**IN THE HIGH COURT OF SOUTH AFRICA**

**(GAUTENG DIVISION, PRETORIA)**

**Case number: 24364/2016**

**Date: 16 August 2016**

DELETE WHICHEVER IS NOT APPLICABLE
(1) REPORTABLE: ~~YES/NO~~
(2) OF INTEREST TO OTHERS JUDGES: ~~YES/NO~~
(3) REVISED

16/8/2016 .....
DATE SIGNATURE

In the matter between:

**BORBET SA (PTY) LTD** — **FIRST APPLICANT**

**PG GROUP (PTY) LTD** — **SECOND APPLICANT**

**CROWN CHICKENS (PTY) LTD** — **THIRD APPLICANT**

**AGNI STEELS SA (PTY) LTD** — **FOURTH APPLICANT**

**AUTOCAST SOUTH AFRICA (PTY) LTD t/a AUTOCAST PORT ELIZABETH** — **FIFTH APPLICANT**

**NELSON MANDELA BAY BUSINESS CHAMBER** — **SIXTH APPLICANT**

**And**

**THE NATIONAL ENERGY REGULATOR OF SOUTH AFRICA**

**FIRST RESPONDENT**

**ESKOM HOLDINGS SOC LTD**

**SECOND RESPONDENT**

**MINISTER OF ENERGY**

**THIRD RESPONDENT**

**NELSON MANDELA BAY MUNICIPALITY**

**FOURTH RESPONDENT**

**SOUTH AFRICAN LOCAL GOVERNMENT ASSOCIATION**

**FIFTH RESPONDENT**

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**JUDGMENT**

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*PRETORIUS J,*

(1) In this review application the applicants are seeking an order declaring the decision published by the first respondent on 1 March 2016 in respect of the Regulatory Clearing Account ("RCA") application by the second respondent – third Multi-Year Price Determination (MYPD3) Year 1 (2013/2014) (the "Decision") to be inconsistent with the Constitution and invalid and an order reviewing and setting aside the Decision, as well as an order that all future RCA applications by the second respondent in respect of the MYPD3 be submitted and evaluated strictly in accordance with paragraph 14 of the MYPD Methodology, or any future amendment thereof. Furthermore the applicants are seeking an order: *"Declaring the allowed revenue for Eskom for 2016/2017, to be the amount of R170 264 million, as reflected in Table 3 of the Decision, resulting in an average approved*

*increase to standard tariff customers of the Second Respondent for 2016/2017 of 3.51% and 8% for 2017/2018 (the "Lawful Tariff")"*[1].

(2) A further order is sought to direct the first respondent to amend all electricity tariffs approved based on the decision and directing the second respondent to refund all credits resulting from the introduction of the lawful tariff. An order should be issued in relation to distributors and directing that any amount overpaid to the second respondent be credited as excess revenue and directing the first respondent to adjust the revenue requirement for the 2017/2018 calendar year under the MYPD3.

(3) In the alternative an order is sought remitting the decision to the first respondent for reconsideration with directions regarding how the RCA is to be implemented and determined.

**THE PARTIES:**

(4) The first applicant is BORBET SA (PTY) LTD, a private company. Borbet's primary business is the manufacture of aluminium alloy wheels and as a supplier to the automotive sector.

(5) The second applicant is PG GROUP (PTY) LTD t/a SHATTERPRUFE,

[1] Page 561 paragraph 4

a private company. Shatterprufe is a producer of automotive safety glass.

(6) The third applicant is CROWN CHICKENS (PTY) LTD, a private company. Crown Chickens' core business is the production of processed poultry products.

(7) The fourth applicant is AGNI STEELS SA (PTY) LTD, a private company. Agni Steels conducts its primary business as a manufacturer of various steel products.

(8) The fifth applicant is AUTOCAST SOUTH AFRICA (PTY) LTD t/a AUTOCAST PORT ELIZABETH, a private company. Autocast is a manufacturer and supplier of cast components to the automotive sector.

(9) The first to fifth applicants are businesses operating within the Nelson Mandela Bay Metropolitan Municipality ("the municipality"). They are consumers and users of electricity supplied by the municipality, and are directly and negatively affected by NERSA's decision.

(10) The sixth applicant is the NELSON MANDELA BAY BUSINESS

CHAMBER. The Business Chamber represents a broad spectrum of business in the Nelson Mandela Bay with a membership of close to one thousand businesses (including the first to thirteenth applicants).

(11) NERSA is the first respondent. It is a regulatory authority established in terms of section 3 of the **National Energy Regulator Act**[2] ("the NERSA Act"). NERSA's mandate is to regulate the electricity industry in South Africa in terms of the **Electricity Regulation Act**[3]. The Regulator is the custodian and enforcer of the regulatory framework provided for in the **Electricity Regulation Act**[4] ("ERA").

(12) Eskom is the second respondent. It is a public company. The applicants seek costs against Eskom as Eskom opposes this review application. This review application is opposed by the first and second respondents.

(13) The third respondent is the MINISTER OF ENERGY, cited in her official capacity as the National Executive Authority. NERSA falls under the Minister's authority. Aside from costs in the event of opposition, no relief is sought against the Minister.

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[2] Act 40 of 2004
[3] Act 4 of 2006
[4] *Supra*

(14) The fourth respondent is the NELSON MANDELA BAY MUNICIPALITY. The fourth respondent filed an affidavit setting out that it is not opposing or supporting the application, as long as it does not adversely affect the fourth respondent.

(15) The fifth respondent is the SOUTH AFRICAN LOCAL GOVERNMENT ASSOCIATION. The third and fifth respondents did not file opposing papers.

(16) Counsel for both the applicants and the first and second respondents launched condonation applications for the late filing of their heads of argument. In both instances these applications were not opposed and were granted.

**LEGAL FRAMEWORK:**

(17) A regulatory framework has been put in place to determine the price of electricity. According to the applicants the most recent price adjustment has strayed from that framework in circumstances that are impermissible and for unjustified reasons.

(18) Pricing of electricity is regulated by the **Electricity Regulation Act**[5] ("ERA"). Section 4(a)(ii) of the Act states that *"the Regulator must*

[5] Act 4 of 2006

*regulate prices and tariff*". Section 15(1) and (2) of the Act prescribes the principles:

> *"(1) A licence condition determined under section 14 relating to the setting or approval of prices, charges and tariffs and the regulation of revenues-*
>
> *(a) must enable an efficient licensee to recover the full cost of its licensed activities, including a reasonable margin or return;*
>
> *(b) must provide for or prescribe incentives for continued improvement of the technical and economic efficiency with which services are to be provided;*
>
> *(c) must give end users proper information regarding the costs that their consumption imposes on the licensee's business;*
>
> *(d) must avoid undue discrimination between customer categories; and*
>
> *(e) may permit the cross-subsidy of tariffs to certain classes of customers.*
>
> *(2) A licensee may not charge a customer any other tariff and make use of provisions in agreements other than that determined or approved by the Regulator as part of its licensing conditions."*

(19) The **Electricity Pricing Policy**[6] ("EPP") gives broad guidelines to National Energy Regulator of South Africa (NERSA) in approving

[6] Government Notice No. 1398 dated 19 December 2008

prices and tariffs for the electricity supply industry. The EPP sets out principles for determining and approving the revenues that a licensed generator, transmitter or supplier of electricity may derive from its licensed activities. Tariffs are then determined so that the approved revenues are achieved.

(20) The multi-year price determination methodology has been put in place. The MYPD methodology is a comprehensive document. It deals with the Regulatory Clearing Account ("RCA").

(21) The purpose of the RCA is set out in the Methodology as[7]:

> *"14.1 **Risk Management Device***
>
> *The risk of excess or inadequate returns is managed in terms of the RCA. The RCA is an account in which all potential adjustments to Eskom's allowed revenue which has been approved by the Energy Regulator is accumulated and is managed as follows:*
>
> *14.1.1 The nominal estimates of the regulated entity will be managed by adjusting for changes in the inflation rate.*
>
> *14.1.2 Allowing the pass-through of prudently incurred primary energy costs as per Section 8 of the Methodology.*
>
> *14.1.3 Adjusting capital expenditure forecasts for cost and timing variances as per Section 6 of the Methodology.*

[7] Page 80 paragraph 14.1

*14.1.4 Adjusting for prudently incurred under-expenditure on controllable operating costs as may be determined by the Energy Regulator.*

*14.1.5 Adjusting for other costs and revenue variances where the variance of total actual revenue differs from the total allowed revenue. In addition, a last resort mechanism is put in place to trigger a re-opener of the price determination when there are significant variances in the assumptions made in the price determination."*

(22) ERA and EPP set out the principles and the MYPD methodology sets out the process. Each determination of price covers a period of 3 to 5 years. The recent determination by NERSA was the third multi price determination, known as MYPD3. MYPD3 covers five tariff years, between 1 April 2013 and 31 March 2018. The tariff years and Eskom's financial years coincide.

