

ESKOM'S REVENUE APPLICATION FOR 2018/19

Morné Mostert, Local Government
AfriForum



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Introduction

- AfriForum NPC (a non-profit company) registered in South Africa with, among other aims, constructive participation in matters of Government, such as the making of submissions regarding applications for revenue by Eskom on behalf of its members and in the public's interest).
- AfriForum has been active in the energy industry for various years by making submissions regarding applications for electricity price increases on Local Government level, as well as participating in various public hearings in this regard held by NERSA.
- Has more than 120 branches across South Africa that actively take part in service delivery issues including electricity supply.

Purpose of Submission

- To request that, to the extent that ESKOM has based its calculation of the allowable revenue on past expenditure which was *prima facie* incurred in contravention of the Public Finance Management Act (“PFMA”), the Electricity Regulation Act (“ERA”), the Prevention and Combating of Corrupt Activities Act (“PRECCA”) and the Companies Act, that calculation of the allowable revenue be adjusted so that these expenditure items are not factored into the calculation of the allowable revenue.
- To request that, to the extent that ESKOM has based its calculation of the value of the Works Under Construction (“WUC”), which contributes towards the value of the Regulatory Asset Base (“RAB”), on past expenditure which was *prima facie* incurred in contravention of the PFMA, the ERA, the PRECCA, and the Companies Act, that calculation of the allowable revenue be adjusted to exclude these unlawfully incurred expenditure items from the value of the WUC, and therefore from the value of the RAB.

Purpose of Submission(2)

- To request that, to the extent that NERSA is unable to effectively investigate any or all of these submissions and dispose thereof (make definitive findings) for purposes of this revenue application, that the respondents be informed thereof timeously so that this matter can be investigated, mediated or disposed of in terms of section 18 or section 44 of ERA or other appropriate courses of action can be considered.

Allowable revenue

- The MYPD establishes the following criteria for the operating expenses to be allowed:
 - Expenses must be incurred in the normal operations of production and supply of electricity, including an acceptable level of refurbishment, repairs and maintenance costs;
 - Expenses must be prudently and efficiently incurred after careful consideration of available options;
 - Expenses must be incurred in an arm's length transaction. ESKOM must have a competitive procurement policy and demonstrate to the regulator that it has been strictly adhered to in its procurement processes;
 - For any exogenous factors, expenses incurred under extraordinary circumstances consideration shall be given to spreading such expenses over a number of years;
 - Only the efficient human resources will be allowed;
 - Corporate social investment and expenses on charitable donations and broad social development activities however they cannot be included as qualifying (regulated) expenses and would need to be funded from below the bottom-line or by the shareholder;
 - Expenses on advertising not related to the core business of supplying electricity will also be disallowed;
 - Costs of special characters that are allowable in the revenues include primary energy, research and development costs for regulated activities, transmission service quality incentives, transmission supply quality incentives or system minutes, distribution service incentives and Energy Efficiency and Demand Side Management (EEDSM).

Allowable revenue(2)

- The MYPD establishes the following criteria for the operating expenses to be allowed:
 - Expenses must be prudently and efficiently incurred after careful consideration of available options;
 - Expenses must be incurred in an arm's length transaction. ESKOM must have a competitive procurement policy and demonstrate to the regulator that it has been strictly adhered to in its procurement processes;
 - **In Parliament it was stated that Eskom has had deviations of the Supply chain management procedures worth R31.1 Billion**

Allowable revenue(3)

- In making an argument for the exclusion of these expenditure items or exclusion of these values, we posit that:
 - ESKOM has an obligation to only incur **lawful** operational and capital expenditure in execution of its licensed activities;
 - NERSA has the legal authority to **exclude** from the calculation of the allowable revenue operational or capital expenditure which has been **unlawfully** incurred, and any decision taken by NERSA which allows for ESKOM to effectively recover unlawfully incurred expenditure through end user tariffs, will in itself be unlawful and *ultra vires*.
 - There are various instances in which a *prima facie* case of unlawfully incurred operational and capital expenditure has been incurred;
 - The unlawfully incurred operational and capital expenditure should therefore be excluded from the calculation of the allowable revenue for the 2018/2019 financial year;

Allowable revenue(4)

- The expenditure or values which we allege are likely to have been incurred in contravention of the aforementioned legislation is:
 - The unlawful prepayment of R659 million made by ESKOM to Tegeta Exploration (Pty) Ltd (“Tegeta”); [41-62]
 - The unlawful reduction of the contractual penalty inherited by Tegeta through the purchase of Optimum Coal; [63-67]
 - The unlawful payment of a long term executive bonus to all the executives, *alternatively* of the R711 000.00 bonus to Matshelo Koko, the suspended acting Chief Executive Officer (“CEO”) and former head of generation at ESKOM; [88-95]
 - The unlawful payment of R1.6 billion to McKinsey and Trillian Capital in terms of a void contract that was entered into in contravention of the PFMA; [68-79]

Allowable revenue(3)

- The expenditure or values which we allege are likely to have been incurred in contravention of the aforementioned legislation is:
 - The unlawful payments made to Impulse International, who was appointed contrary to the PFMA and Companies Act; [80-87]
 - The cost overruns on Medupi, Kusile and Ingula Power stations that can be attributed to irregular, unauthorised, wasteful and fruitless expenditure (in contravention of the PFMA); [96-113]

Strategy

- The submission made by AfriForum forms part of a longer-term strategy to constructively participate in matters relating to energy affairs, by among other doing the following:
 - Demanding more transparency from Eskom, NERSA, the Department of Energy and the Department of Public Enterprises, through the use of various legislated mechanisms and forums, such as the Promotion of Access to Information Act, 2000 (Act No 2 of 2000), the Human Rights Commission, as well as the NERSA and other criminal and civil procedures;
 - Investigating and challenging corruption and maladministration within Eskom through exposure and litigious as well as non-litigious avenues; and
 - What can be crystallized from the above sections is that NERSA has a duty to ensure that decisions made by the regulator, when regulating applications for electricity tariffs, have been made in a manner so that the foreseeable effects of the decision serves the objects of the ERA and is within powers and in accordance with the duties of NERSA as a regulator as well as the individual members, as set out in ERA.

Conclusion

- This submission aims to ensure that unlawful expenditure incurred by Eskom is not passed on to consumers by way of this application for an electricity tariff increase.
- That Nersa fulfils its mandate by regulating the management of energy and its tariffs by using mechanisms and remedies at its disposal to ensure efficient, economic and effective use of resources, as set out in the Constitution.
- Advocating for the efficient and effective decentralisation of generation, distribution and transmission activities from Eskom to independent power producers, distributors and transmitters



 **AfriForum**

Thank you

