01 November 2024

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The National Energy Regulator of South Africa (NERSA)
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CONSULTATION PAPER FOR ESKOM'S MYPD6 REVENUE APPLICATION

1. The South African Institute of Chartered Accountants (SAICA) welcomes the opportunity to make submissions to NERSA on the Consultation Paper for Eskom's Multi-Year Price Determination (MYPD) 6 Revenue Application.

2. SAICA is South Africa's pre-eminent accountancy body and is widely recognised as one of the world's leading accounting institutes. The Institute provides a wide range of support services to more than 60,000 members who are chartered accountants [CAs(SA)], associate general accountants [AGAs(SA)] and accounting technicians [ATs(SA)] who hold positions as chief executive officers, managing directors, board members, entrepreneurs, chief financial officers, auditors, and leaders in their respective spheres of operation.

3. Our work as an Institute goes beyond member support but also includes a significant focus on advocacy to drive and support improvement in the South African economy and society. This work is closely linked to SAICA's constitutional imperatives which places responsibility on SAICA to contribute to the economic and social development of the country and thereby acting in the public interest.

Current economic situation of the country

4. Eskom's MYPD 6 Revenue Application comes during a period where the country is grappling with high unemployment, low economic growth, high interest rates and high inflation with the most vulnerable members of society, the poor, mostly affected by these elements.

5. According to Statistics South Africa, the country's unemployment rate stood at 33,5% in the second quarter of 2024, marking an increase of 0.6 of a percentage point when compared to the first quarter of 2024. The expanded unemployment rate (which includes discouraged job seekers) on the other hand, increased by 0,7 of a percentage point to 42,6% for the same period.

6. According to Statistics South Africa, gross domestic product (GDP) increased by 0,4% in the second quarter of 2024. This followed a 0.0% growth in the first quarter of 2024. The South African Reserve Bank's (SARB) forecast is 0.6% for both quarters 3 and 4 of 2024.

7. South Africa has experienced high interest rates since the beginning of the SARB's hike cycle in 2021. Although a reduction of 25 basis points was announced after the SARB's September 2024 meeting, the policy rate remains high at 8% which puts strain on household finances and spending.

NPO-020-050 VAT No. 4570104366 | 17 Fricker Place, Illovo, Sandton, Johannesburg, 2196 | Private Bag X32, Northlands, 2116 | TEL +27 8610 SAICA (72422), WEBSITE http://www.saica.org.za | EMAIL saica@saica.co.za | www.saica.co.za | www.accountancysa.org.za | Member of the International Federation of Accountants (IFAC), Pan African Federation of Accountants (PAFA), Global Accounting Alliance (GAA), Chartered Accountants Worldwide (CAW) and Investors in People. Proudly South African.

8. The combined effect of high unemployment, low GDP growth rates, high interest rates and inflation puts massive strain on household finances and mostly affects the most vulnerable members of society, the poor, the so-called middle class and small medium business. Therefore, any electricity price increases proposed by Eskom and approved by NERSA must be considered in this context and it must factor the needs of the poor as the most vulnerable members of society. In addition, the increase may negatively impact affordability of electricity for the middle class which may lead to increased arrear debts for both Eskom and municipalities.

MYPD methodology

9. NERSA's mandate is to regulate the electricity, piped-gas and petroleum pipelines industries. Specifically for the electricity industry, this mandate is derived from the Electricity Regulation Act, 2006 (Act No. 4 of 2006).

10. As indicated in The Decision and Reasons for Decision on Eskom's MYPD5 Revenue application for the 2023/24 and 2024/25 Financial Years document, the MYPD is a process of determining allowable revenues for Eskom over a predetermined control period. The MYPD is based on a cost-of-service, rate of return-based methodology, namely the Multi-Year Price Determination Methodology (MYPDM), which provides the regulated entity with an opportunity to recover prudent costs and achieve a reasonable return. The application of the MYPDM should incentivise cost savings and efficient and prudent procurement by the licensee. This process is a basis for determining tariffs for various customer categories.

