18 December 2015

Ms Legume Masika
National Electricity Regulator of South Africa
526 Madiba Street,
Arcadia, 0083,
Pretoria, South Africa

Dear Sir/ Madam:

SAIPPA COMMENTS ON THE ESKOM REGULATORY CLEARING ACCOUNT (RCA) APPLICATION FOR MYPD 3 YEAR

We thank you for the opportunity to comment on the Eskom RCA Application. The members of SAIPPA have a deep understanding of the Electricity Supply Industry (ESI) in South Africa and can provide valuable insights into the current electricity situation in South Africa.

The goals of the Independent Power Producers Association of South Africa are to promote the collective interests of IPP's in South Africa, to assist with public policy formation and implementation, and to serve as a platform for information dissemination to its members.

We seek to pro-actively engage with legislators, government officials, planners and regulators as part of our initiatives to achieve energy security in South, as well as Southern Africa.

The IPPs and Companies participation in the association promote the interests of independent power producers in Southern Africa, with due regard for the prescripts and limitations imposed by the Competition Act. Members meet on a six weekly basis in Johannesburg and the agenda covers current pertinent issues affecting.

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A key aspect of the work of SAIPPA is focused on broad industry reform, with the objective of creating a modern ESI which provides an enabling environment for all IPPs, towards the provision of competitively priced, reliable and available electricity.

Context

The comments on Eskom's RCA application should be viewed in the context of SAIPPA's objective of promoting access to the South African electricity market for its members. It is therefore imperative that Eskom behaves in a way that enables access to grid infrastructure to IPPs. Such access should be provided on an equitable basis and at costs that are reasonable and substantiated.

The private sector has shown its ability to contribute its skills and resources under the REIPPP program. With a fleet of new generation capacity being added on quarterly basis to Eskom current struggling fleet, SA is running one of the cheapest and most successful renewable programs in the world. ESKOM's ability is portrayed by its limited success on commissioning Medupi and Kusile which should be compared to timeous achievements on the side of the private sector lead REIPPP program.

Artificial barriers, created by Eskom, is preventing timeous access to the grid for IPP's. This unfortunate situation was again underlined when Eskom recently requested selective exemption from clause 2(2) of the Network Code which requires them to supply budget quotes for new connections to the transmission system. Even though their request relates to REIPPPP bids after BW3 until the end of MYPD3 (31 March 2018) and is therefore not related to their RCA application, it highlights how Eskom stifles equitable access to grid infrastructure to IPP's.

Issues to be addressed by NERSA

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In considering the RCA application, NERSA should carefully consider the following issues and possibly improve the MYPD methodology to prevent a reoccurrence of such undesirable outcomes in future:

i. NERSA should ensure that no cross-subsidisation is entertained between allocations made for capital expenses and those made for operating expenses. If capital and operating expenses are not appropriately ring-fenced, it could lead to under-investment in grid infrastructure to the detriment of grid access to IPP's.
ii. NERSA should ensure that Eskom is held accountable to commit to the capital investments as intended in the MYPD allocation. Reallocation of capital expenditure to the detriment of enhancing transmission and distribution capability, should be prevented. It is concerning to IPP's that capital underspending on transmission amounted to R4 679 million and on distribution amounted to R412 million. This under-investment in grid infrastructure could be to the detriment of grid access for IPP's.

Beyond this RCA application, NERSA should ensure that Eskom adequately provides for capital investment in transmission and distribution in future MYPD cycles. Adequate investment should be in support of electricity demand projections and should also consider electricity supply that can be sourced from IPP's at appropriate sites. Allocations in future MYPD cycles, earmarked for transmission and distribution infrastructure development and operation, should be appropriately ring-fenced from operating expenditure and other capital expenses.

Reallocation of funds from the "Wires Business" (transmission and distribution) to other Eskom Business (particularly generation) is not supportive of investment and Government's ambition around attracting Private Sector generation. The transfer of funds allocated by NERSA from Transmission to Generation may lead to transmission and distribution capital shortages for IPP connections and customers. This is a concern as it may directly affect the certainty that IPP projects require for financial close.