(23) The RCA application was made in terms of the Regulator's Multi-Year Price Determination Methodology (MYPD). It forms the basis on which NERSA will evaluate the price adjustment application from Eskom.

(24) The MYPD methodology was, according to the NERSA document, developed for the regulation of Eskom's required revenues. The

capability and expertise of NERSA's personnel were not an issue in the present application.

(25) The Regulatory Clearing Account ("RCA") is used to debit or credit potential adjustments to Eskom's allowed revenue and it is set out, *inter alia*, how it should be used in section 14.2.4 pertaining to the methodology. Section 14.2.5 obliges Eskom to present NERSA with possible adjustments based on the methodology on a quarterly basis. The applicants further rely on the provisions of paragraph 14.2.6 which refer to *"any adjustment required in the subsequent financial year's tariff adjustment"*.

(26) According to NERSA the following objectives were adopted to develop the MYPD methodology:

> *"1. to ensure Eskom's sustainability as a business and limit the risk of excess or inadequate returns; while providing incentives for a new investment;*
>
> *2. to ensure reasonable tariff stability and smoothed changes over time consistent with socio-economic objectives of the Government;*
>
> *3. to appropriately allocate commercial risk between Eskom and its customers;*
>
> *4. to provide efficiency incentives without leading to unintended consequences of regulation on performance;*

5. *to provide a systematic basis for revenue/tariff setting; and*

6. *to ensure consistency between price control periods."*

(27) According to the first respondent the methodology does not preclude NERSA from applying reasonable judgment to its consideration of Eskom's revenue, bearing in mind and after due consideration of the best interests of the South African economy and the consumers as a whole.

(28) NERSA approved an 8% annual increase on the approved revenues for the 2013/2014 tariff year. NERSA approved an additional price increase in respect of the 2013/2014 tariff year of R11.2 billion to take effect on 1 April 2016, to be recovered during the 2016/2017 tariff year.

(29) This decision by NERSA is being challenged by the applicants, as it represents a tariff increase for the 2016/2017 tariff year of 5.9% in addition to the previously approved increase under MYPD3. The applicants contend that NERSA has allowed Eskom to reach back to the 2013/2014 period to recover an additional R11.2 billion in 2016/2017, 27 months after the annual audited financial statements became available.

(30) The Regulatory Clearing Account ("RCA") is governed by section 14.2 of the methodology which provides:

*"The RCA is used to debit/credit all the aforementioned potential adjustments to Eskom's allowed revenue and must be used as follows:*

*14.2.1 The RCA will be created at the beginning of the financial year and continuously monitored. The evaluation of the account (for the purpose of determining the pass-through and/or claw-back will be done with actuals for the full financial year.*

*14.2.2* ***This account must be updated quarterly so as to use it for regular alerts to customers of any possible adjustment in the coming year. Eskom must therefore submit actual financial data on a quarterly basis.***

*14.2.3 The RCA balance will be measured as a percentage of total allowed revenue and will act as a trigger for a re-opener as follows:*

*14.2.3.1 ...*

*14.2.3.2 ...*

*14.2.3.3 If the balance is greater than 10% of the allowable revenue, there will be a full stakeholder consultation process before any pass-through is allowed.*

*14.2.4* ***The adjustment to be included in the RCA and***

***balance of the RCA will be approved by the Energy Regulator in terms of the MYPD Methodology.*** *The Energy Regulator will only have to determine the timing of when it should be passed through or clawed-back.*

*14.2.5* ***Eskom will, on a quarterly basis, present the Energy Regulator with possible adjustments based on the Methodology, the costs to date and the projections to year-end.***

*14.2.6 The Energy Regulator will review Eskom's submissions and make a preliminary assessment of any adjustments* ***required in the subsequent financial year's tariff adjustment.***

*14.2.7 The review will be performed on receipt of audited statements from Eskom."* (Court emphasis)

The RCA allows Eskom to obtain adjusted revenues for prior years by after the fact adjustments to the electricity price. Once NERSA has approved it, the adjustment is effected through price increases in subsequent years. This decision is that of NERSA only. NERSA does not agree that it has an unlimited discretion to depart from the methodology, but argues that the methodology gives NERSA the discretion to weigh up several considerations in the interest of the consumers and the South African economy.

(31) Section 10(1) of **National Energy Regulator Act**[8] **("NERA")** provides:

*"(1) Every decision of the Energy Regulator must be in writing and be-*

*(a) consistent with the Constitution and all applicable laws;*

*(b) in the public interest;*

*(c) within the powers of the Energy Regulator, as set out in this Act, the Electricity Act, the Gas Act and the Petroleum Pipelines Act;*

*(d) taken within a procedurally fair process in which affected persons have the opportunity to submit their views and present relevant facts and evidence to the Energy Regulator;*

*(e) based on reasons, facts and evidence that must be summarised and recorded; and*

*(f) explained clearly as to its factual and legal basis and the reasons therefor."*

**SEPARATION OF POWERS:**

(32) The first respondent dealt with the concepts of the separation of powers at great length. I agree with the first respondent's argument that courts are reluctant to become involved in issues of policy. However, I have to decide whether dealing with this review on the grounds of rationality, lawfulness and fairness would interfere in the sphere of policy of the executive and the implementation of the

[8] Act 40 of 2004

decision by NERSA.

(33) I am mindful of the *dictum* as set out in **Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs and Others**[9] where the court held:

> *"**In treating the decisions of administrative agencies with the appropriate respect, a Court is recognising the proper role of the Executive within the Constitution**. In doing so a Court should be careful not to attribute to itself superior wisdom in relation to matters entrusted to other branches of government. A Court should thus give due weight to findings of fact and policy decisions made by those with special expertise and experience in the field. The extent to which a Court should give weight to these considerations will depend upon the character of the decision itself, as well as on the identity of the decision-maker. A decision that requires an equilibrium to be struck between a range of competing interests or considerations and which is to be taken by a person or institution with specific expertise in that area must be shown respect by the Courts. Often a power will identify a goal to be achieved, but will not dictate which route should be followed to achieve that goal. In such circumstances a Court should pay due respect to the route selected by the decision-maker. This does not mean, however, that where the decision is one which will not reasonably result in the achievement of the goal, or which is not reasonably*

[9] 2004(4) SA 490 CC at paragraph 48

*supported on the facts or not reasonable in the light of the reasons given for it, a Court may not review that decision.* ***A Court should not rubber-stamp an unreasonable decision simply because of the complexity of the decision or the identity of the decision-maker.***" (Court emphasis)

(34) In **Logbro Properties CC v Bedderson NO and Others**[10], Cameron JA dealt with "polycentric decision-making" as follows:

*"The fact is that the committee's performance of its duty in 1997 was a prime instance of what commentators have dubbed 'polycentric decision-making'. It was not a unilinear question involving the assertion of one subject's rights against the administration. The appellant had a right to a fair tender process in 1995.... When, therefore, the committee set out to 'reconsider' the compliant tenders, it undertook the typically complex task of balancing all the public interests its mandate required it to fulfil. This included fair reconsideration of the appellant's tender - but not to the exclusion of considerations involving its broader responsibilities. These included the public benefit to be derived from obtaining a higher price by re-advertising the property."*

In paragraph 21 he dealt with judicial deference as follows:

*"It is in just such circumstances that a measure of judicial deference is appropriate to the complexity of the task that*

[10] 2003(2) SA 460 (SCA) at paragraph 20 and 21

*confronted the committee. Deference in these circumstances has been recommended as*

*'. . . a judicial willingness to appreciate the legitimate and constitutionally-ordained province of administrative agencies; to admit the expertise of those agencies in policy-laden or polycentric issues; to accord their interpretation of fact and law due respect; and to be sensitive in general to the interests legitimately pursued by administrative bodies and the practical and financial constraints under which they operate. This type of deference is perfectly consistent with a concern for individual rights and a refusal to tolerate corruption and maladministration.* ***It ought to be shaped not by an unwillingness to scrutinize administrative action, but by a careful weighing up of the need for - and the consequences of - judicial intervention. Above all, it ought to be shaped by a conscious determination not to usurp the functions of administrative agencies; not to cross over from review to appeal.'*** (Court emphasis)

(35) In **Minister of Environmental Affairs and Tourism and Others v Phambili Fisheries (Pty) Ltd; Minister of Environmental Affairs and Tourism and Others v Bato Star Fishing (Pty) Ltd**[11] the court emphasized that a court in a review application is not sitting in appeal

[11] 2003(6) SA 407 (SCA)

on the correctness of the functionary's decision, even more so where the subject matter of administrative action is very technical.

