

Decision

On 27 August 2015, the National Energy Regulator of South Africa (“NERSA” or ‘the Energy Regulator’) approved:

1. A trading margin of R8.69/GJ for the period 01 July 2015 to 30 June 2016 and R8.97/GJ for the period 01 July 2016 to 30 June 2017;
 2. That the actual cost of debt be subjected to an independent verification and if necessary, it may be clawed back in the next trading margin;
 3. A discount must be applicable to all traders (all resellers of gas including distributors and reticulators) equivalent to 50% of Sasol Gas’ trading margin;
 4. That discounts are allowed and must be applied in accordance with the non-discrimination provisions of section 22 of the Gas Act, 2001 (Act No 48 of 2001); and
 5. That the trading margins are applicable for the period 27 August 2015 to 30 June 2017, and will remain in force until the date the Energy Regulator approves new trading margins.
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Reasons for Decision

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Reasons for Decision

1. APPLICABLE LAW

- 1.1 The legal basis for the National Energy Regulator of South Africa (“NERSA” or “the Energy Regulator”) to regulate prices of piped-gas is derived from the National Energy Regulator Act, 2004 (Act No. 40 of 2004) (‘the National Energy Regulator Act’), read with the Gas Act, 2001 (Act No. 48 of 2001) (‘the Gas Act’).

2. BACKGROUND

A. The Methodology to Approve Maximum Prices for Piped-Gas in South Africa (2011)

- 2.1 In terms of section 4(g) of the Gas Act, the Energy Regulator must, as appropriate, in accordance with this Act regulate prices in terms of section 21(1)(p) in the prescribed manner.
- 2.2 Section 21(1) (p) of the Gas Act prescribes that the Energy Regulator may impose licence conditions within the following framework of requirements and limitations: ‘maximum prices for distributors, reticulators and all classes of consumers must be approved by the Gas Regulator where there is inadequate competition as contemplated in Chapters 2 and 3 of the Competition Act, 1998 (Act No. 89 of 1998)’.
- 2.3 The essence of section 4(g), therefore, is that when the licensee holds a licence that contains a condition in terms of section 21(1)(p), then such licensee’s maximum prices must be approved by the Energy Regulator in the prescribed manner where there is inadequate competition.

2.4 Regulation 4 of the Piped Gas Regulations, 2007 (published under Government Notice No. R. 321 in *Gazette* No. 29792 on 20 April 2007) (“Piped Gas Regulations”) dealing with the price regulation principles and procedures provides as follows under sub regulation (3) and (4), respectively –

2.4.1 that the Energy Regulator must, when approving the maximum prices in accordance with section 21(1)(p) of the Act, *inter alia* be objective based on a systematic methodology applicable on a consistent and comparable basis; and

2.4.2 that the maximum prices referred to in sub regulation (3) must enable the licensee to –

(a) recover all efficient and prudently incurred investment and operational costs; and

(b) make a profit commensurate with its risk.

2.5 In line with this particular requirement, the National Energy Regulator has developed the Methodology to Approve Maximum Prices of Piped-Gas in South Africa, 2011 (‘the Maximum Pricing Methodology’ or ‘the Methodology’). The Methodology is available on the National Energy Regulator’s website at www.nersa.org.za.

B. Determination of Inadequate Competition

2.6 Approving maximum prices and the use of the Methodology are contingent on the National Energy Regulator determining that ‘there is inadequate competition as contemplated in Chapters 2 and 3 of the Competition Act, 1998 (Act No. 89 of 1998) (“Competition Act”)’.

2.7 Therefore, for the National Energy Regulator to regulate maximum prices of piped-gas, it must be of the view that there exist market conditions or market features indicating inadequate competition in line with the provisions of Chapters 2 and 3 of the Competition Act.

- 2.8 The determination of inadequate competition contemplated in section 21(1) (p) of the Gas Act is made by the Energy Regulator outside of this methodology from time to time. The determination of inadequate competition was approved by the Energy Regulator on 08 February 2012 and may be reviewed every three years.
- 2.9 The Maximum Pricing Methodology also provides for the determination of a trading margin, which is referenced to the Tariff Guidelines.

