

Unplugging corruption at Eskom

A report by the Organisation Undoing Tax Abuse (OUTA) to the
Portfolio Committee on Public Enterprises

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UNPLUGGING CORRUPTION AT ESKOM

A. INTRODUCTION

- i. This report outlines some of the most significant allegations against Eskom Holdings SOC Ltd. While many of these allegations and incidents are already in the public domain, together they outline a pattern of behaviour which urgently needs addressing by oversight bodies like the Portfolio Committee on Public Enterprises: Eskom's secrecy, inadequate public reporting and manipulation of policies and procedures has allowed what appears to be the establishment of questionable practices as "norms" or routine, which is a way of legitimising and entrenching corruption. This behaviour has been endorsed by the habitual and alarming dismissal by those in authority of almost all investigations into corrupt activities, irrespective of how authoritative and damning they may be.

- ii. Decisions by organs of state relating to procurement are not only limited to the right to just administrative action as contemplated in 33 of the Constitution. The Constitutional Court in *Allpay Consolidated Investment Holdings (Pty) Ltd v South Social Security Agency* 2014 (1) SA 604 (CC) indicated that "it is because procurement so palpably implicated socio-economic rights that the public has an

interest in it being conducted in a fair, equitable, transparent, competitive and cost-effective manner.”

- iii. Deviations from due process in procurement may themselves be symptoms of corruption or malfeasance in the process. Corruption poses a real danger to South Africa’s developing democracy as it undermines the ability of SOEs to meet their commitments to deliver services to the public and contribute meaningfully to the economy.
- iv. It should be noted that OUTA does not claim that this document is an investigative report. Extensive investigations have already been conducted by an array of entities into irregularities within Eskom. These investigative reports have not been attached to this document, as they are already in the public domain and subject to severe scrutiny.
- v. OUTA submits that it would be redundant to illustrate every allegation contained in the various investigative reports. For this reason, OUTA wishes to assist the Parliamentary Portfolio Committee on Public Enterprises in essentially “joining the dots”.
- vi. OUTA calls on the Portfolio Committee on Public Enterprises to consider the weight of evidence on corruption and malfeasance against those in charge of Eskom, or previously in charge, consider the available investigations on these matters and their

recommendations, and find a way to action those investigations and recommendations to rescue Eskom.

B. MANDATE & INTRODUCTION

1. OUTA is a proudly South African non-profit civil action organisation, supported and publicly funded by people who are passionate about improving the prosperity of our nation. OUTA was established to reintroduce accountability to government and to challenge the abuse of authority with regards to taxpayers' money in South Africa.
2. On 28 June 2017, OUTA published its "*No Room to Hide: A President Caught in the Act*" report. A copy of this report was distributed to Members of Parliament and other interested parties. The report identified, *inter alia*, irregularities within state-owned entities, maladministration within the executive sphere of government as well as improper relationships between state officials and the Gupta family.
3. The report primarily aimed to furnish Parliament with substantial information regarding President Jacob Zuma's misconduct in relation to the series of events presented in the report.
4. In publishing the allegations as set out in the "*No Room to Hide*" report, OUTA wishes to assist the Parliamentary Portfolio Committee on Public Enterprises ("the Committee"), by supplementing its initial findings. This supplementary report will set out the chronological narrative on the proliferation of corruption within Eskom.

5. OUTA has identified some key events, in addition to the common allegations surrounding state capture, which illustrate Eskom's deterioration on both financial and governance levels. These events will be thematically summarised below.

C. STEPS TAKEN BY OUTA

6. In recent months, South Africa has been rocked by the Gupta emails and documents (“#GuptaLeaks”) which were ostensibly retrieved from the server of Sahara Computers Pty (Ltd) (Sahara). These #GuptaLeaks have substantiated most of the allegations pertaining to state capture and have unveiled evidence of misconduct by members of the Gupta family, many high-ranking government officials and private individuals.

7. Upon further investigation into the documentation that transpired from the #GuptaLeaks, OUTA laid a series of criminal complaints and complaints with the relevant regulatory bodies of individuals affiliated with Eskom. Below follows a brief summary on each charge laid by OUTA, relating to Eskom.

8.1. BRIAN MOLEFE

- On or about 2 August 2017, OUTA laid criminal charges against Brian Molefe at the Randburg Police Station, under Criminal Administration System (CAS)

number 34/8/2017. A copy of the affidavit is attached hereto and marked “**ANNEXURE OUTA1**”.