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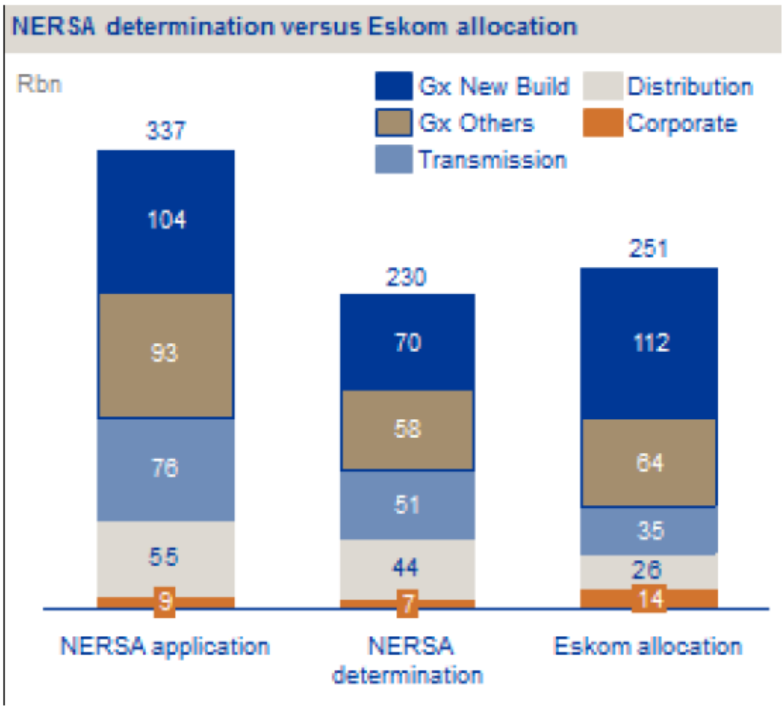

If Eskom is spending money on CSP and Wind how does it compete equitably with IPP's – the Excess costs including cheap financing and legal need to be considered in this evaluation.

Medupi and Kusile are defined as being plagued by poor contractor performance generating increased costs. Poor contractor performance is generally a function of poor contractor management. How is this cost being managed to prevent further escalation using an outsider contract management team to provide contract guidance to Eskom?

Table 6 on page 31 defines that short term IPP costs have not been applied for and hence dispatch of these units is not preferred relative to the far more expensive gas turbines. Why is this? Why is a sensible dispatch order not established utilising the optimal generation capacity available?

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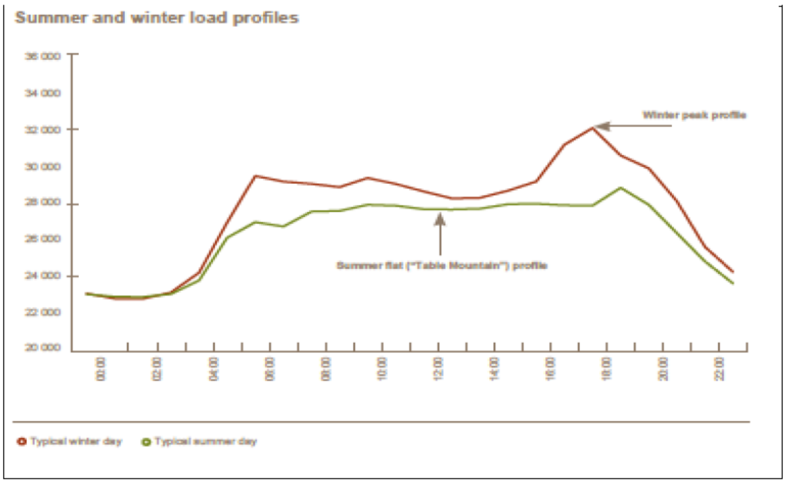

The daily load profile (Figure 24) indicates that there is a potential for 6 GW (28GW – 22GW) of mixed renewable IPP power to be installed in the country; preferably at a municipal level. This would decrease transmission and distribution costs and create significant employment in the sector

There is significant Eskom commentary on the aging fleet, a problem which will grow and not be solved by Nuclear so a reversal to the White paper and a drive for 30% IPP should be stimulated, particularly through novel financing as much of the available rands based financing for power generation is spoken for and perhaps a tranche of dollar based should be considered. This will be very competitive and perhaps be a forerunner for gas IPP where the primary fuel costs will be dollar based in any event.

General considerations

SAIPPA supports Eskom's RCA application for Year 1 (2013/14) of the third Multi Year Price Determination (MYPD3) for as far as it relates to the actual prudent cost of supplying electricity. Eskom should be allowed to recover their full cost as well as enjoy symmetrical treatment of operating cost variances. Not allowing for the full cost of generation in the tariff, will result in the Eskom tariff being artificially low and IPP's will not be treated on an equitably basis in the South African electricity market. Full recovery of Eskom's cost will allow IPP's to compete on an equitable basis and to add value to the South African economy.

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In addition the indirect negative effect on the economy, job losses, investor uncertainty and the business sector could potentially have a far greater long term impact, which is believed to be more negative than short term tariff increases.

Eskom's RCA application suggests that Eskom is unable to manage capital and operating expenses prudently. If the RCA claw-back of prudent costs is not granted, it may force Eskom's shareholder to bail it out. This will create an unequitable situation towards IPP's that don't have access to "bail-out" finance.

It is suggested that NERSA introduces a mechanism through which a portion of the tariff increases and related income to ESKOM will be channelled and dedicated for implementation of projects led by the private sector. It is proposed to set up a more dedicated budget facility hosted for the private sector under NERSA implementation rules. This budget facility is to be managed by the private sector and appointed members from e.g. the Energy Intensive User Group along with Eskom representatives as to realise a cohesive approach.

Yours faithfully,

SISA NJIKELANA
CHAIRMAN: SAIPPA

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