C. Relationship to the Tariff Guidelines

- 2.10 According to section 4(h) of the Gas Act, the Energy Regulator has a duty to *'monitor and approve, and if necessary regulate, transmission and storage tariffs and take appropriate actions when necessary to ensure that they are applied in a non-discriminatory manner as contemplated in section 22'*.
- 2.11 In order to implement this mandate, the National Energy Regulator developed the Guidelines for Monitoring and Approving Piped-Gas Transmission and Storage Tariffs in South Africa, 2009 ('the Tariff Guidelines'). The Tariff Guidelines are available on the National Energy Regulator's website at www.nersa.org.za.
- 2.12 Hence, the Tariff Guidelines give guidance on tariff-related activities, which are charges for gas services and which must be added to the piped-gas energy price(s).

D. The Piped-Gas Regulations

- 2.13 The maximum price determination principles outlined in the Maximum Pricing Methodology, are further informed by the Piped-Gas Regulations.
- 2.14 Sub-regulation 4(3) prescribes that the Energy Regulator must, when approving the maximum price in accordance with Section 21(1)(p) of the Act:

- a) be objective i.e. based on a systematic methodology applicable on a consistent and comparable basis;
- b) be fair;
- c) be non-discriminatory;
- d) be transparent;
- e) be predictable; and
- f) include efficiency incentives.

2.15 Sub-regulation 4(4) prescribes that the maximum prices referred to in sub-regulation 4(3) must enable the licensee to:

- a) recover all efficient and prudently incurred investment and operation costs; and
- b) make a profit commensurate with risk.

2.16 Sub-regulation 4(6) then requires that, when gas is sold, the accompanying invoice must itemise the constituent elements of the total price reflected on the invoice, including at least the cost of gas, and transport tariffs and any other charges.

2.17 Annexure A of the Regulations provides the definition of the classes of customers as classified by their annual gas consumption in Gigajoules as follows:

CLASS	ANNUAL GAS CONSUMPTION		
Class 1	Less than 400 GJ pa		
Class 2	401 GJ pa	to	4 000 GJ pa
Class 3	4 001 GJ pa	to	40 000 GJ pa
Class 4	40 001 GJ pa	to	400000 GJ pa
Class 5	400 001 GJ pa	to	4 000 000 GJ pa

CLASS	ANNUAL GAS CONSUMPTION		
Class 6	> 4 000 000 GJ pa		

2.18 These legislative aspects, as prescribed by the Gas Act are essential in defining the scope and nature of the Maximum Pricing Methodology developed by the National Energy Regulator.

Approving maximum prices of piped-gas

2.19 As the Maximum Pricing Methodology highlights, in approving maximum piped-gas prices:

- the National Energy Regulator will not set prices but will review maximum piped-gas price applications prepared by licensees or applicants;
- the National Energy Regulator may request licensees or applicants to amend maximum prices; and
- the National Energy Regulator may approve or decide not to approve maximum prices.

2.20 The process of piped-gas maximum prices application is as follows:

- The Energy Regulator has requested licensees or applicants to submit their maximum piped-gas price applications based on the Methodology approved by the Energy Regulator.
- To ensure consistency of applications and predictability of analysis of the applications, the National Energy Regulator has specified the following:
 - a) prescribed sources of information that must be used for the input variables in the maximum price calculations;
 - b) prescribed weights applied to energy price indicators; and
 - c) the Methodology to determine trading margins.
- Applicants must provide information regarding the assumptions as well as the details of the calculation.

2.21 This application must:

- be provided on an annual basis, although applicants are allowed to apply for approval of maximum prices for a longer or shorter period; and
- indicate the manner and frequency of price adjustment to be approved by the Energy Regulator.

2.22 The Methodology further states that, 'NERSA will periodically conduct reviews of approved prices to assess the impact and to verify whether the prices comply with the requirements of the Act and the Regulations'.

3. SASOL GAS TRADING MARGIN APPLICATION

3.1 On 05 June 2015, the Energy Regulator received a multi-year trading margin application from Sasol Gas Ltd ("applicant" or "Sasol Gas") for the periods 01 July 2015 to 30 June 2016 and 01 July 2016 to 30 June 2017. The trading margin application is attached as **Annexure B (*Annexure B – Sasol Gas trading margin application*)**.

3.2 This is an amended application of the trading margin application that was submitted on 03 March 2015. The Piped Gas Subcommittee of 18 May 2015 instructed Sasol Gas to amend its application because of differences in the WACC, RAB, expenses and claw back.