(36) The court has been warned not to intrude in the executive sphere and not to blur the separation of powers.

(37) I am thus mindful, referring to all the above decisions, that I am confined to review the procedure that NERSA had adopted in arriving at its decision. It is so that the court will deal with each review application on its own merits when considering procedural fairness, reasonableness and the balance that has to be maintained between the competing interests.

**RATIONAL, LAWFUL AND PROCEDURALLY FAIR REVIEW:**

(38) The applicants set out clearly that this court is only requested to consider whether the decision by NERSA was rational, lawful and procedurally fair in all respects. In **Democratic Alliance v President of the Republic of South Africa**[12] the court held:

> ***"It is therefore difficult to conceive how the separation of powers can be said to be undermined by the rationality enquiry.*** *The only possible connection might be that rationality has a different meaning and content if separation of powers is*

[12] 2013(1) SA 248 CC at paragraph 44

*involved than otherwise. In other words, the question whether the means adopted are rationally related to the ends in executive decision-making cases somehow involves a lower threshold than in relation to precisely the same decision involving the same process in the administrative context. This is wrong.* ***Rationality does not conceive of differing thresholds. It cannot be suggested that a decision that would be irrational in an administrative law setting might mutate into a rational decision if the decision being evaluated was an executive one. The separation of powers has nothing to do with whether a decision is rational. In these circumstances, the principle of separation of powers is not of particular import in this case. Either the decision is rational or it is not.*** " (Court emphasis)

(39) In **Albutt v Centre for the Study of Violence and Reconciliation, and Others**[13] the Constitutional Court dealt with a rationality review as follows:

*"The Executive has a wide discretion in selecting the means to achieve its constitutionally permissible objectives. Courts may not interfere with the means selected simply because they do not like them, or because there are other more appropriate means that could have been selected.* ***But, where the decision is challenged on the grounds of rationality, courts are***

[13] 2010(2) SACR 101 (CC) paragraph 51

> ***obliged to examine the means selected to determine whether they are rationally related to the objective sought to be achieved.*** *What must be stressed is that the purpose of the enquiry is to determine not whether there are other means that could have been used,* ***but whether the means selected are rationally related to the objective sought to be achieved.*** *And if,* ***objectively speaking, they are not, they fall short of the standard demanded by the Constitution. This is true of the exercise of the power to pardon under s 84(2)(j).***"
> (Court emphasis)

(40) The process by which the decision is made and the decision itself must be rationally related as set out in the abovementioned cases. In the present application the court has to decide whether NERSA applied the MYPD methodology lawfully, rationally and fairly if all the facts are considered.

**BACKGROUND:**

(41) The facts in the review are not in dispute. The applicants allege that NERSA did not comply with the MYPD methodology when it approved Eskom's RCA application and therefor the decision was unlawful, irrational and procedurally unfair.

(42) On 28 February 2013 Eskom's MYPD3 was approved by NERSA. At the same time the average percentage tariff increase for each of the years in the five year period from 1 April 2013 to 31 March 2018 were approved as follows:

> *"On 28 February 2013, the Energy Regulator approved Eskom's MYPD3 Revenue Requirement for the control period 2013/2014 to 2017/2018 as follows:*

| | 2013/2014 | 2014/2015 | 2015/2016 | 2016/2017 | 2017/2018 |
|---|---|---|---|---|---|
| ***Allowed revenues from tariffs based sales (R'm)*** | *142 746* | *155 477* | *171 838* | *189 396* | *209 025* |
| *Forecast sales to tariff customers (GWh)* | *217 890* | *219 744* | *224 877* | *229 495* | *234 519* |
| ***Standard average price (c/kWh)*** | *65.51* | *70.75* | *76.41* | *82.53* | *89.13* |
| ***Percentage price increase (%)*** | *8.0%* | *8.0%* | *8.0%* | *8.0%* | *8.0%* |
| *Total expected revenue from all customers (R'm)* | *149 937* | *163 584* | *180 378* | *196 378* | *216 322* |

(43) On 10 November 2015 Eskom submitted its RCA application for the 2013/2014 tariff year under MYPD3. This lead to the decision by NERSA that is currently under review.

(44) The application by Eskom was for an RCA balance of R22 789 million for the first financial year of the MYPD3 cycle, which was 1 April 2013

to 31 March 2014. If granted this would have the effect of increasing the average electricity tariff for 2016/2017 by a greater percentage than would have been the case otherwise.

(45) Eskom's reason for launching the RCA application was according to Eskom, the under-recovery of revenue and the incurring of higher energy costs to meet demand.

(46) On 6 January 2016 the Regulator published a notice in the Business Day Newspaper titled *"Notice on the public hearings on Eskom's Regulatory Clearing Account ("RCA") Application – Third Multi Year Price Determination (MYPD) (Year One) (2013/2014)"*. Interested parties had to submit their request to make a presentation at the public hearing to the respondent by 13 January 2016. Public hearings were conducted from 18 January 2016 until 4 and 5 February 2016 in Cape Town, Port Elizabeth, Durban, Mahikeng, Kimberley and Johannesburg.

(47) During 13 November 2015 until 22 February 2016 NERSA published Eskom's RCA application for public comment and held public hearings. Private individuals, small users, energy-intensive users, environmental activists and local government, including the sixth applicant submitted comments.

(48) On 22 February 2016 the Electricity Subcommittee ("ELS") met, after notice had been given that a special meeting of ELS would take place on this date. The meeting was held to consider the decision and reasons for the decision of Eskom's RCA application.

(49) An *aide memoire*, dated 12 January 2016 was prepared for the benefit of the ELS, which provided background information to Eskom's MYPD3 RCA application and the decision making process; analysed each of Eskom's requests and summarised and analysed the written stakeholder comments[14].

(50) On 24 February 2016, the Chairperson of the ELS signed a written report to the Regulator setting out the reasons why the Regulator should approve the draft decision and reasons for the decision of Eskom's application, as recommended by the ELS.

(51) The public was notified on the Regulator's website, as provided for in section 8(9)(a) of ERA[15] of the meeting to be held by the Regulator on 1 March 2016 to consider Eskom's RCA application. The decision and reasons were published on the Regulator's website on 29 March 2016, after NERSA had approved Eskom's RCA application on 1 March 2016.

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[14] Record page 255 item 4
[15] *Supra*

(52) According to the applicants NERSA had not complied with the MYPD methodology when it approved Eskom's RCA application and therefor the decision was unlawful, irrational and procedurally unfair.

(53) The test that must be applied in "unlawfulness" as a ground of review is whether the purpose sought to be achieved by the injunction has been achieved as set out in **Democratic Alliance v President of the Republic of South Africa and Others**[16].

(54) I find in the present application that although I am mindful of the separation of powers, it does not preclude me to consider whether the decision was rational if measured against the principles set out in the **Democratic Alliance case**[17].

(55) The first respondent argues that the decision by NERSA *"is one that required an equilibrium to be struck between a range of competing interests or considerations by the Regulator, employing specific expertise in the field of electricity and economics"*. The further argument by the first respondent, as I understand it, is that the grounds of review set out in the applicants' supplementary affidavit and the applicants' heads of argument are confusing. According to the first

[16] 2013(1) SA 248 CC at paragraph 44 (*Supra)*
[17] *Supra*

respondent the applicant relies in the supplementary founding affidavit on temporal and procedural requirements of the Methodology derived from the principles of legality and section 6(2)(a)(i), 6(2)(b), 6(2)(d), 6(2)(e)(iii), 6(2)(f)(i), 6(2)(h) and 6(2)(i) of the **Promotion of Administrative Justice Act**[18] ("PAJA"). According to the applicants both the temporal and procedural requirements in the MYPD methodology were not complied with.

