Eskom Regulatory Clearing Account (RCA) year 5 of MYPD 3

Public Hearings- Rustenburg

Date: 28 January 2019

RCA (Yr 5, MYPD3) Timeline

Eskom

RCAs require 3 decisions:

1 Balance decision

2 Liquidation decision

3 Reasons for decisions

RCA Year 5, MYPD 3

31 March 2018
End of financial year

1
14 June 2018
NERSA decision on Yr 2,3,4 RCA balance

12 September 2018
Submitted to NERSA

2
2 October 2018
NERSA decision on Yr 2,3,4 RCA liquidation

19 October 2018
NERSA publishes RCA (Yr 5) for comment

30 November 2018
Closing date for written comments

3
7 December 2018
NERSA reasons for decision on Yr 2,3,4 RCA balance

14 January 2019
Start of public hearings

The Regulatory Clearing Account (RCA) is the regulatory mechanism for risk management

RCA is a balancing mechanism between what was awarded by NERSA on the basis of a forecast (MYPD), and what actually materialised (Eskom's audited financial statements) - a backward looking reconciliation

NERSA Framework:

1. Differences materialise if Eskom either does not achieve or exceeds the awarded revenue (due to pricing or demand factors), or incurs costs greater or lower than those which were taken into account when NERSA calculated the MYPD allowable revenue

2. RCA balance could either be in favour of Eskom or consumer

3. RCA is subject to approval by the Regulator

4. Liquidation of the RCA as approved by the regulator may result in an increase or decrease in future electricity prices

5. The MYPD Methodology as published by NERSA in December 2012 is applicable to the MYPD3 control period

The RCA is a globally accepted regulatory principle and is part of RCA best practices; MYPD2 RCA decision made in 2014 and MYPD3 RCA Year 1 (2013/14) made in 2016. The RCA balance decision for FY2015, FY2016 and FY2017 was made in June 2018.

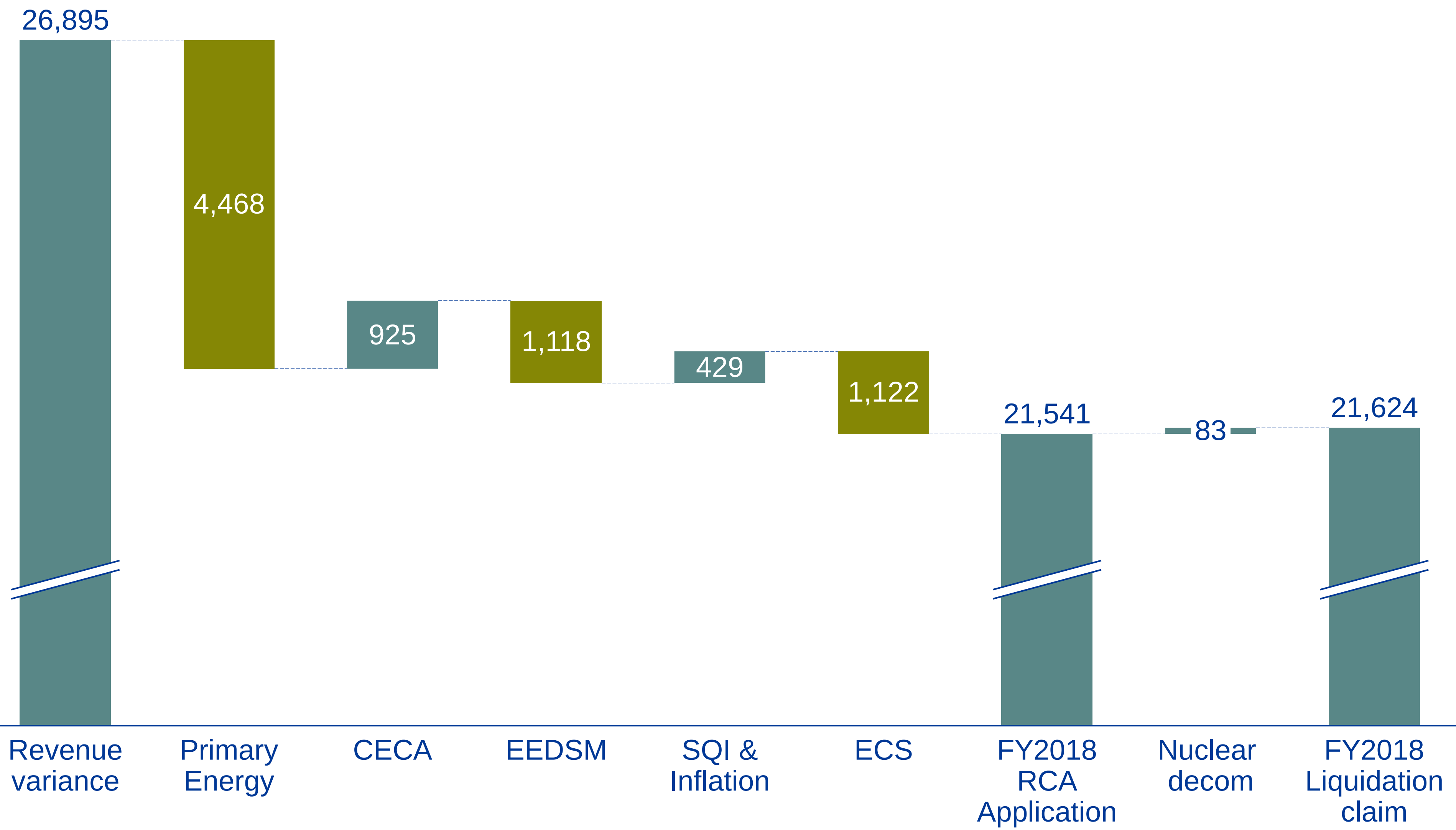
RCA Year 5 of MYPD 3 balance application