- The charges include contraventions of the Public Finance Management Act, 1999 (PFMA), the Companies Act, 2008 and fraud.
- Molefe, in his capacity as Eskom’s Chief Executive (CE), misrepresented to the Eskom Pension and Provident Fund (EPPF) that he was entitled to approximately R30 million in pension pay-outs.
- Upon such misrepresentation(s), Molefe received a substantial amount, based on his misleading interpretation of the EPPF Rules.
- OUTA has yet to receive feedback from the South African Police Service (SAPS), save for the fact that an investigation is underway.

8.2. **ANOJ SINGH**

- On or about 28 August 2017, OUTA laid criminal charges against Anoj Singh at the Randburg Police Station. The matter has since been transferred to the Sandton Police Station and registered under CAS number 942/8/2017. A copy of the affidavit is attached hereto and marked “**ANNEXURE OUTA2**”.
- The charges against Singh include fraud and corruption.

- Singh, in his capacity as Eskom's Chief Financial Officer at the time, facilitated irregular payment to Trillian Management Consulting (Pty) Ltd (TMC).
- TMC submitted an invoice to Singh requesting payment in the amount of R 30 666 222.00, upon which Singh authorised payment.
- It was established by Geoff Budlender, SC, in his report on "Allegations with regard to the Trillian Group of Companies, and related matters" dated 29 June 2017 that TMC had no contractual relationship with Eskom. Singh thus approved irregular expenditure and exposed Eskom to severe financial risk.
- OUTA has yet to receive feedback from the SAPS, save for the fact that an investigation is underway.

8.3. **MARK PAMENSKY**

- On or about 14 August 2017, OUTA laid criminal charges against Mark Pamensky at the Brooklyn Police Station. The matter was registered under CAS number 330/8/2017. A copy of the affidavit is attached hereto and marked "**ANNEXURE OUTA3**".
- The charges against Pamensky include fraud and corruption.
- While serving as a non-executive director on the Eskom board, Pamensky also served on the boards

of Gupta entities Shiva Uranium (Pty) Ltd and Oakbay Resources and Energy (Pty) Ltd.

- Pamensky used his position at Eskom to influence corporate decisions at Eskom board level, to the benefit of the Gupta companies on which he served concurrently.
- OUTA has yet to receive feedback from the SAPS, save for the fact that an investigation is underway.

8.4. **BEN NGUBANE**

On or about 13 June 2017, OUTA laid criminal charges against Ben Ngubane at the Olifantsfontein Police Station. The matter has since been transferred to the National Head Office and registered under CAS number 159/6/2017. A copy of the affidavit is attached hereto and marked "**ANNEXURE OUTA4**".

- The charges against Ngubane include fraud and corruption, relating to allegations that he and his wife borrowed R50 million from the Ithala Development Finance Corporation Ltd, used it to buy mineral rights and failed to repay it.
- On 2 August 2017, OUTA laid further criminal charges against Ngubane, in the same case against Molefe, in connection with Molefe's pension payout. This is CAS number 34/8/2017 at Randburg police station and a copy of the affidavit is attached hereto and marked "**ANNEXURE OUTA1**".

8.5. MATSHELA KOKO

- On or about 4 October 2017, OUTA laid criminal charges against Matshela Koko at the Randburg Police Station. The matter was registered under Sandton CAS number 187/10/2017. A copy of the affidavit is attached hereto and marked “**ANNEXURE OUTA5**”.
- The charges against Koko include fraud and corruption.
- While serving as Eskom’s Group Executive: Technology and Commercial (GE: T&C), Koko used his position to help facilitate the Tegeta Exploration and Resources (Pty) Ltd (Tegeta) acquisition of Optimum Coal Holdings (Pty) Ltd (OCH).
- Koko was responsible for the engineering of Eskom’s so-called coal supply emergency and helped secure lucrative contracts for Tegeta.
- OUTA has yet to receive feedback from the SAPS, save for the fact that an investigation is underway.

D. THE ROAD TO RUIN**9. 2000 – PREFERENTIAL PROCUREMENT POLICY FRAMEWORK ACT, 2000**

- 9.1. On 3 February 2000, the Preferential Procurement Policy Framework Act (PPPFA) came into effect, aiming to give

effect to section 217(3) of the Constitution of the Republic of South Africa, providing for, inter alia, a framework for the implementation of the procurement policy contemplated in section 217(2).

9.2. Eskom is subject to the provisions of the PPPFA, as it qualifies as an organ of state as contemplated in section 239 of the Constitution. Section 2 of the PPPFA highlights the framework that ought to be implemented when an organ of state determines its preferential procurement policy.