11. The MYPD is developed as a guide to the Regulator in the regulation of the electricity supply industry in a manner that should be deemed rational and would result in predictable and stable prices. It forms the basis on which NERSA will evaluate the price adjustment for Eskom over a multi-year period. Previous High Court decisions have indicated that revenue applications need to be made in accordance with a methodology that is in existence at the time. The current methodology in existence is the MYPD 4 methodology that was published by NERSA in 2016 and therefore in compliance in the High Court order, the MYPD 4 methodology should be applied in assessing the MYPD 6 revenue application.

Eskom's allowable revenue application

12. The table below depicts Eskom's allowable revenue application and tariff increases.

Year	Allowable revenue	Standard tariff increase	Municipal tariff increase
FY2026	R446 billion	36,15%	43,55%
FY2027	R495 billion	11,81%	3,36%
FY2028	R537 billion	9.1%	11,07%

13. As demonstrated on the above table, Eskom is requesting standard tariff increases of 36,15%, 11.81% and 9.1% for FY2026, FY2027 and FY2028, respectively. This in turn translates to municipal tariff increases of 43,55%, 3,36% and 11,07% for FY2026, FY2027 and FY2028, respectively. The municipal tariff rates are higher due to the different financial years between Eskom and municipalities.

14. The allowable revenue is further broken down to the below components in line with the MYPD methodology:

Allowable Revenue (R'millions)	AR	Formula	Decision FY2025	Application FY2026	Application FY2027	Application FY2028	Post Application FY2029	Post Application FY2030
Regulated Asset Base (RAB)	RAB		988 345	1 066 724	1 192 878	1 219 244	1 243 078	1 278 277
WACC %	ROA	X	1.58%	4.00%	5.00%	6.00%	7.47%	9.69%
Returns			15 616	42 669	59 644	73 155	92 908	123 916
Primary energy	PE	+	92 816	128 000	133 061	128 869	129 492	134 119
International purchases	PE	+	9 334	10 262	9 737	13 656	11 853	12 387
IPPs	PE	+	76 970	66 633	77 640	109 820	135 510	140 943
Environmental levy	L&T	+	6 503	6 539	6 279	5 337	4 781	4 767
Carbon tax	L&T	+	-	5 534	21 291	19 895	19 274	20 948
Arrear debt	E	+	-	8 914	9 917	10 752	12 037	13 310
Operating costs	E	+	61 442	93 315	93 834	97 864	100 152	105 100
Depreciation	D	+	73 376	66 931	69 952	77 431	79 685	85 961
MYPD6 Allowable Revenue			**336 057**	**428 798**	**481 355**	**536 778**	**585 691**	**641 450**
Add: Approved RCA/court order for liquidation	RCA		16 109	16 765	14 000	-	-	-
TOTAL MYPD6 Allowable Revenue	R'm		**352 166**	**445 563**	**495 355**	**536 778**	**585 691**	**641 450**

Extract from Eskom's submission to NERSA on the MYPD 6 Revenue Application for FY2026 – FY2028

15. In its application, Eskom has stated that for FY2026, the major contributors to the price increase of 36,15% are as depicted in the below table.

Major contributor	Reason for the increase	SAICA Comments
Primary energy costs FY2026 at 11.2%	Due to increase in coal costs arising from further dependence on coal-fired power stations to compensate for the independent power producers (IPPs) not materialising.	(a) While it is appreciated that delays in the materialisation of IPPs may lead to increased costs of coal because of further dependence on coal-fired power stations, **it may not be appropriate for consumers to bear the costs for inefficiencies that result to these delays.** Eskom should rather consider playing an advocacy role to influence the faster materialisation of IPP projects, especially those that are renewable energy in nature as this may allow Eskom to further save on electricity production costs, achieve a reduction on its impact on the environment and possibly save on carbon taxes. It is also expected that there should be an inverse relation between IPP costs and primary energy costs in that as more IPP projects come online, the costs of coal should reduce.