3.3 The first Sasol Gas trading margin was approved on 31 March 2013 for the periods 26 March 2014 to 30 June 2014 and for the period 01 July 2014 to 30 June 2015. The other component of the maximum price, the Gas Energy Price was approved in March 2014 (as a multi –year price) until 30 June 2017.

3.4 According to the Maximum Prices Methodology, an application is due four months prior to the start of the next maximum prices period. Before re-submitting this amended application for a trading margin, Sasol Gas had filed its application on 03 March 2015, within four months of the next maximum price period.

The applicant

- 3.5 Sasol Gas Limited (registration number 1964/006005/06) is wholly owned by Sasol Gas Holdings (Pty) Ltd (registration number 2000/013669/07), a limited liability company incorporated in terms of South African company law. Sasol Gas Holdings (Pty) Ltd is in turn a wholly owned subsidiary of Sasol Limited.
- 3.6 Sasol Gas is vertically integrated in the gas industry supply chain in South Africa, i.e. it is active in gas transmission, gas distribution and gas trading. Sasol Limited has also secured rights to natural gas from the Republic of Mozambique through a series of agreements with the Mozambican Government.
- 3.7 Sasol Gas trades;
- piped natural gas from the Mozambican gas fields, as well as
 - piped methane-rich gas produced at Secunda.
- 3.8 The applicant's gas pipeline network covers parts of the Gauteng Province, as well as parts of the Free State, Mpumalanga and KwaZulu-Natal provinces.
- 3.9 This trading margin application is for various areas in which Sasol Gas is licensed to conduct trading activities. The number of licences and areas to which the trading margin applies to is listed in the trading margin application hereto attached as Annexure A. In summary the trading margin will apply to all areas where Sasol Gas has been issued with a trading licence.
- 3.10 In accordance with the Regulatory Reporting Manuals (RRM), Sasol Gas has unbundled its accounts into three licensed activities namely; trading, transmission and distribution. Thus cost allocation and reporting are done per licensed activity.
- 3.11 The trading section of Sasol Gas business maintains ownership of the gas molecules as they are transported through various pipelines up to the point of sale at the exit flange of the customer meter station.

3.12 The table below shows the summary components of the allowable revenue to be recovered through the trading margins as well as the forecasted volumes for the respective periods:

Table1

Sasol Gas Trading Margin calculation Summary				
(AR = (RAB*WACC) + E +D +T±C)			2015/16	2016/17
(RAB = v-d +net working capital)				
Total Regulatory Asset Base	Rands (R)	RAB		
WACC		WACC		
Rab x WACC= (a*b)	R	RAB *WACC		
Operating Expenses	R	E		
Depreciation and Amortization	R	D		
Tax	R	T		
Clawback	R	C		
Allowable Revenue (AR) = (c+d+e+f+g)	R	AR	1,532,008,373	1,652,989,985
Volume	GJ	V	176,295,555	184,279,820
Trading Margin	R/GJ	AR/V	8.69	8.97

3.13 Sasol Gas stated that it combined all trading costs and assets for all types of customers and proposes charging all customers the same trading margin subject to distinguishing features approved by NERSA in 2013 for traders and reticulators.

3.14 In 2013, Sasol Gas applied for a distinguishing feature that was approved by the Energy Regulator on 26 March as follows, *“To grant an additional discount to traders (all resellers of gas including distributors and reticulators) equivalent to 50% of Sasol Gas’ trading margin, applicable to each customer class.”*

4. NERSA ANALYSIS OF THE APPLICATION

4.1 When assessing an application, NERSA is guided by section 3.6.3 of the Methodology which states that:

“The trader’s margin (as a percentage) will be calculated in nominal terms. The nominal Weighted Average Cost of Capital (WACC) of the trader will be the trading margin (%), since all other expenses are allowed to the licensee as a pass-through. In so doing, the Energy Regulator will ensure the return on

investment as derived in the cost of capital calculation explained below is achieved.

Gas trading margins will be applied to the sum of 'Cost of Sales' plus 'Trading RAB' of that trader plus 'Working Capital'.

Cost of Sales and operating expenses that are allowable in the piped-gas trading business are those determined in terms of the prescribed Volume 1 and Volume 3 of the Regulatory Reporting Manuals for the piped-gas industry."

