as a shareholder of Sasol. That case is now, however being severely tested by the Government's decision even to think of windfall taxes as a potential policy step.

Page 94 of the Task Team's discussion document includes the idea that in the face of an embargo, Sasol was established and financed to help develop needed energy and that now it may, with handsome earnings, properly be expected to “repay” for past financial support. Perhaps, to be fair, it may be claimed that Sasol should be “paid back” by being helpful in the country's time of need.

My surprise at the Government's move in February derived in part from a conviction that Nelson Mandela's demonstrated character in letting “bygones be forever bygones” had already provided a lasting model. Nevertheless, I am sure that the mode of his life after incarceration for 27 years will continue to have an enormous influence on the still developing renaissance of South Africa. I was premature in my judgment as to how far along South Africa had come. Obviously, there is still much work to be done.

## **Profits and Losses - Costs and Prices – Some Comments**

Profits (and losses) can be viewed mainly as effects. Given costs of production in the field of commodities, profit fluctuations in the short run derive from price fluctuations in the prices of commodities and their inputs. A company can plan for profits, but properly, it cannot plan profits. Companies typically do their best, decision by decision, to behave so that the present value of the company, not to be confused with the share price, is maximized. Strictly speaking, profits are an unwitting byproduct of a company's struggle. This line of argument will come as a shock to those who would have us believe that profits derive from the greedy entrepreneur gouging the hapless customer. "Gouging" and "hapless" cannot properly be part of the lexicon in business. Competition prevents them.

Well, if prices and profits are effects, what is the cause of those effects? The short answer is varying pressures of demand on supply. These pressures wax and wane. When demand waxes, prices on that account will increase. Of course, when supply is reduced for any of a multitude of reasons, the pressure of demand will win out and prices will rise – other conditions unchanged.

### **A Case For Windfall Profits Taxes?**

When prices and profits are wandering around because both demand and supply are wandering, who is to blame when profits wander? Understanding this brings into question the very concept of "windfall". Are all changes windfalls? The price system is there to do away with such judgments. The South African constitution prohibits discrimination that, I understand, includes discrimination as between companies and industries. Government is there to generate rules for market place behavior and the courts and police are there to enforce them.

In view of the above, I find the merits of all of the four mechanisms to address anticipated "windfall" profits (page 87) to be nil. The ordinary corporate income tax for all corporations should suffice. Once going down the windfall track, who would be safe from whim, even retroactive whim? In any case, all four options would involve an additional layer of regulation and costs!

### **Note On Corporate Income Taxes**

All income taxes distort behavior as avoidance schemes of great variety develop and have costs to administer which bear on government, taxpayer, and the general public. This is not to advocate abolition of all income taxes. Personal consumption taxes should be an important source of revenue. As practical and philosophical matters, finance departments get revenues where they can while doing as little damage as possible to productivity while minimizing criminal activity in the form of evasion. I abstract from the urge in politicians to bear down on finance departments in efforts to get reelected.

All changes in rules and tax rates are costly. All changes in prospects for change are costly. Total costs of change cannot be measured. Costs are spread far beyond the ken of both the payers and government. Adjustments of behavior to changes spread far and wide, even to those that would deny being affected.

### **Miscellaneous Observations**

I find the line of questioning on Page 91 to be particularly offensive. It deals with the deep past and constitutes a make-work fishing trip leading nowhere. It is heavy with innuendo, pettiness and an air of seeking to justify vengeance for alleged wrongs far in the past.

It is impossible to do one thing. This little sentence deserves pondering. The Task Team will discover that the current maze of taxation, subsidization, regulation, past deals and understandings is already a mess. Undoing messes will be costly and temporarily messy. This is not to discourage attempts to find needed undoings. Inter alia, the best ideas will get rid of bureaucratic fiefdoms in order to reflect the march of time and further expand freedom and productivity.

### **New Zealand – October 1984**

I was there. New Zealand's economy was a maze of controls. A new Labour Government had been elected. Roger Douglas was the new Finance Minister. Whenever I brought up the subject of New Zealand's economy, adjectives such as a mess, hopeless, a crock were mentioned. The situation was ripe for reform. Import duties, quotas, export subsidies, subsidized industries, taxes of great variety, groups of the citizenry given special treatment for many of life's deemed exigencies, etc. Douglas recognized that it was a hopeless mess. In short order he put forth his case to Cabinet that "hopeless" provided opportunity. He was told to go to work. Over night, he cancelled hundreds of practices that had been sanctioned in previous decades in the areas mentioned above and many not referred to. The astoundingly favourable results came so rapidly that doomsayers didn't have time to get out their shopworn prognoses of doom. Now, it will be said that South Africa's case is different. Properly understood, it is not.

### **An Opportunity**

Of far greater significance, even the proposal of a windfall tax is a blot on the escutcheon of South Africa in the eyes of much of the developed world's citizenry. The very proposal that such a tax should be considered is prima facie evidence of arbitrariness, opportunism, and industrial discrimination, combined with a serious lack of judgment. I venture that to call the whole thing off, especially if accompanied by moves to undo at least some of South Africa's current regulatory excesses, would be greeted by congratulations, especially in the financial and international political worlds. It would be a wonderful sign of magnanimity, flexibility and maturity. This is a fabulous opportunity for South Africa - enhanced by bringing up the subject of windfall taxes and rejecting the idea. Don't miss it!

With respect and good wishes,

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