- RCA submission is **based on MYPD3 Methodology decision and reasons for decision for MYPD 3 RCA 2013/14**
- Is **driven substantially by revenue under-recovery due to lower sales** as assumed in the MYPD 3 decision for FY 2018..
- The determined **RCA application of R21 541 million** is **motivated with facts and evidence** to enable prudency assessments by NERSA
- Cost variances relate predominantly to **primary energy costs** which **off-set the revenue variance** related to sales
- **Opex variances are not included in RCA as it is not re-measurable** in terms of the MYPD 3 methodology (has been changed in revised methodology)
- **Energy Conservation Scheme** (ECS) adjustments **~ R1 100 million** of sales variance
- Nuclear spent fuel decommissioning costs of R830 m incurred in 2013/14 approved for recovery over 10 years resulting in R83m being included in the total RCA claim for liquidation purposes of R21 624 million (i.e R21 541m + R83m)

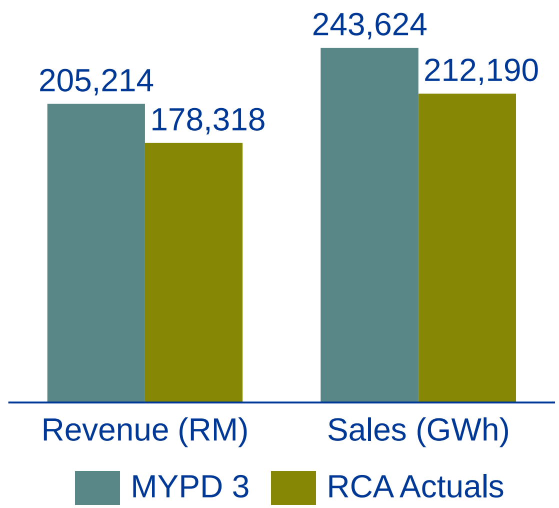
MYPD Year 5 RCA application: Revenue variance makes up majority of the balance