Major contributor	Reason for the increase	SAICA Comments
Arrear debt FY2026 ay 2.6%	Due to debt not collected by Eskom. *NB: NERSA has denied this expenditure in the MYPD 5 decision*	It is noted that in the MYPD 5 decision, NERSA disallowed the arrear debt on the basis that paying customers should not be burdened by debt not recovered by Eskom. SAICA agrees with the NERSA view and maintains that this view must be maintained in this MYPD 6 application decision. **Eskom should rather implement effective debt collection strategies to ensure that debt owed is recovered.** It is acknowledged that the current National Treasury Municipal Debt Relief Programme has not been effective in ensuring that municipalities are able to settle their Eskom debt. However, **this inefficiency should not be passed on to paying customer. In addition, burdening those customers who are paying with disproportionate pricing increases may be seen as a an attempt to achieve the overall level of price increase across consumers by leveraging off the recoverability of existing payers. This may in turn significantly impair the ability of the current paying consumer to continue to do so.**
Return on Assets (ROA) • FY2026 at 7.9% • FY2027 at 4% • FY2028 at 2.8%	Iin a bid to migrate towards cost reflectivity in line with the request from the Minister of Finance to allow for Eskom's migration towards financial sustainability and lessening the burden on the fiscus. This is also a critical part of the Eskom Debt Relief Programme that came into effect on 07 July 2023 to provide relief to Eskom on its debt servicing costs.	SAICA supports the assertion that Eskom should migrate towards a cost-reflectivity in line with the Minister of Finance's request and the MYPD Methodology which states that the Energy Regulator should ensure Eskom's sustainability as a business and limit the risk of excess or inadequate returns. However, **this must be done with prudence to ensure that customers are not overburdened by such an increase**. The application for an increase in the ROA from the 1.58% decision in FY2025 to 4% in FY2026, 5% in FY2027 and 6% in FY2028 may not achieve the prudency requirement.
IPPs • FY2027 at 2.7% • FY2028 at 6.6%	As delayed IPP projects will start coming online which will lead to additional costs.	In its application, Eskom indicates that delayed IPPs will start to come online. However, the basis of this expectation is not apparent in the application especially given the delays that have been experienced in the past. **NERSA should therefore request a basis for this expectation from**

Major contributor	Reason for the increase	SAICA Comments
		Eskom to appropriately evaluate the assumption made in this regard.