(56) The applicants further contend that the ground of review based on the efficiency testing requirement of the methodology derived from the principle of legality and sections 6(2)(a)(i), 6(2)(b), 6(2)(d), 6(2)(e)(iii), 6(2)(e)(vi), 6(2)(f)(i), 6(2)(f)(ii), 6(2)(h) and 6(2)(i) of **PAJA**[19].

(57) According to the first respondent the issue stated by the applicants is whether the decision and decision-making process were lawful, rational and procedurally fair. The second respondent argues that the applicants' case is an appeal dressed up and disguised as a judicial review, as the applicants attack the correctness of NERSA's decision, not the irregularity of the decision. The second respondent's argument is that both Eskom and NERSA had complied with material procedures and conditions prescribed by the relevant laws in the result that their actions were procedurally fair.

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[18] Act 3 of 2000
[19] *Supra*

(58) The court will deal with the question whether NERSA, when NERSA made the decision, applied the MYPD methodology lawfully, rationally and fairly in this review application.

(59) In **Chairperson of the National Council of Provinces Appellant v Julius Malema and Another**[20] the Supreme Court of Appeal held:

> *"What is in dispute is whether the Chairperson [of the National Council of Provinces] lawfully and rationally applied the standing order.* ***The legality and rationality thresholds are not lowered because the decisions were made in Parliament. And testing the Chairperson's exercise of what, after all, is a public power against those thresholds falls well within the judiciary's constitutional province.*** *"* (Court emphasis)

I have to deal with the present application having regard to this finding.

(60) The decision[21] by NERSA was set out as:

> *"Based on the available information and the analysis of the Regulatory Clearing Account (RCA) Application for Year 1 (2013/2014) of the third Multi-Year Price Determination (MYPD3) the Energy Regulator, at its meeting held on 01 March 2016 decided that:*

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[20] (535/2015) [2016] ZASCA 69 (20 May 2016)
[21] Page 905

1. *the RCA balance of R11 241m be recoverable from the standard tariff customers, local SPA's and international customers in the financial year 2016/2017;*
2. *the amount of R10 257m be recoverable from standard tariff customers for the 2016/2017 financial year only;*
3. *the average tariff for standard tariff customers be increased by 9.4% for the 2016/2017 financial year only;*
4. *the amount of R983m be recoverable from Eskom's local SPA customers and international customers for the 2016/2017 financial year only; and*
5. *Eskom must submit a new MYPD application, within three months, based on revised assumptions and forecasts that reflect the recent circumstances."*

**THE GROUNDS OF REVIEW:**

(61) According to the applicants the MYPD methodology was not followed in two broad respects as NERSA did not comply with the temporal and procedural requirements set out in the methodology and did not comply with the methodology's requirements of efficiency testing. In the reasons set out by NERSA: *"The Act places an obligation on the Energy Regulator to consider an application that has been brought in terms of section 15,* ***read with the MYPD methodology***" (Court emphasis). It further set out: *"The MYPD methodology is premised on the principle that total allowed revenue has to cover all the allowed*

*costs plus a reasonable return"*[22]. NERSA stated in the decision[23]:

> *"116. The divergences from the allowed revenue and costs in the first three years of the MYPD3 are unlikely to be corrected by further submissions of RCA applications by Eskom. Thus the objectives of the MYPD methodology. Furthermore, they do not achieve the abovementioned objectives of the MYPD.*
>
> *117. There is a need to revisit and revise the assumptions for further electricity price increases in view of the current circumstances (i.e. low commodity prices, economic downturn,. generation fleet performance, maintenance strategy and implementation)."*

In the answering affidavit NERSA averred: *"The Regulator avers that its decision complied with the MYPD methodology"*[24]. This position was reiterated in the answering affidavit where NERSA stated[25]:

> *"This decision is in line with the purposive approach to the issue of substantial compliance with a statutory provision.* ***There was compliance with the MYPD Methodology****. The object sought to be achieved by the RCA procedure was achieved in this instance."* (Court emphasis)

(62) In the founding affidavit to the urgent application, the applicants

[22] Paragraph 24 footnote 913
[23] Page 927
[24] Page 1137 paragraph 106.2
[25] Page 1152 paragraph 116.2

submitted[26]:

> *"Once implemented millions of consumers will be forced to pay the unlawful portion of the electricity tariff. If NERSA's decision is subsequently set aside, it may be difficult for the applicants and the public to recover those sums. Although I am advised that an enrichment claim would lie, there may be significant hurdles. These include that it may be impossible to "unscramble the egg": overpaid amounts may be difficult to separate from the fiscus of Eskom and municipalities. A court may be unwilling to order Eskom and municipalities to reverse budgetary processes, particularly where overpaid sums have been spent on capital investment and infrastructure."*

The first respondent replied to this by stating:

> *"The applicants state that the NERSA decision was also unlawful under MYPD methodology because the RCA process should have been initiated during the 2013/2014 tariff year and completed when the Eskom financial statements were released, instead of which the RCA application was only submitted during November 2015 (paras 88-9).* ***However, this is not a peremptory requirement in terms of the applicable MYPD methodology.***"[27] (Court emphasis)

(63) In the answering affidavit NERSA changed its position and averred:

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[26] Page 44 paragraph 93
[27] Page 451 paragraph 12.5

*"The development of the Methodology does not preclude the Regulator from applying reasonable judgment to its consideration of Eskom's revenue after due consideration of the best interests of the overall South African economy and the public."*[28]

(64) This statement relied on paragraph 1 of the NERSA MYPD3 document where it is stated: *"The development of the methodology does not preclude the Energy Regulator from applying reasonable judgment on Eskom's revenue after due consideration of what may be in the best interest of the overall South African economy and the public"*[29] and adds *"...it is an oversimplification to describe the MYPD methodology as being more than guidelines".*

(65) Therefor NERSA is, on the one hand, relying on compliance with the MYPD methodology, but on the other hand it is keeping its options open by declaring it was empowered to depart from the methodology.

(66) NERSA mentioned the last-mentioned argument for the first time in its answering affidavit as it was neither raised in the RCA application, nor at the public hearings.

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[28] Page 1108 paragraph 50.2
[29] Page 5 paragraph 1

(67) The applicants argue that NERSA must decide on which facts it is relying, citing the **Chamber of Mines of South Africa v National Union of Mineworkers and Another**[30] where it was said:

> ***"One or other of two parties between whom some legal relationship subsists is sometimes faced with two alternative and entirely inconsistent courses of action or remedies. The principle that in this situation the law will not allow that party to blow hot and cold is a fundamental one of general application."*** (Court emphasis)

(68) NERSA criticizes the applicants for arguing that a "host" of documents was not included in the review record. According to NERSA the only documents not included were the bi-annual reports from Eskom. It must be mentioned that according to the methodology quarterly reports had to be furnished to NERSA and not bi-annual reports. NERSA is of the opinion that reference to the documents in the *aide memoire* of 12 January 2016 and the Chairperson's report of 22 February 2016 are adequate and therefor the bi-annual reports, which form part of the record, supports the decision by NERSA.

(69) According to the first respondent the court has to decide whether the purpose of the RCA had been met as the actual figures for the financial year had been submitted. In the summary of comments the

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[30] 1987(1) SA 668 (A) at 690 D-G

purpose of the methodology, according to the stakeholders[31]:

> *"...is to provide a clear price path and predictability. Eskom has not followed the prescribed RCA methodology in that it did not provide quarterly updates during 2013/2014.*
>
> *The stakeholders are urging NERSA to either reject the application due to procedural failure or penalise Eskom for not following process prescribed in the MYPD methodology."*

NERSA conceded that quarterly reports were not submitted, but did not deal with concerns regarding the purpose of the methodology.

(70) The second respondent argues that the applicants have mistakenly argued that procedural requirements are considered on their own merits, instead of concentrating on the final outcome. In **Allpay Consolidated Investment Holdings (Pty) Ltd and Others v Chief Executive Officer, South African Social Security Agency, and Others**[32] the court found:

> *"Under the Constitution there is no reason to conflate procedure and merit. The proper approach is to establish, factually, whether an irregularity occurred. Then the irregularity must be legally evaluated to determine whether it amounts to a ground of review under PAJA.* ***This legal evaluation must, where appropriate, take into account the materiality of any***

[31] Page 278 paragraphs 133 and 134
[32] 2014(1) SA 604 CC at paragraph 28

***deviance from legal requirements, by linking the question of compliance to the purpose of the provision, before concluding that a review ground under PAJA has been established.***" (Court emphasis)

(71) The purpose of the temporal requirement appears from paragraph 14.2 of the MYPD methodology. Both NERSA and Eskom conceded that Eskom had not provided quarterly reports as regular alerts to customers of any possible adjustment in the coming tariff year.