- 4.2 The formula for trading services provided to trading customers of a trading licensee is:



Where:

TRAB = approved historical trading services assets less accumulated depreciation

Working Capital = approved 45-day-average trading working capital

Expenses = approved efficient trading operating expenses including depreciation

Cost of Sales = Opening inventory of gas held for sale + Purchases of gas for sale -
Closing inventory of gas held for sale

Margin = Trading margin (%) determined in nominal WACC terms

T = Corporate tax expense for the period

C = Clawback (+/-)

- 4.3 The above formula illustrates that the Sasol Gas allowable revenue calculation is essentially the estimation of the cost of providing trading services to customers.
- 4.4 The paragraphs below provide an analysis of each component of the trading allowable revenue formula. A summary table will then illustrate the calculation of the trading margin at the end of discussing each component of the allowable revenue.

A. Trading Regulatory Asset Base (RAB)

- 4.5 In terms of section 3.6.1 of The Methodology, *trading licensees would not have piped-gas network assets, and if they do it would be insignificant [such assets are referred to as the 'Piped-gas trading plant in service' in the Regulatory Reporting Manuals (RMM)]. There may also be limited amounts of non-network assets (referred to as the 'Piped-gas general plant' in the RRM). The sum of the two will form the regulatory asset base (RAB) of a trading licensee.*
- 4.6 Investments in such limited and trading-specific piped-gas network assets, which are ordinarily required in the normal course of a piped-gas trading business, plus the general plant used for piped-gas trading, will be recovered through the trading margin.
- 4.7 The RAB value is a historical amount which is not trended. The formula for this is as follows:

$$\text{Regulatory Asset Base} = \text{Original Cost of Property, Plant \& Equipment (v)} - \text{Accumulated Depreciation (d)}$$

- 4.8 Using this approach, the resultant trading RAB for Sasol Gas including projected additions and depreciation for the period 01 July 2015 to 30 June 2016 is [REDACTED] and [REDACTED] for the period 01 July 2016 to 30 June 2017. This RAB is predominantly computer software, passenger vehicles and office furniture & equipment which are termed non-network assets ('piped-gas general plant') and have relatively short useful economic lives when compared to network assets (useful lives are typically 2 to 10 years).
- 4.9 The RAB figure of [REDACTED] is expected to depreciate to [REDACTED] in 2017. The reason for the 2017 RAB remaining at [REDACTED] is that Sasol Gas will commission new assets valued at [REDACTED] in the trading margin period and these will be pro-rated into the RAB. The Energy Regulator will check to assure itself that the additions indeed occurred and the value of the addition at the end of the Sasol Gas financial year, when the Regulatory Financial Reports (RFRs) of Sasol Gas are audited. An overstated RAB will be corrected using claw back in the next trading margin determination.

B. Depreciation

4.10 Sasol Gas calculated its straight line depreciation as ██████████ for the 01 July 2015 to 30 June 2016 (“FY15/16”) period and ██████████ for the 01 July 2016 to 30 June 2017 period (“FY 16/17”). These depreciation amounts are significant (over 30% of assets value) when compared to the value of the assets and reflect that non-network assets have relatively short economically useful lives (about 2 - 10 years) when compared to network assets (about 80 years). NERSA calculated the depreciation to be ██████████ and ██████████ for the same respective periods as those calculated by Sasol Gas. The difference in NERSA and Sasol Gas calculation is that Sasol Gas depreciated each asset item whereas NERSA grouped assets according to classes and depreciated on this basis. NERSA used the Sasol Gas figures because these will be audited when the RFRs are submitted and if differences are noted, these will be clawed back in the next tariff calculation.

C. Net Working Capital (w)

4.11 Net working capital refers to the various regulatory asset base funding requirements other than trading utility plant in service. This is determined using the following formula:

Net working capital = inventory + receivables + operating cash – trade payables.

4.12 Sasol Gas stated that it has not conducted lead lag studies to ascertain its working capital requirements. Sasol Gas followed the stipulation of the Methodology and used the 45 day operating cycle as indicated in the tariff guidelines and applied for ██████████ as the working capital for FY 2015/16 and ██████████ for FY 2016/17. These are the same figures that NERSA used.