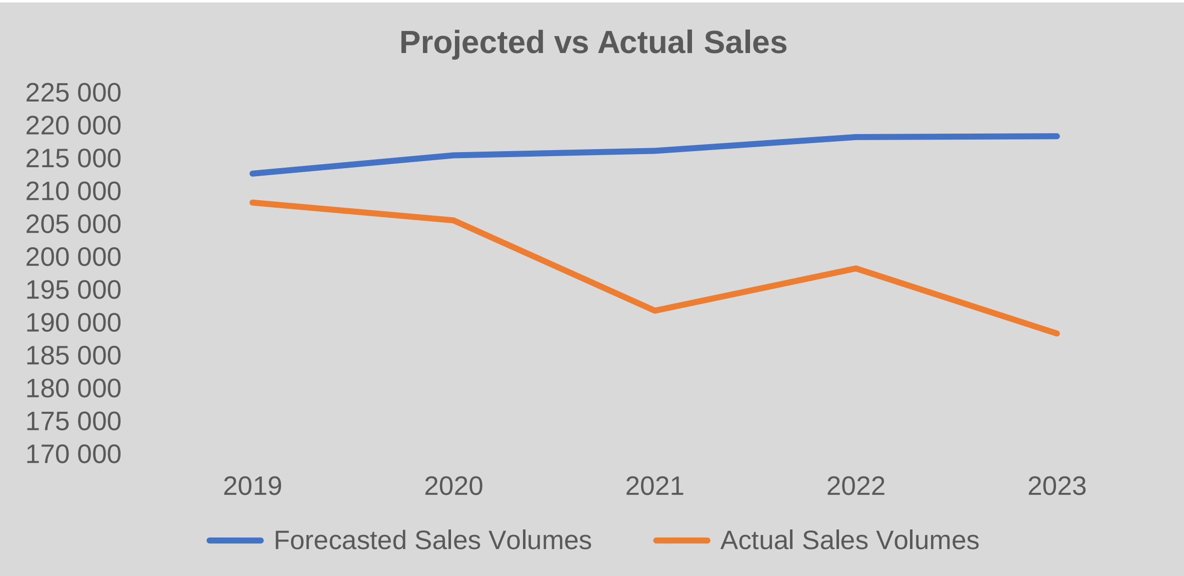
Sales volumes

16. Eskom has stated that one of the key assumptions in the MYPD6 application is the latest available forecasted sales volumes. The below table depicts Eskom's forecasted sales from FY2023 to FY2030:

Sales volumes (GWh)	Actual FY2023	Projection FY2024	Projection FY2025	Application FY2026	Application FY2027	Application FY2028	Post Application FY 2029	Post Application FY2030
Standard tariff sales	166 980	167 977	156 039	152 836	150 394	149 689	148 231	147 323
Year-on-year growth (%)		0.6%	-7.1%	-2.1%	-1.6%	-0.5%	-1.0%	-0.6%
Negotiated pricing agreement	10 413	10 440	22 679	22 581	22 625	22 713	22 564	22 591
Year-on-year growth (%)		0.3%	117.2%	-0.4%	0.2%	0.4%	-0.7%	0.1%
Total local sales	**177 392**	**178 416**	**178 717**	**175 417**	**173 019**	**172 403**	**170 796**	**169 914**
International Sales	11 357	9 619	10 355	10 235	10 235	10 265	10 235	10 235
Year-on-year growth (%)		-15.3%	7.7%	-1.2%	0.0%	0.3%	-0.3%	0.0%
Total Sales (incl. Internal	**188 749**	**188 035**	**189 072**	**185 652**	**183 254**	**182 668**	**181 031**	**180 149**
Year-on-year growth (%)		**-0.4%**	**0.6%**	**-1.8%**	**-1.3%**	**-0.3%**	**-0.9%**	**-0.5%**

Extract from Eskom's submission to NERSA on the MYPD 6 Revenue Application for FY2026 – FY2028

17. Historically and as depicted in the graph below, **Eskom's projected sales volumes have tended to be vastly different from the actual sales volumes (as reflected in the 2023 Integrated Report) which indicates some possible deficiencies in the forecasting methodology**. Eskom's price increases based on these sales volumes may be overstated. It is recommended that NERSA interrogates the details of projected sales volumes prior to making the allowable revenue and price decision.



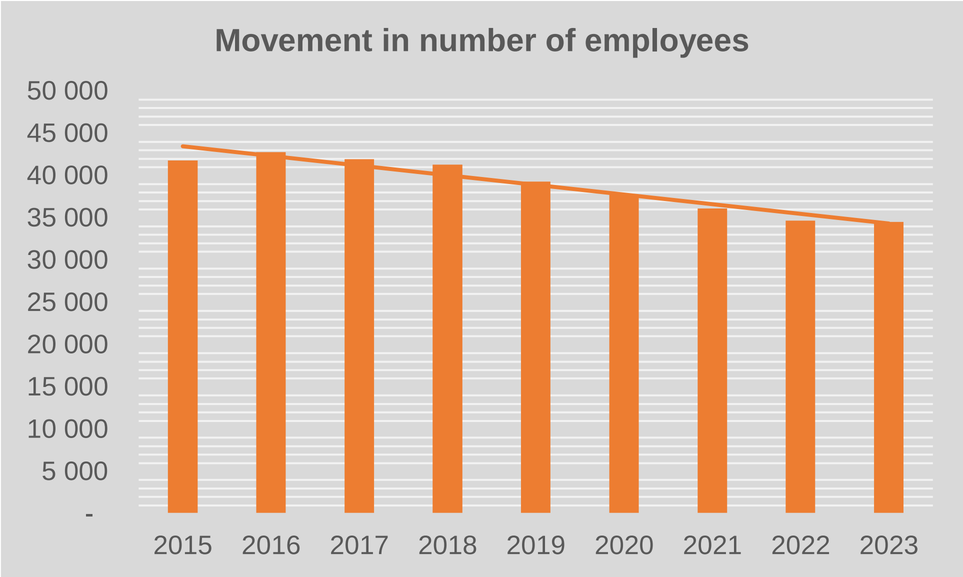
Depiction of projected actual sales volumes vs forecasted sales volumes