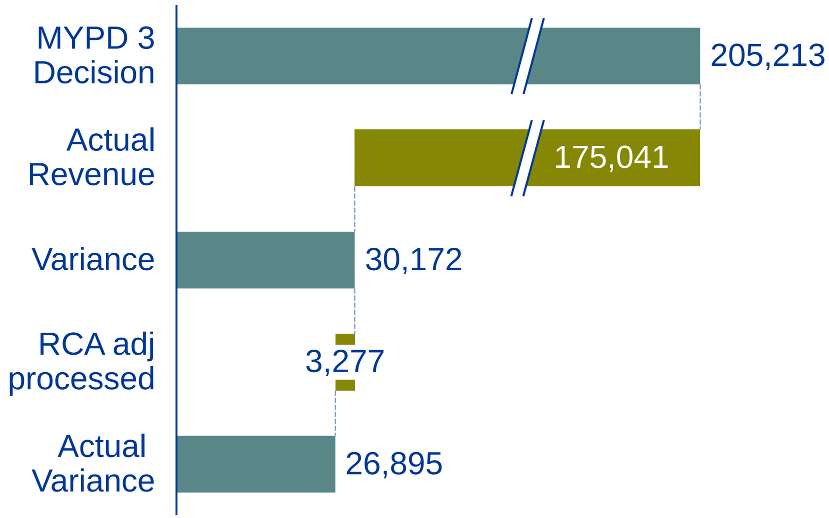
RCA for 2017/18 (Year 5 of MYPD3)	MYPD3 Decision	Actuals 2017/18	Variance to MYPD3	RCA adjustments	RCA 2017/18
Total Revenue R million	205 213	175 041	30 172	-3 277	26 895
Primary Energy , R million					
Coal	49 914	46 992	-2 922	-15	-2 937
Open Cycle Gas Turbines (OCGTs)	1 724	328	-1 396		-1 396
Other primary energy	6 766	7 576	810	-	810
Independent Power Producers	23 018	19 317	-3 701	1 983	-1 718
International Purchases	470	2 768	2 298		2 298
Environmental levy	9 746	8 061	-1 685		-1 685
Demand Market Participation (DMP)	-	160	160		160
Total primary energy , R million	91 638	85 202	-6 436	1 968	-4 468
CECA for RCA , R million	33 667	34 592	925	0	925
EEDSM for RCA , R million	1 244	142	-1 102	-17	-1 118
Operating costs for RCA , R million	47 764	51 892	4 128	-4 128	-
SQI for RCA , R million				390	390
Inflation adjustments , R million				39	39
ECS (Electricity conservation scheme) adjustment				-1 122	-1 122
FY2018 RCA application for year					**21 541**
Nuclear decom - RCA 2013/14 phased 10 years for liquidation					83
FY2018 Liquidation claim , R million					**21 624**

Summary of RCA 2017/18



Electricity sales volumes continue to remain lower than that assumed by NERSA in the MYPD 3 decision





Eskom's electricity revenue is derived from 3 customer categories:

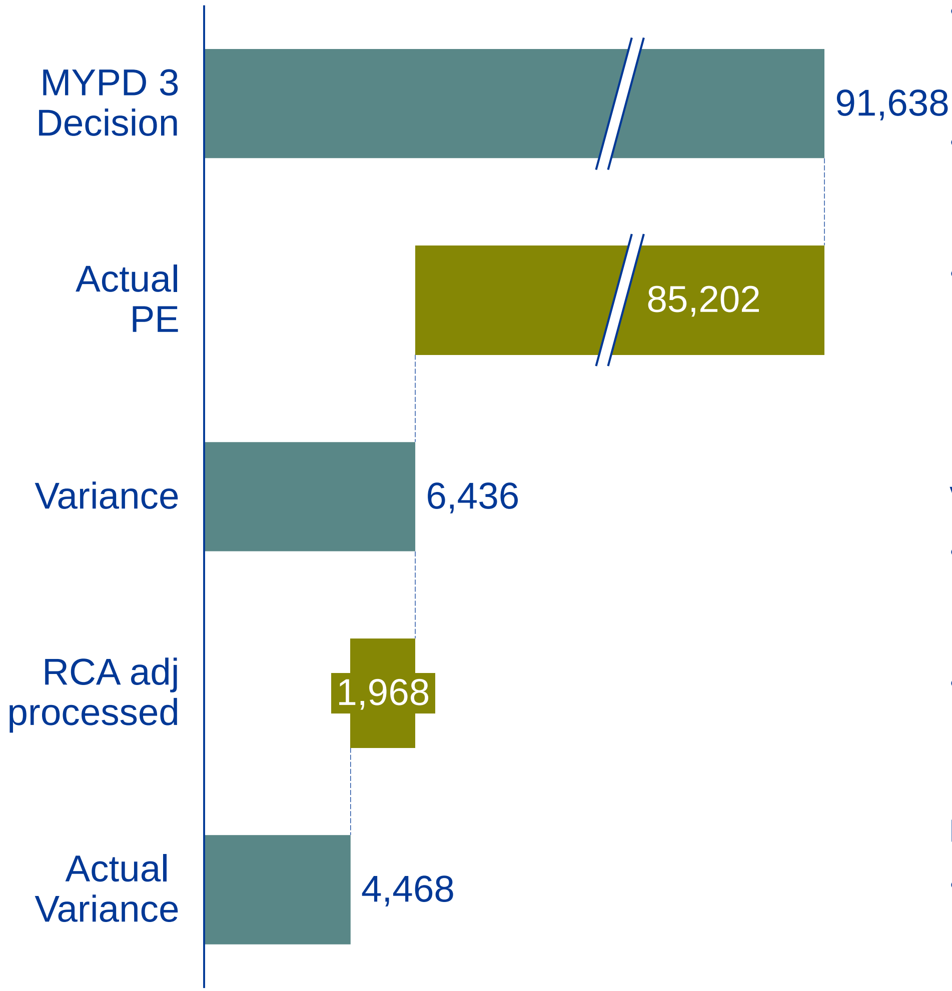
1. standard tariffs
2. local negotiated pricing agreements
3. exports (international) customers