(72) Should I find that there was a deviation from the methodology then the question will be whether the deviation from the methodology was done arbitrarily, irrationally or unfairly and whether the purpose of the RCA application has been met. The applicants' argument is that NERSA published the methodology and created the impression that it would be followed as there was no notification at any time to any party that there would be a deviation from the methodology when considering the RCA application. This, according to the applicants, is unlawful as set out in **Premier, Mpumalanga, and Another v Executive Committee, Association of State-Aided Schools, Eastern Transvaal**[33] where O'Regan J held that:

*"Expectations can arise either where a person has an expectation of a substantive benefit,* ***or an expectation of a***

[33] 1999(2) SA 91 (CC) at paragraph 36

> ***procedural kind**. There are also circumstances in which a legitimate expectation will arise which has interrelated substantive and procedural elements, as Corbett CJ also recognised in Traub (at 758F). Once a person establishes that a legitimate expectation has arisen, it is clear from the language of s 24(b) of the interim Constitution that he or she will be entitled to procedural fairness in relation to administrative action that may affect or threaten that expectation".* (Court emphasis)

(73) NERSA relies on paragraph 1 of the MYPD methodology as set out above, but that does not absolve NERSA from justifying a decision to deviate and to publish the reasons for such a deviation so that the public can make an informed decision whether to oppose such a deviation and to deal with such a deviation. This NERSA did not do and only relied on this ground for the first time in the answering affidavit. In **MEC for Agriculture, Conservation, Environment and Land Affairs v Sasol Oil (Pty) Ltd and Another**[34] the Supreme Court of Appeal found:

> ***"The adoption of policy guidelines by state organs to assist decision-makers in the exercise of their discretionary powers has long been accepted as legally permissible and eminently sensible. This is particularly so where the decision is a complex one, requiring the balancing of a range of competing interests or considerations**, as well as*

[34] 2006(5) SA 483 (SCA) at paragraph 19

*specific expertise on the part of a decision-maker. As explained in Bato Star Fishing (Pty) Ltd v Minister of Environmental Affairs, a court should in these circumstances give due weight to the policy decisions and findings of fact of such a decision-maker.* ***Once it is established that the policy is compatible with the enabling legislation, as here, the only limitation to its application in a particular case is that it must not be applied rigidly and inflexibly, and that those affected by it should be aware of it. An affected party would then have to demonstrate that there is something exceptional in his or her case that warrants a departure from the policy.*** " (Court emphasis)

I find that NERSA was obliged to inform the customers and public in general that it intended deviating from the methodology and to provide reasons for the deviation to the affected parties, as set out in the above case.

**FIRST GROUND OF REVIEW: TEMPORAL/PROCEDURAL:**

(74) The applicants rely on the temporal requirements of the MYPD methodology as set out in section 14, which governs RCA applications. The argument by the applicants is that there exist several textual markers which temporally provide that an RCA application should relate to the tariff year. According to this argument Eskom is not permitted to submit and NERSA to evaluate a RCA application beyond

that time limit.

(75) The temporal requirement is set out in sections 14.2.1, 14.2.2 and 14.2.6 under the heading *"The Regulatory Clearing Account"* ("RCA").

(76) The RCA is used to debit or credit potential adjustments to Eskom's allowed revenue and it is clearly stated that it *"must be used as follows"*, which includes the aforementioned paragraphs.

(77) In the present instance the RCA application for the 2013/2014 tariff year was submitted on 10 November 2015 and not during 2013/2014. The applicants argue, firstly that Eskom did not open an RCA account and provide quarterly updates as required by the methodology in section 14. Secondly, that Eskom should have applied earlier to NERSA for this tariff increase. This was admitted by NERSA in the answering affidavit where it set out the facts of compliance as[35]:

> *"112.1.2.1 Eskom **did not open an RCA** in the 2013/2014 year.*
>
> *112.1.2.2 It **did not submit quarterly** RCA reports to the Regulator.*
>
> *112.1.2.3 It submitted two "bi-annual" RCA reports in around October 2014 to the Regulator.*
>
> *112.1.2.4 It submitted a proper MYPD3 RCA Application **in***

[35] Page 1143 paragraph 112.1.2

***November 2015.***

*112.1.2.5 It submitted its audited annual financial statements for the 2013/2014 year to the Regulator in* ***July 2014.***" (Court emphasis)

(78) According to NERSA the issue is not whether Eskom proved that it had complied with the MYPD methodology, but whether the Regulator was satisfied with Eskom's compliance with the MYPD methodology. Eskom submitted its annual financial statements as early as 11 July 2014, 27 months before launching the RCA application.

(79) The applicants argue that the failure to adhere to the procedural and/or temporal requirements defeated the purpose of a RCA application by not giving Eskom's customers regular quarterly alerts of possible price adjustments in the coming year, so that the customers and South African public at large could take it into account when planning for the future.

(80) In **Allpay Consolidated Investment Holdings (Pty) Ltd and Others v Chief Executive Officer, South African Social Security Agency, and Others**[36] the court found:

[36] *Supra* at paragraph 30

*"That strict mechanical approach has been discarded. Although a number of factors need to be considered in this kind of enquiry, the central element is to link the question of compliance to the purpose of the provision. In this court O'Regan J succinctly put the question in ACDP v Electoral Commission as being* ***'whether what the applicant did constituted compliance with the statutory provisions viewed in the light of their purpose'. This is not the same as asking whether compliance with the provisions will lead to a different result.*** *"* (Court emphasis)

The argument by the applicants is that the provisions of section 14.2.1, 14.2.2 and 14.2.6 are peremptory due to the fact that section 14.2.1 sets out that the RCA *"will be created at the beginning of the financial year"* and section 14.2.2 sets out that the account has to be updated quarterly. This is also set out in peremptory language, *"This account must be updated quarterly..."* and *"Eskom must therefore submit actual financial data on a quarterly basis"*. NERSA *"will make a preliminary assessment of any adjustment required in the* ***subsequent financial year's tariff adjustment***". Although our law no longer relies on terms of *"peremptory"* or *"directory"*, the purpose of the provision, in this instance section 14.2 of the MYPD methodology must guide the court's enquiry to consider the statutory provisions "*in the light of their purpose*".

(81) NERSA's argument is that the purpose of the methodology and the

regulation of RCA applications is to *"ensure Eskom's sustainability as a business and to limit the risk of excess or inadequate returns"*. This does not acknowledge the purpose as set out in section 14.2.2 of the methodology.

(82) The further argument is that the proper approach is that the issue of compliance with the statutory requirements is whether the jurisdictional facts have been complied with. NERSA argues that the court has to determine the purpose of the legislation and measure the decision against it. The second respondent, Eskom, argues that the court has to interpret section 14.2 of the Methodology sensibly and contextually. The court agrees with this, but the question is whether NERSA complied with the provision of section 14 of the Methodology in view of the purpose of the methodology.

(83) The argument is that Eskom's auditors had confirmed that the RCA application had complied with the MYPD3 methodology. Eskom further relies on section 17 of the MYPD methodology and argues that NERSA will conduct a review of the MYPD methodology, but that special circumstances may arise, resulting in NERSA making changes to the methodology as set out in section 17.1 of the MYPD Methodology[37]. Section 15(3) of **ERA**[38] provides that NERSA may in prescribed circumstances approve a deviation from set or approved

[37] Record page 33
[38] *Supra*

tariffs.

(84) In this regard Eskom disagrees with NERSA as to the purpose of the RCA and section 14.2 of MYPD Methodology and sets out[39]:

> *"9.5.2.1 creation, monitoring and quarterly updates by Eskom of a RCA to alert customers of possible adjustment in the coming year;"*

And

> *"22.1* ***Save to admit that the creation of the RCA, quarterly updates of the RCA and submissions by Eskom in terms of section 14.2 of the MYPD Methodology are (i) meant for regular alerts to consumers of any possible adjustment in the coming year and (ii) NERSA's preliminary assessment of any adjustment required****, the remainder of the allegations contained in these paragraphs are denied."* (Court emphasis)

The contents of these paragraphs correspond with the applicants' submission as to the purpose of section 14.2.2 of the RCA application.