D. Cost of Sales (COS)

4.13 Section 3.6.3 of The Methodology states that Cost of Sales and operating expenses that are allowable in the piped-gas trading business are those determined in terms of the prescribed Volume 1 and Volume 3 of the Regulatory Reporting Manuals for the piped-gas industry. The cost of sales and expenses

submitted by Sasol Gas were prepared in terms of the principles of its Cost Allocation Manual (“CAM”) approved by NERSA on 17 July 2012.

4.14 The Cost of Sales figure shows the cost of gas as purchased by Sasol Gas. It was reported that Sasol Gas buys natural gas from Sasol Petroleum Temane (SPT). In terms of the gas supply agreement, the total cost of gas charged by SPT to Sasol Gas comprises the well-head cost plus the central processing facility costs (CPF). Sasol Gas also buys methane rich gas from Synfuels and purchases syngas from Infrachem.

4.15 Sasol Gas buys gas from the following internal parties:

- SPT – natural gas
- Synfuels – methane rich gas.
- Infrachem – syngas. (Sasolburg)

Volumes

	2016 Volume (GJ)	2017 Volume (GJ)
SPT	██████████	██████████
Synfuels	██████████	██████████
Infrachem	██████████	██████████
Total	176 295 555	184 279 820

4.16 This yielded a cost of sales figure of ██████████ at a cost of ██████ for FY 2015/16 and ██████████ at a cost of ██████ for FY 2016/17.

E. Tax (T)

4.17 The Energy Regulator used the flow-through tax approach to determine the amount of tax payable in the allowable revenue. This is the same method used by Sasol Gas to arrive at a tax expense of ██████████ for FY 2015/16 and ██████ ██████ for FY 2016/17.

F. Operating Costs (E)

4.18 According to section 3.6.2 of the Methodology, all operating costs, including depreciation for the application year, that are efficient and prudently incurred by the piped-gas trading licensee shall be allowed as a pass-through in the trading margin. The operating expenses shall be grouped and reported to the Energy Regulator in accordance with the RRM. In considering the Sasol Gas expenses, NERSA also referred to the tariff guidelines section 4.3 that stipulate that each expenses item should be assessed using principles such as whether the expense was “prudently incurred”, its controllability and efficiency.

4.19 Sasol Gas applied for operating expenses of [REDACTED] for FYI 2015/16 and [REDACTED] for FY 2016/17. NERSA used the principles as articulated in the Methodology and assessed each expense item as provided by Sasol Gas and used the same figures as Sasol Gas.

G. Weighted Average Cost of Capital (WACC)

4.20 The Methodology requires that the trader’s margin (as a percentage) be calculated in nominal terms. The nominal Weighted Average Cost of Capital (“WACC”) of the trader will be the trading margin (%).

4.21 The nominal WACC will be calculated as prescribed in **Appendix 1** of The Methodology (**Appendix 1 – Determination of WACC**).

4.22 The formula to determine the WACC is as follows:

$$WACC_{(nominal)} = \left[\left(\frac{E}{Dt + E} \right) * Ke_{(nominal)} \right] + \left[\left(\frac{Dt}{Dt + E} \right) * Kd_{(nominal)} \right]$$

Where:

E = equity

Dt = debt

Ke_(nominal) = nominal cost of equity derived from the Capital Asset Pricing Model (CAPM)

Kd(nominal) = the post-tax nominal cost of debt.

4.23 Sasol Gas determined its WACC to be 00.00% based on a nominal pre-tax cost of debt (Kd) of 00% and nominal cost of equity (ke) of 00%. Sasol Gas indicated in its WACC calculation that [REDACTED].

4.24 To calculate its cost of equity, Sasol Gas used 11.95% for the Risk Free Rate (RFR) and 7.65% for the Market Risk Premium (MRP). Sasol Gas indicated that it used the Johannesburg Stock Exchange (JSE) (all share index -total returns index J203) as a proxy for market returns and Government Bonds of 10 years and longer as the proxy risk free rate.

4.25 Sasol Gas used 32 years (384 months) from March 1982 to February 2014 indicating that this is the longest time period in calculating the MRP and the RFR. As part of the reasons, it stated that ideally the period should not be shorter than the useful life of the pipeline assets. Sasol Gas contends that this would ensure that the return expectations are commensurate with the investment horizon. A long MRP would also allow for all possible economic situations and scenarios to be captured in the calculation of the MRP estimate. Sasol Gas further stated that this principle is consistent with frequently cited International practice by Ibboston Associates.