Revenue variance of R30 172m in AFS is adjusted by R3 277m to account for revenue impairment resulting in a RCA revenue adjustment of R26 895m. Thus RCA includes all billed revenue (not collected revenue as in AFS)

The drivers for the declining sales trend include:

- **Weakening markets –** oversupply and high stock levels; low commodity prices; environment that favours cutbacks over growth.
- **Low growth and low infrastructure spend in SA –** projects (sales growth) being delayed or cancelled; inadequate infrastructure and policy/regulatory uncertainty
- **Increasing prices** – Energy efficiency improvements; closures due to competitiveness and profitability; reduced peak / high season usage; increased use of own generation.
- **Deteriorating electricity supply performance (maintenance and restoration)** – poor quality and reliability of supply causing plant stoppages.

Eskom has aligned the treatment of primary energy to the NERSA 2013/14 RCA decision



Variances in favour of consumer:

- The coal burn variance of R2 937 million is a result of lower electricity production, lower production from cost-plus and fixed price mines, delays in coal quality improvement.
- The energy availability of Eskom fleet, commissioning of new power stations and usage of IPPs have resulted in lower usage of OCGT and a variance of R1 396 million
- Eskom utilized 64 GWh more energy from IPPs when compared to the MYPD3 decision in 2017/18, but due to lower average costs the results was R1 718 million less spent on IPPs compared to the MYPD3 decision.

Variances in favour of Eskom:

- Eskom acquired electricity from neighboring countries that resulted in an international purchases variance of R2 768 million
- Variances of R160 million for Demand market participation (DMP) costs and R810 million for other primary energy costs

RCA Adjustments include :

- DoE peakers - where capacity charge for RCA is recovered in same year as expenditure is incurred whereas in AFS in accordance with IFRS, it is capitalised over term of PPA

Other categories contributing to the RCAs

CECA for RCA , R million	925
EEDSM for RCA , R million	-1 118
SQI for RCA , R million	390
Inflation adjustments , R million	39

- **Capital Expenditure Clearing Account** (CECA) - Variance is attributable to higher costs incurred for new build projects, outage capital costs and partially reduced by lower expenditures incurred for Transmission and Distribution networks; following Eskom's capital expenditure reprioritisation process.
- **EEDSM** programs produced less verified capacity savings during year, than determined by NERSA, resulting in variance in favour of the consumer
- Eskom has exceeded **service quality incentive** targets set by NERSA for Distribution and Transmission during 2017/18. This resulted in Distribution achieving an SQI of R292.8 million and Transmission of R99.7 million
- **Inflation adjustment-** On opex is due to higher inflation rate in actual mode versus that assumed by NERSA in MYPD 3 decision.


THANK
YOU!