(85) NERSA concedes that the RCA serves a signalling function, but argues that this is only one aspect, whilst NERSA viewed it as part of the whole paragraph on the RCA, contrary to the applicants' view that

[39] Page 1286 paragraph 9.5.2.1; Page 1300 paragraph 22.1

it impacts on the whole process. The further argument by NERSA is that quarterly alerts would not be a reliable basis for customers to do forward planning as to future expenses, as Eskom's RCA balance varies throughout different times of the year. This may be so, but it is precisely for this reason that the account must be updated quarterly in terms of section 14.2.2 to alert customers as to possible future increases or decreases.

(86) It is further common cause that Eskom's financial statements were available, in this instance, for the 2013/2014 tariff year in July 2014, although a RCA application was only launched in November 2015. There is no real explanation for the delay of the application for more than a year. According to NERSA an implementation of an MYPD2 balance resulted in a tariff increase from 1 April 2015 and that it would not have been feasible and undesirable to consider a double increase in the same year. This does not explain why the RCA application could not have been launched as soon as the audited financial statements for 2013/2014 tariff year became available in July 2014 and could have been dealt with in 2014.

(87) The argument, by Eskom, is that the methodology has a signalling function and is separate from NERSA's assessment of the RCA application. Therefor a failure to comply with section 14.2, does not impact on section 14.1 of the MYPD. Eskom sets out that the audited

financial statements are traditionally made available in July of every year. In the present instance Eskom's RCA application was only submitted and evaluated in 2015. The applicants argue that this breach of section 14.2 resulted in NERSA's decision to be irrational. According to NERSA Eskom's audited financial statements were available and submitted to NERSA in July 2014. NERSA's submission that[40]:

> *"...the soonest that the tariff increase (or decrease) can be assessed is in the financial year following the year in which the revenue was generated and/or the expenditures were incurred. This means that the increase (or decrease) can only be effected in a subsequent financial year (and after assessment); effectively in the second year after the relevant tariff year. Eskom's RCA application was therefore not out of time..."*

I cannot agree with this statement as the audited financial statements had been available for the 2013/2014 tariff year, at the latest in July 2014 and the tariff increase could and should have been assessed in the 2014 tariff year.

(88) Eskom submits that section 14 and the MYPD methodology as a whole do not prescribe any time limits for the submission of the RCA application. This statement disregards the provisions of section 14.2.6 of the Methodology.

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[40] Page 1092 paragraph 23

(89) Eskom admits that it did not comply with most of the procedural requirements as follows[41]:

> *"It should also be born in mind that the process for the MYPD2 RCA which covered a period (2010/11 – 2012/13) was started in August 2013 and ended in November 2014. It took a long time to implement. Since it was the first time it was implemented, there were discussions and clarifications that occurred.* ***Eskom had to see the process through to the final decision of NERSA before submitting next RCA, since the one for MYPD2 would, amongst other things, set precedents****. As already indicated, the initial submission of the MYPD2 RCA was made during August 2013. The MYPD2 RCA balance, implementation and tariff decisions were made between March 2015 and November 2015. During this period several discussions were held between the parties, and some agreements were reached."* (Court emphasis)

And

> ***"It is admitted that Eskom does not have any records as contemplated by clause 14.2.1, 14.2.2, 14.2.4, 14.2.5 and 14.2.7****. Although NERSA agreed with the stakeholders that the quarterly reports were not submitted by Eskom, NERSA further stated that the requirements in section 14.2 are for monitoring*

[41] Page 1302 paragraph 23.2; Page 1303 paragraph 24.1

*purposes and that Eskom submitted both the bi-annual reports and the audited financial statements. It has already been indicated that the RCA submitted by Eskom should be measured for compliance with section 14.1 of the MYPD Methodology in relation to its content and the audited financial statements are the basis for determining the RCA application as compared to the quarterly reports that would not have been audited and are only required for the monitoring purpose in section 14.2 that informs public alertness and NERSA's preliminary assessments."* (Court emphasis)

It is thus clear that the MYPD methodology, which was put in place, was to assist both Eskom and NERSA when required to deal with an RCA application, but furthermore and foremost to inform the SA public, businesses and consumers as to how further price increases are to be expected and to ascertain what impact it may have on their future business and the economy as a whole. The concession by both Eskom and NERSA that quarterly reports had not been submitted by Eskom and the concession by Eskom as to the purpose of the quarterly reports, must result in the court finding that the non-compliance with the MYPD methodology in this regard was irrational, unfair and therefor unlawful.

(90) The reasons for the decision were published by NERSA on 29 March 2016 as set out above. In the answering affidavit by Fransiskus Esser

Hinda the respondents produced the following reasons for the decision[42]:

> *"13.1 the timing of the release of Eskom's audited annual financial statements meant that the MYPD methodology could not be complied with;*
>
> *13.2 NERSA was permitted to deviate from the methodology;*
>
> *13.3 Eskom was advised in its various pricing applications by an executive "War Room"; and*
>
> *13.4 There were various "discussions and clarifications" between NERSA and Eskom, presumably about Eskom's RCA applications and its compliance with the MYPD methodology."*

(91) These new reasons were submitted *ex post facto* and did not form part of the Rule 53 record and were not dealt with by NERSA in the March 2016 decision and were thus not the basis on which NERSA relied when coming to the decision in this instance.

(92) As already set out above, the timing of the release of Eskom's audited annual financial statements could not have played a role as to why NERSA could not comply with the MYPD Methodology as these statements had already been available in July 2014.

(93) These reasons were not dealt with during the decision making, nor

[42] Page 7 of Applicants' Heads of Argument

were they canvassed at the public hearings. The applicants' argue that if these documents do not form part of the Rule 53 record and were not before NERSA at the time of the decision and are now supplied as reasons for the decision, then the court must decide that the decision is unlawful. NERSA relies on the fact that NERSA is expressly given the power to determine the timing when the RCA balance should be passed through or clawed back, referring to[43]:

> *"The adjustments to be included in the RCA and balance of the RCA will be approved by the Energy Regulator in terms of the MYPD Methodology. The Energy Regulator will only have to determine the timing of when it should be passed through or clawed-back."*

The Regulator uses the example that the respondents may, in the customer's interest, spread the tariff increase, pursuant to an RCA balance over two years. This may be so, but in this instance the adjustment did not take place in the subsequent financial year as is provided for in section 14.2.6 of the Methodology and once more NERSA did not comply with the provisions of its own methodology. I must agree with the applicants that by submitting the RCA application 27 months after the first quarterly report was due, the consumers were confronted by a *fait accompli*. There is thus no certainty to consumers if Eskom can draw on the RCA years after the particular tariff year had lapsed.

[43] Page 81 paragraph 14.2.4

(94) In **Allpay**[44] it was decided that *"if there has been compliance with the injunction the object sought to be achieved by the injunction and the question whether this object has been achieved are of importance"*. In this instance NERSA found[45]:

> *"The application is procedurally correct in that actuals for the full financial year have been submitted in line with the provisions of the MYPD methodology."*

This cannot be correct as Eskom had not complied with the methodology by providing quarterly reports and did not comply with section 14.2.6 of the MYPD methodology. Eskom waited for more than a year after the annual financial statements were available to launch the RCA application in November 2015.

(95) I find that NERSA had to adhere to the methodology and cannot rely on substantial compliance, although no quarterly reports had been filed. Section 14.2.4 of the MYPD Methodology sets out in clear terms:

> *"The adjustments to be included in the RCA and balance of the RCA will be approved by the Energy Regulator in terms of the MYPD Methodology."*

There can be no doubt that section 14.1 cannot be divorced from section 14.2 when deciding whether NERSA had reviewed the temporal and procedural aspects of the RCA application. Eskom has conceded that it did not comply with section 14.2.5 by only providing

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[44] *Supra*
[45] Record page 342 paragraph 12

bi-annual adjustments and projections of costs to year-end based on the methodology and not doing so on a quarterly basis. NERSA did not comply with the provisions of section 14.2.6 as NERSA did not adhere to the temporal aspect. I find that NERSA did not apply the MYPD methodology in the temporal and procedural aspects.

(96) If I apply the test as set out in **Allpay**[46] then I have to decide whether the non-compliance by NERSA of the methodology has an impact on the purpose of the provisions. NERSA did not inform any of the applicants, customers or the South African public that it intended deviating from the methodology and did not set out and inform the public to which extent it would deviate from the methodology or at all. NERSA published the methodology and I find that the deviation from the methodology causes such serious consequences to the applicants, business and customers in South Africa that the decision was irrational, unfair and unlawful.