4.26 Sasol Gas indicated that it determined beta with reference to average beta of six international pipeline companies indicating that this is in line with the NERSA Tariff Guidelines section 4.4.5. Sasol Gas indicated that the beta for proxy companies is extracted from Bloomberg on the same basis used for the Sasol Group WACC and is based on historic data for a five-year period measured weekly. The 5 year beta period has changed from the two year data measured weekly that Sasol Gas used in the previous (March 2013) approved trading margin approved.

4.27 Sasol Gas stated that it followed the tariff guidelines and calculated its asset beta as the weighted average of the estimated asset betas for the proxy companies. Sasol Gas specified how it calculated the asset and how it applied the Hamada formula to obtain the company's equity beta. Sasol Gas calculated its equity beta as [REDACTED].

4.28 In assessing the reasonableness of the WACC, NERSA used the Methodology and came up with a nominal post-tax WACC of [REDACTED]. [REDACTED]

This is also the same method that Sasol Gas used.

4.29 The yield on loan stock traded on the stock exchange of Government bonds with a maturity of 10 years and over were used for the expected risk free return (Rf) in the estimation of cost of equity. This yielded a nominal risk free rate of 11.21% calculated over 25 years as required by the sources of information approved and published by NERSA.

4.30 The MRP was calculated using the JSE ALL Share Index for the previous 25 years up to June 2014 as required by the sources of information approved and published by NERSA. This yielded a nominal MRP of 5.81%. The difference between the NERSA MRP and risk free rate calculation and the Sasol Gas MRP and risk free rate calculation is in the estimation period. Sasol Gas opted to motivate for 32 years. NERSA used 25 years which was approved after a public consultation process and is published on the NERSA website.

4.31 The beta (β) was determined by proxy. As a proxy, the average of six gas pipeline companies chosen by the Energy Regulator and listed on stock exchanges must be used as per the Methodology. The following US companies were used by the NERSA as proxies:

- AGL Resources Inc.
- UGI Corporation
- South Jersey Industries
- WGL Holdings Inc.
- The Laclede Group
- Piedmont Natural Gas Company Inc.

4.32 NERSA used the same companies as those selected by Sasol Gas.

4.33 Although the Methodology does not specify the estimation window and the raw beta adjustment formula, it has been NERSA's practice in the piped-gas calculations to use:

- weekly returns observations;
- an estimation window using returns measured over a two-year period; and
- adjusted betas from Bloomberg as cited in the approved sources of information.

4.34 In line with the Methodology, the beta was calculated using the Hamada formula and yielded a beta of [REDACTED].

4.35 A cost of debt (Kd) of [REDACTED] was provided by Sasol Gas and used to calculate the post-tax cost of debt of [REDACTED]. The table below summarises the WACC calculation:

Table 2: 2015/17 WACC calculation summary

	Component	Symbol	NERSA	Sasol Gas
	Cost of Equity (Ke=Rf+(MRP*beta)+SSP)			
a	Risk free rate (Rf)	Rf	11.21%	11.95%
b	Market Risk Premium (MRP)	MRP	5.81%	7.65%
c	Beta	β	[REDACTED]	[REDACTED]
d	Small Stock Premium	SSP	[REDACTED]	[REDACTED]
e	Cost of Equity (Ke) = ((a+(b*c)+d))	Ke	[REDACTED]	[REDACTED]
	Cost of Debt			
f	Nominal Cost of Debt		[REDACTED]	[REDACTED]
g	Corporate tax rate	Tax	28.00%	28.00%
i	Nominal Cost of Debt (Post-tax)	Kd	[REDACTED]	[REDACTED]
j	Debt percentage		[REDACTED]	[REDACTED]
k	Equity percentage		[REDACTED]	[REDACTED]
l	Weighted Average Cost of Capital	WACC	[REDACTED]	[REDACTED]

H. Claw-back

4.36 Sasol Gas calculated an over recovery claw back of [REDACTED] that will be subtracted from the current allowable revenue. NERSA used the same clawback figure as calculated. Below is a table illustrating the claw back calculation:

Table 3: Claw back calculation

Clawback	Estimates used in tariff setting	NERSA Clawback Calculation	Sasol Clawback Calculation
	R	R	R
Total RAB			
WACC			
Return on assets (RAB*WACC)			
Operating Costs (E)			
Depreciation - Gas Assets(D)			
Taxation			
Allowable Revenue	1,409,272,027	1,390,029,334	1,387,141,084
Volumes	171,700,012	171,670,889	171,670,889
Margin (R/GJ)	8.21	8.10	8.08
Tariff Over recovered			
Actual Volumes sold			
Clawback (C)	-		

4.37 The trading margin assessment is summarised in the tables below:

Table 4:

2015/16 Trading Margin Calculation Summary			
(AR = (RAB*WACC) + E +D +T±C)		NERSA (R)	Sasol Gas (R)
(RAB = v-d +net working capital)			
a	Total Regulatory Asset Base	RAB	
b	WACC	WACC	
c	Rab x WACC= (a*b)	RAB *WACC	
d	Operating Expenses	E	
e	Depreciation and Amortization	D	
f	Tax	T	
g	Clawback	C	
h	Allowable Revenue (AR) = (c+d+e+f+g)	AR	1,394,773,759
i	Volume	V	176,295,555
j	Trading Margin	AR/V	7.91
			8.69

Table 5:

2016/17 Trading Margin Calculation Summary			
$(AR = (RAB * WACC) + E + D + T \pm C)$		NERSA (R)	Sasol Gas (R)
$(RAB = CoS + Assets + Net Working capital)$			
a	Total Regulatory Asset Base	RAB	
b	WACC	WACC	
c $Rab \times WACC = (a * b)$		RAB * WACC	
d	Operating Expenses	E	
e	Depreciation and Amortization	D	
f	Tax	T	
g	Clawback	C	
h	Allowable Revenue (AR) = $(c+d+e+f+g)$	AR	1,502,619,536
i	Volume	V	184,279,820
j	Trading Margin	AR/V	8.15

5. STAKEHOLDER CONSULTATION

- 5.1 The Sasol Gas trading margin application was published on 30 June 2015. Notices for the public hearing were published in the Business Day, Mail and Guardian, the Star and Sunday Times newspaper during the week ending 10 July 2015.
- 5.2 A customer of Sasol Gas submitted its comment regarding the trading margin application indicating that the Gas Act nor Piped Gas Regulations do not provide for the regulation of the trading margin. Illovo Sugar indicated that any trading margin will be included in the price calculated using the “basket of alternatives” and that adding a separate trading margin will be double counting and will unnecessarily increase the price of gas.
- 5.3 The customer also noted that the issue it is contending with is subject to a separate litigation process and is a matter that is before the courts.
- 5.4 Sasol Gas responded to the comment indicating that the GE price is only used to determine the molecule price and that a trading margin is added to the GE price to enable a licensee to make a profit.
- 5.5 NERSA’s position is that the GE price does not include the trading margin as shown in the Methodology. Section 21(1) p of the Gas Act empowers the Energy

Regulator to approve maximum prices, which maximum prices must enable the licensee to make a profit commensurate with risk as provided for in the Piped Gas Regulations. Regulation 4(4) states that,

“Maximum prices referred to in sub regulation (3) must enable the licensee to –

- a) recover all efficient and prudently incurred investment and operational costs;*
- and*
- b) make a profit commensurate with risk.”*

5.6 NERSA thus notes the comment and will await the finalisation of the court process.

5.7 During the public hearing, clarification was sought pertaining to the Cost of Debt, Cost of Sales, MRP and risk free rate periods, as well as a comparative of the change in the approved trading margins. The paragraphs below provide additional explanations to questions asked during the public hearing.

Cost of Debt (kd)

5.8 Sasol Gas reported that it [REDACTED]. However, the Methodology prescribes a [REDACTED] debt ratio of [REDACTED], hence Sasol Gas indicated that it used the Sasol Group cost of debt of [REDACTED].

5.9 It was further indicated that the cost of debt is reflective of the debt costs at group level. Sasol Gas submitted that in the absence of debt in the business, the prudent approach for them is to thus apply the Sasol Group cost of debt. NERSA accepted the approach and used the same cost of debt as Sasol Gas. However, NERSA will verify the actual Sasol Group cost of debt when the RFR are audited and will effect clawback if the actual group cost of debt is different to that used in the WACC calculation.