18. In its application, Eskom has indicated that the volume forecast does not include future load shedding as the forecast is a representation of the expected volume requirement in the market. However, load shedding has previously had an impact on Eskom's final sales volumes. In addition, we believe that Eskom is able to estimate the expected stages of load shedding which are linked to megawatts power. Eskom should therefore be able to determine the impact of load shedding on forecasted sales which should ideally lower the forecasted sales which will in turn lower the price increase approved by NERSA. This is still applicable even though the country has experienced more than 200 load shedding free days as Eskom has indicated in a media statement in August that for a scenario where unplanned outages rise to 14 000MW, Stage 1 loadshedding could be implemented.

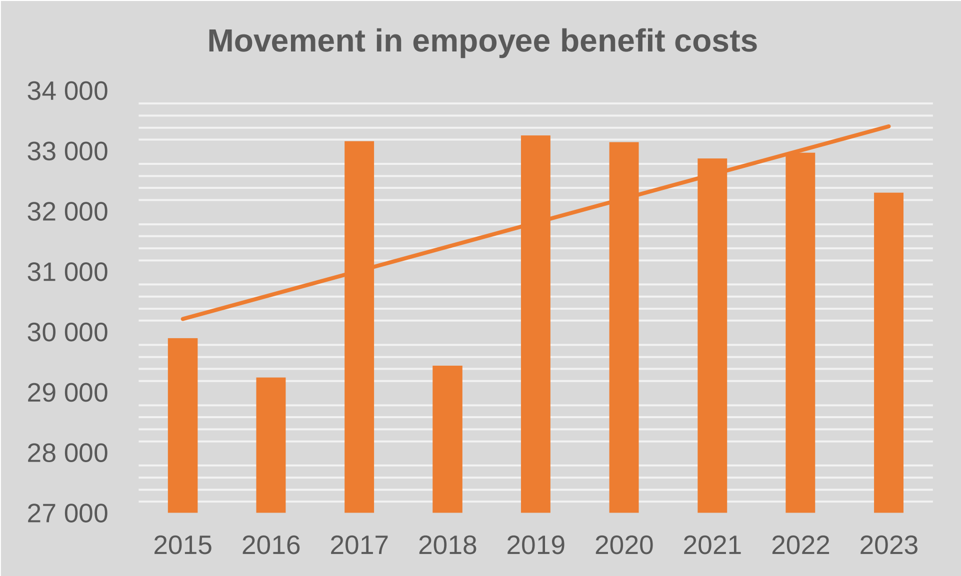
19. SAICA has identified the following challenges with regards to the assumptions applied by Eskom on the sales volumes include:
    a. Gross domestic product (GDP) where it is stated that in the sales volume forecast, the gap between sales growth and GDP is widening due to lower energy-intensive sales during the forecast years and migrating towards a greater service-oriented economy. In addition, several mines and large industrial customers are exploring alternative sources of energy. However, on review of the application submission, **it is unclear how GDP growth expectations are factored into the sales volumes forecasts.** It would have been expected that the forecast should indicate the sales volume scenarios versus the GDP growth rate which is currently not reflected in Eskom's submission. What is reflected in is sales growth versus GDP growth without an indication of how the two impact each other. **It is therefore impossible for the GDP assumption to be effectively interrogated in the submission**.
    b. Commodity prices where it is stated that platinum prices are expected to remain high in the short term and during the MYPD 6 period. It is further stated that the gold price is expected to start stabilising in the short term after reaching record highs in 2020. The source of these expectations is the World Banks 2023 Commodity Markets Outlook which only forecasts commodity prices until the year 2024 and does not cover the MYPD 6 period of FY2026, FY2027 and FY2028. **It is therefore unclear how the commodity price assumptions for the MYPD 6 application have been determined.**
    c. Customer projects where it is stated that only projects that have a high probability of start-up and have budget quotation accepted by customers are included in the sales forecast. However, **there is no additional information given about the projects referred to under this assumption which makes it impossible to evaluate the assumptions made about new customer projects**. Information such as project name, commencement and end date and sales volumes committed could assist in evaluating the assumption. This may also assist in promoting transparency by Eskom and allow for the public to interrogate the information as part of the submission to NERSA.
    d. Impact of leap year where it is stated that there are additional sales in February 2028 due to the extra day. This is considered to be a reasonable expectation as an extra day in a year may result in additional volume sales. However, one day is not expected to have a significant impact on the projected sales volumes for the FY2028 application period as this only equates to 0,27%.