**SECOND GROUND OF REVIEW: EFFICIENCY:**

(97) I will deal with the second ground of review as well, should it be found that I was wrong in my decision on the first ground of review. The second ground of review is the failure to test the efficiency of Eskom's costs. The applicants submit that the primary purpose of the RCA is to facilitate price adjustments if pricing assumptions do not hold. There

[46] *Supra*

should be a rational relationship between this purpose and NERSA's decision. The applicants argue that the efficiency of Eskom is central to the regulatory framework and that the respondents failed to test for the efficiency of the costs at all, or did so irrationally.

(98) In the answering affidavit NERSA set out that this is not the only reason, as the applicants also rely on alerting customers to a possible increase. This is so, but then NERSA sets out that[47]:

> *"...ensuring Eskom's sustainability as a business and limiting the risk of excessive or inadequate returns; and appropriately allocating commercial risk between Eskom and its customers. Also the Regulator may consider what is best for the overall South African economy and public."*

NERSA further argues that Eskom claimed an increase in the RCA application in the amount of R22 789 billion, whilst NERSA only granted R11 241 billion.

(99) The applicants' submission in this regard is that the purpose of the RCA is not a survival mechanism for Eskom, as taxpayers and the RCA cannot be utilized to come to the rescue of Eskom, when Eskom do not pass the efficiency test. Therefor the strict controls imposed by the MYPD methodology should apply to decide when Eskom can draw on the RCA. NERSA is obliged to act independently, lawfully and fairly

[47] Page 1156 paragraph 121.1.1

in deciding a RCA application and to consider the impact the decision will have on the South African economy.

(100) Section 15(1) of the **ERA**[48] provides as set out above.

Efficiency is the cornerstone for electricity tariffs. The EPP set out[49]:

> *"a. must enable an efficient licensee to recover the full cost of its licensed activities, including a reasonable margin or return;*
>
> *b. must provide for or prescribe incentives for continued improvement of the technical and economic efficiency with which services are to be provided;*
>
> *c.* ***must give end users proper information regarding the costs that their consumption imposes on the licensee's business;"*** (Court emphasis)

And set out in the table of objectives as:

> *"Price levels should assume an efficient and prudent utility, in other words, prices should be based on least cost options* ***and exclude inefficiencies"***. (Court emphasis)

(101) The methodology deals with efficiency throughout as it requires expenses to be *"prudently and efficiently incurred"* and NERSA to

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[48] *Supra*
[49] *Supra*

*"decide on incentives to Eskom to minimise costs that are under its control as well as to encourage Eskom to reduce some of the costs that are not under its control".*

(102) As set out above section 15(1)(a) enables the licensee to recover the full cost of its licensed activities, including a reasonable margin of return. Adjusting for changes in the inflation rate, adjusting capital expenditure forecasts for costs and timing variances and adjusting for other costs and revenue variances where the variance of total actual revenue differs from the total allowed revenue are not subjected to the prudency assessment in the Methodology.

(103) In **Foodcorp (Pty) Ltd v Deputy Director-General, Department of Environmental Affairs and Tourism: Branch Marine and Coastal Management, and Others**[50] Harms JA founds:

> ***"A reasonable decision-maker would, in my judgment, have used a formula to make a provisional allocation but would have considered the output as a result of the application of the formula and then have considered whether the output gives reasonably justifiable results bearing in mind the facts."*** (Court emphasis)

I agree with the first respondent that efficiency is not the only criterion and that NERSA may not limit its decision making by adherence to a

[50] 2006(2) SA 191 SCA at paragraph 19

fixed rule of efficiency. It is however one of the facts that have to be considered and dealt with in a transparent manner. This did not take place in this RCA application as NERSA did not deal with efficiency in an adequate manner, or at all.

(104) Independent Power Producers ("IPP") are entities, other than Eskom, that owns or operates independent power generation facilities. Purchases by Eskom of electricity from independent power producers ("IPB") must be reviewed by NERSA for efficiency and prudency of these amounts before and after they are concluded and *"Each pass-through cost will be reviewed by the Energy Regulator to determine the* ***efficiency and prudence with which pass-through costs have been incurred above***". (Court emphasis)

(105) It is thus, according to the applicants, incumbent on NERSA to test the efficiency of the costs claimed in a RCA application. It seems as if NERSA did not deal with this part adequately or at all and does not pass the test as set out above in **Foodcorp**[51].

(106) The applicants submit that the court has to decide whether NERSA applied an efficiency test to the cost categories that were allowed, either rationally or at all. The argument is that NERSA did not apply its mind within the framework of the MYPD methodology to the actual

[51] *Supra*

costs incurred in the agreement with Aggreko International Projects Limited, an IPP, in Mozambique. This agreement was approved by NERSA in May 2011.

(107) In the RCA application and the decision by NERSA, the prudency and efficiency of costs incurred in terms of the Aggreko agreement, there is no indication that NERSA tested the efficiency and prudency of costs incurred once more, but relied on its approval of the agreement in May 2011. In paragraphs 49, 50 and 51 of the decision NERSA set out[52]:

> *"49. The Independent Power Producer (IPP) costs were based on approved Power Purchase Agreement (PPA) contracts submitted by Eskom.*
>
> *50. Therefore Eskom is allowed the variance of R580m with regard to IPP costs in its favour.*
>
> *51. The purchase of power from the regional IPP was approved by the Energy Regulator when generation performances deteriorated as a cheaper option."*

This was thus not done in accordance with paragraph 9.2 of the EPP. NERSA argues that[53]:

> *The "review" of each pass-through cost by the Regulator for efficiency and prudence means the Regulator's consideration thereof and not its decision thereon. It cannot be that the Regulator authorises a PPA and then refuses to allow costs*

[52] Page 917 paragraphs 49, 50 and 51
[53] Page 1171 paragraph 126.4

*incurred in terms of the agreement."*

(108) This is contrary to what is stated in paragraph 9.2 and 9.9 in the EPP, as it requires NERSA to review the efficiency and prudency of the IPP before and after contracts are concluded. The applicants argue that without efficiency testing there is no rational connection between the decision by NERSA and the efficiency purpose of the methodology. This review by NERSA would not have impacted on the agreement which was in place at the time, but NERSA had to consider whether the variance of R580 million was in line with the efficiency review. If NERSA found that the variance was due to Eskom's inefficiency, it should not have allowed the variance. The original agreement with Aggreko would not have been affected and no breach of contract would have taken place.

(109) In the present instance NERSA allowed a variance for decreased revenue, but this could only be done if the lower sales had not been due to Eskom's own inefficiencies. NERSA ignored the fact that Eskom actively encouraged its consumers to use less electricity and provided monetary incentives to consumers in this regard. According to the applicants this conduct by Eskom is irrational and the decision by NERSA to compensate Eskom for the lesser income, is therefore irrational, unfair and thus unlawful.

(110) I must agree that this results in double-counting. Eskom receives money from the consumers, pay money to other consumers to use less electricity which results in a decreased income for Eskom and then NERSA decides to grant a RCA increase to compensate for the decreased income. This decision does not impact on the IPP's as they are the beneficiaries of further costs incurred by Eskom from them and has no relation to the contracts already concluded with the IPP's. The Methodology requires the IPP variances must be assessed for efficiency during a RCA application. The first respondent maintains that it is not only the methodology that should be considered, but that the relevant law is contained in the Regulatory Rules for Power Purchase Cost Recovery[54] ("Rules") as well as the methodology.

(111) Although the Rules provide that, once the Regulator has authorised power purchase cost recovery *"costs incurred will be allowed as a pass-through for the duration of the PPA"*, this will not exempt the Regulator to ensure that the efficiency assessment of the use of the IPP's is consistent with the methodology. I do not understand the applicants to argue that costs incurred in terms of the agreement should not be allowed, but that the variance which was allowed by NERSA should have been tested for prudency and efficiency. There is no indication that this would result in a breach of contract with the IPP's.

[54] GNR119 in GG32964 of 22 February 2010

(112) NERSA stated in the decision[55]:

> *"The inclusion of actual cost of electricity generated in South Africa as part of net export is disallowed as it is already accounted for in the total primary energy variances."*

The decision by NERSA is in variance with its own findings where NERSA found that Eskom could only achieve an EAF of 75.1%, whilst the target was 81.5%. NERSA is forced to test the efficiency of the costs claimed by Eskom and find that the cost claimed were efficiently incurred.