Cost of Sales

5.10 Sasol Gas confirmed that the cost of gas provided in the cost of sales calculation is the amount it pays to SPT, Synfuels and Infrachem. Sasol Gas stated that the gas is bought at arm's length, and according to accounting definitions, would thus qualify as a market related transaction. It was reported that there are gas supply contracts between Sasol Gas and its suppliers. According to Sasol Gas, one of these agreements between Sasol Gas and SPT indicates the total cost of gas charged by SPT to Sasol Gas is comprised of the well-head cost plus the central processing facility costs (CPF).

5.11 Sasol Gas provided some assumptions it used in estimating the cost of sales figures. The volumes used in the 2015/16 trading margin are the same as the volumes submitted to the NERSA finance division. However, different volume estimates were submitted for FY 2016/17. The volume submitted in the trading margin application for 2016/17 is 184 279 820 GJ whilst the volume submitted to the NERSA finance division for the same period is 179 303 579 GJ. Sasol Gas explained that the 184 279 820 GJ submitted with the tariff is the figure that was approved by their management during the preparation of the Sasol Gas budget. Sasol Gas went on to indicate that all forecasts are reviewed quarterly and that the difference in the figures could be because of the submission of the information at different periods. It was also explained that the volume used in the 2016/17 cost of sales includes additional volumes to be supplied using loop line two to be constructed in Mozambique. NERSA used the forecasted volumes as submitted by Sasol Gas because they will be audited and subjected to clawback after the end of the trading margin period in which they apply.

Comparison with Previous Approved Margin

5.12 Sasol Gas applied for trading margins for the period 01 July 2015 to 30 June 2017. The trading margin applied for by Sasol Gas in 2015/16 is a 16% decrease from the 2014/15 trading margin. The movement in the trading margin is shown below:

Table 6: Trading Margin Trend

2014/15 Trading Margin	2015/16 Trading Margin	2016/17 Trading Margin
R/GJ	R/GJ	R/GJ
10.40	8.69	8.97

5.13 Below is a comparison of the trading margin application approved for FY15 and the current requested margin for FY16.

Table 7:

Sasol Gas Trading Margin Comparison			2014/15	2015/16
(AR = (RAB*WACC) + E +D +T±C)				
(RAB = v-d +net working capital)				
a	Total Regulatory Asset Base	Rands (R)	RAB	
b	WACC		WACC	
c	Rab x WACC= (a*b)	R	RAB *WACC	
d	Operating Expenses	R	E	
e	Depreciation and Amortization	R	D	
f	Tax	R	T	
g	Clawback	R	C	
h	Allowable Revenue (AR) = (c+d+e+f+g)	R	AR	1,886,893,720
i	Volume	GJ	V	176,295,555
j	Trading Margin	R/GJ	AR/V	10.40
				8.69

5.14 The above summary illustrates that Sasol Gas over estimated expenses, depreciation, RAB and volumes in FY 15 when compared to the current FY 16 application and this is the reason for the decline in the current trading margin. The audit of Sasol Gas FY 15 RFRs is about to commence and NERSA will ensure that the actuals are captured accurately for the purposes of calculating claw back in the next trading margin application

5.15 Sasol Gas also commented on the application, explaining the differences between the NERSA preliminary assessment and the Sasol Gas assessment. Sasol Gas indicated that the differences were in the following elements

5.15.1 Beta;

5.15.2 Differences in the MRP; and

5.15.3 Differences in the clawback.

5.16 For the beta and MRP, Sasol Gas reiterated the explanation provided when the application was submitted. However, Sasol Gas agreed with NERSA on the clawback calculation and it revised its trading margin calculation downwards submitting a new lower trading margin for approval. The trading margin will decrease from R8.71/GJ to R8.69/GJ for the period 01 July 2015 to 30 June 2016. The trading margin for the period 01 July 2016 to 30 June 2017 did not change and Sasol Gas is still applying for R8.97/GJ. The trading margin applied for by Sasol Gas of R8.97/GJ will be the one that is approved by the Energy Regulator and not the one calculated by NERSA.

6. CONCLUSION

6.1 On the conspectus of the facts and evidence, it is appropriate and in compliance with the requirements of the National Energy Regulator Act, 2004 (Act No. 40 of 2004) to make the decision set out above.