Employee benefit costs

Eskom has stated in the application that its operating costs include employee benefits, maintenance, other expenses and allocated corporate costs. In the MYPD6, Eskom is applying for employee benefit costs of R37 billion in FY2026, R39 billion in FY2027 and R41 billion in FY2028. Furthermore, Eskom has indicated that workforce optimisation has been identified as a major component to drive internal efficiencies, increase productivity and lower operating costs. It is also assumed that the planned number of employees will decrease through planned attrition or alternatives that support savings initiatives and efficiencies.



Movement in number of employees



Movement in employee benefit costs

20. **While it is noted that the number of employees has been decreasing, it is concerning that this decrease has not translated to a reduction in employee benefit costs**. As depicted in the graph above, the number of employees has been decreasing since 2015 (from 41 787 to 34 518 in 2023) while the employee benefit costs have been increasing during the same period (from R29,9 billion in 2015 to R32,3 billion in 2023). If this trend continues, Eskom will continue to not reap the benefits of a lower workforce thereby leading to further increases in operating costs which NERSA should not allow in the allowable revenue application. It is further recommended that deeper analysis into the increase in these employee benefit costs be performed. This should be read in the context of the audit opinion raised in paragraph 22 below.

Governance challenges at Eskom

21. SAICA acknowledges the efforts that have been made by the Eskom board in addressing the historical governance challenges as depicted in the below diagram. However, over the past few years, the external auditors have consistently issued a qualified opinion on the audit of the annual financial statements due to a lack of accurate records for irregular expenditure, fruitless and wasteful expenditure and losses due to criminal conduct. **This lack of accurate records has led to the auditors being unable to determine the full extent of the misstatements of irregular expenditure and fruitless and wasteful expenditure and the understatement of losses due to criminal conduct.**

![SAICA Difference Makers logo]

Extract from the Eskom Integrated Report for the year ended 31 March 2024

22. NERSA has previously stated that it will ensure that all **expenditure related to fraud and maladministration, as well as fruitless and wasteful expenditure, should be recovered and credited in favour of customers**. SAICA agrees with this view and encourages NERSA to apply the same principle in allowing revenue for the MYPD6 application period.
23. SAICA further recommends that Eskom should be held accountable to provide feedback on the recovery of expenditure related to fraud and maladministration, as well as fruitless and wasteful expenditure.

Conclusion

24. We would also appreciate the opportunity to engage further, and we would be willing to discuss the comments if required. We would appreciate the opportunity to make a submission at the public hearings. Please do not hesitate to contact Natashia Soopal (natashias@saica.co.za) or Odwa Benxa (odwab@saica.co.za) in this regard.

Regards,

Milton Segal

Executive Director: Standards