(113) Eskom acknowledges that many of the costs incurred were due to inefficiencies on the part of Eskom. Furthermore NERSA took into consideration the decrease in revenue where Eskom actively encouraged consumers not to use electricity. I have dealt with this phenomenon already, but find this to have been irrational. I find, due to my findings on inefficiency that NERSA failed to apply the MYPD methodology benchmark on efficiency by not testing it or testing it irrationally. NERSA did not discharge its statutory and regulatory mandate.

(114) I cannot find that NERSA's decision is due to incompetence or bias from the Regulator. I find it was irrational for NERSA not to have the

[55] Page 921 paragraph 77

quarterly financial reports for the 2013/2014 year, not to alert consumers and the public that it intended to deviate from the MYPD methodology and not to allow the consumers and public to deal with the deviation in the public hearings and submissions to NERSA. I further find that it was irrational, unfair and unlawful to not deal with the deviation in 2014, which was the subsequent year, but to wait 27 months before launching the RCA application. Furthermore, it was irrational of NERSA to grant the RCA application, not dealing properly with the inefficiencies of Eskom, and allowing an adjustment to the agreement with Aggreko International Projects Limited by passing it through without any consideration as it was supposed to do. I find that due to all the above-mentioned actions and non-compliance with the MYPD methodology in regards to the temporal and procedural requirements, as well as the efficiency requirement, the decision by NERSA was irrational, unfair and unlawful and should be set aside.

**REMEDY:**

(115) Eskom argues that it will not be in the interest of justice should the court hand down a declaratory order if regard is being had of the impact it will have on the whole economy. I have, at the outset, indicated that I am aware of the issues in this review application and that I will not make a decision which will intrude in the other spheres of government, but will deal with the review at hand as set out in **National Treasury and Others v Opposition to Urban Tolling**

**Alliance and Others**[56].

(116) In **Fose v Minister of Safety and Security**[57] the Court held:

> *"When Courts give relief, they attempt to synchronise the real world with the ideal construct of a constitutional world created in the image of s 4(1). There is nothing surprising or unusual about this notion. It merely restates the familiar principle that rights and remedies are complementary. The relationship holds true and is uncontroversial at common law. The Constitution is also a body of legal rules and we should expect to find in it the same pairing of rights and remedies."*

(117) I do agree with Mr Gauntlett that it will not be in the interest of justice to issue a declaratory order if the impact on the economy of South Africa is considered.

(118) Section 15(2) of **ERA**[58] precludes this court from determining a tariff as it provides:

> *"A licencee may not charge a consumer any other tariff...other than that determined or approved by the regulator as part of its*

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[56] 2012(6) SA 223 CC at paragraphs 44, 68 and 70

[44] ... This means that the Constitution requires courts to ensure that all branches of government act within the law. However, courts in turn must refrain from entering the exclusive terrain of the executive and the legislative branches of government unless the intrusion is mandated by the Constitution itself.

[57] 1997(3) SA 786 CC at page 834 G-H

[58] *Supra*

*licencing conditions."*

(119) The respondents argue that this court cannot set aside the RCA increase as it is indivisible from the tariff approved by NERSA under MYPD3. I do not agree with this argument, as the MYPD3 decision is not reviewed. At the time NERSA approved the RCA application it did not re-evaluate and re-approve the MYPD3 decision. The only decision currently under review is the approval of the RCA application.

(120) I agree with the applicants that a just and equitable remedy has two functions by, firstly, ensuring that there are no undue interruption to the provision and pricing of electricity and, secondly, to ensure that consumers who have overpaid receive just and equitable relief.

(121) The question is whether the court can deal with this, without interfering with the executive arm of government. There are two types of electricity tariffs; the tariff Eskom charges its customers and the tariff charged by municipalities to their ultimate customers. The applicant set out in great detail how the overpayments can be dealt with as Eskom had already indicated in its answering affidavit[59] that the applicants' prejudice is commercial and limited and it can be addressed by crediting customers, whether directly or indirectly, dependant whether they are direct or indirect customers.

[59] Page 394 and 395 paragraph 7.7

(122) I agree with the applicants that, even if the RCA increase is set aside, the revenue approved for the 2016/2017 tariff year will remain in force, as well as the direct tariff to customers and the tariff to municipalities.

(123) I was referred to the case of **Organisation Undoing Tax Abuse v The National Energy Regulator of South Africa and Others**[60] where the court held:

> *"Of critical importance, in my view, is that according to NERSA, should the tariff have been interdicted there would have been no tariff applicable at all as from 01 April 2016 onwards, as section 15(2) of ERA proscribes the charging of the tariff other than the one approved by NERSA. Mr Raath retorted that the tariff which applied before 01 April 2016 would continue to apply. I disagree. My understanding of the tariff regulation regime applicable here is that, each tariff is borne by its own circumstances. So the previous tariff as approved by NERSA could never have been the default or fall-back position, when the increased tariff was set aside. The reason being that the justification of the tariff approved and imposed, is in terms of the realities of ESKOM's business, as approved by NERSA."*

I cannot agree with this finding, as the tariff for 2016/2017 can be separated from the tariffs as set out in the decision.

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[60] (24365/2016) [2016] ZAGPPHC 479 (8 April 2016) at paragraph 55

(124) In **Minister of Environmental Affairs and Tourism and Others v Phambili Fisheries (Pty) Ltd; Minister of Environmental Affairs and Tourism and Others v Bato Star Fishing (Pty) Ltd**[61] Schutz JA held:

> *"Judicial deference is particularly appropriate where the subject-matter of an administrative action is very technical or of a kind in which a Court has no particular proficiency."*

This is the case in this instance.

(125) I agree that section 8(1)(c)(ii) of PAJA only permits a court in exceptional cases to substitute the court's finding for that of NERSA. I will not usurp the decision making powers of NERSA as in **Trencon Construction (Pty) Ltd v Industrial Development Corporation of South Africa Ltd and Another**[62] the court found:

> *"In our constitutional framework a court considering what constitutes exceptional circumstances must be guided by an approach that is consonant with the Constitution. This approach should entail affording appropriate deference to the administrator. Indeed, the idea that courts ought to recognise their own limitations still rings true. It is informed not only by the deference courts have to afford an administrator but also by the* ***appreciation that courts are ordinarily not vested with the***

[61] 2003(6) SA 407 (SCA) at paragraph 53
[62] 2015(5) SA 245 (CC) at paragraph 43

***skills and expertise required of an administrator.*** " (Court emphasis)

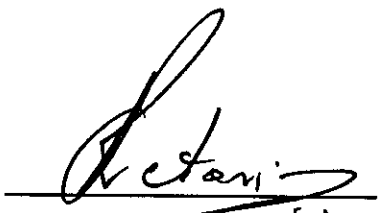
(126) I cannot find exceptional circumstances and therefor I will not substitute the decision as requested by the applicants.

(127) I have been furnished with draft orders by both the applicants and the respondents on 13 August 2016, with notes by both parties. I have considered these draft orders, as well as the comments. Once more counsel have been able to assist the court in this regard. The order of Manamela AJ in the interim application on 31 March 2016 in regard to costs was: *"The costs of this hearing shall be reserved"*. Therefore I will deal with the costs of the interim application as well.

(128) In the result the following order is made:

1. The decision published by the first respondent on 1 March 2016 in relation to the Regulatory Clearing Account ("RCA") application by the second respondent – third Multi Year Price Determination (MYPD3) Year 1 (2013/2014) (the "Decision") is reviewed, set aside and remitted to the first respondent.
2. It is directed that all future RCA applications by the second respondent in relation to the MYPD3 must be submitted and evaluated in accordance with paragraph 14 of the MYPD3 Methodology, or any future amendment thereof.

3. The first and second respondents are to pay the costs of this application jointly and severally, as well as the costs occasioned by the interim application of 31 March 2016, including the costs of three counsel.



Judge C Pretorius

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| Case number | : 24364/2016 |
| Matter heard on | : 14 & 15/06/2016 |
| For the Applicants | : Adv DN Unterhalter SC |
| | Adv M Du Plessis |
| | Adv J Mitchell |
| | Adv ALS Msimang |
| Instructed by | : Couzyn Hertzog & Horak |
| For the First Respondent | : Adv DM Fine SC |
| | Adv A Pantazis |
| Instructed by | : Hogan Levells (SA) Inc |
| For the Second Respondent | : Adv JJ Gauntlett SC |
| | Adv SM Lebala SC |
| | Adv EM Baloyi-Mere |
| Instructed by | : Ledwaba Mazwai Attorneys |
| Date of Judgment | : 16 August 2016 |