9.3. The Minister of Finance may, in terms of section 3, exempt any organ of state from any or all provision of the PPPFA. Eskom was exempted from certain regulations under the Act from 7 December 2011 to 7 December 2012.¹

10. 2001 – ESKOM CONVERSION ACT

10.1. On 3 August 2001, the Eskom Conversion Act, 2001 was promulgated. This Act provided for the conversion of Eskom into a public company having a share capital incorporated in

¹ See General Notice R1027 in Government Gazette 34832 of 7 December 2011.

terms of the Companies Act, 1976.² The act came into effect on 1 July 2002.

- 10.2. The conversion entailed that Eskom be subjected to the provisions of the old Companies Act. Section 6 of the old Companies Act provided for the registration of a memorandum and articles of association as determined by the Minister at the time.
- 10.3. The main objective for Eskom's conversion from a statutory body to a state-owned company (SOC), was to afford it an opportunity to review its existing governance structures at the time, which would have allowed for a more effective decision-making process.
- 10.4. As part of the process, Eskom established various board committees in addition to an Executive Management Committee (Exco) to streamline decision making. It should be noted that Eskom's conversion did not have an impact on its obligations in terms of the PPPFA.

11. 2001 – MAJUBA POWER STATION

² This act was repealed by section 224(1) of the Companies Act 71 of 2008. Eskom is currently subject to the Companies Act 71 of 2008.

- 11.1. Eskom started construction of its Majuba Power Station in 1983, with a generation capacity of approximately 4110 MW. This was one of South Africa's most innovative construction operations in the energy sector as it was part of Eskom's so-called "six-pack" fleet. Majuba's final generation unit was operative in April 2001.
- 11.2. Prior to 2001, Majuba received its coal from a dedicated colliery. This colliery became economically "unminable" due to irregularities in the coal seam caused by frequent dolerite inclusions into the seam and other geological problems.
- 11.3. Presently, Majuba receives its coal from the Mpumalanga coal field (various suppliers). This coal is hauled on road and rail which increases operational costs and underutilisation of Majuba's surrounding coalfields. Eskom did, however, engage with Canadian-based Ergo Exergy Incorporated (Exergy) to introduce an underground coal gasification (UCG) project. Eskom launched a pilot project in 2002 generating some 6 MW near Majuba – enough co-fire a single burner at the power station.
- 11.4. A feasibility study yielded positive results, though the UCG technology was ultimately abandoned, allegedly due to disagreements between Eskom and Exergy relating to intellectual property.

11.5. Eskom opted to continue with coal procurement from various coal suppliers, overstressing its governance and compliance capabilities.

12. 2005 – CONTRACTS WITH MCKINSEY AND OTHER CONSULTANTS

12.1. It needs to be noted that McKinsey, Accenture and others have dominated the Eskom consulting scene virtually non stop since at least 2005, with various “turnaround” assignments, helping previous chairs establish new BEE groupings to become dominant suppliers to Eskom, manage coal supplies and various other tasks that should ordinarily be accomplished by Eskom staffers, who seemingly did not have the capacity to execute duties they were appointed (and highly rewarded) to do.

12.2. This even extended to “clerical staff” who were being billed to Eskom at around \$400/hr plus living expenses.

12.3. Other “perpetual appointments” included major legal firms and auditors who conduct on average more than 100 “forensic reviews” per year on Eskom as divisions spy on each other. This has been ongoing since 2005. Most of the “forensic reviews” are conducted for divisions and the results are hidden from Eskom Corporate. It may be informative to

obtain copies of these reviews; such copies should be with Eskom or the suppliers themselves the top five law firms and the top five audit firms. Specialist energy firms were also contracted on a semi-continuous basis, hence they were not independent. Reviews were often biased and limited.

- 12.4. Once of these reviews revealed that an organised syndicate of about 54 people was involved in coal scams amounting to billions of rand, circa 2007. This involved invoicing for fictitious coal transport at fictitious qualities.
- 12.5. At the time, Eskom was not geared to receive dozens of coal deliveries by truck daily and no proof-of-delivery systems were in place or systems to check coal quality of each truckload.
- 12.6. In many instances, deliveries were not offloaded. Instead, the Eskom official was merely paid a small amount to record the arrival of the delivery, and the truck then went to rejoin the queue to record a further delivery within minutes.
- 12.7. Of even more concern was that some of these “perpetual” consultants (including most of the big law and accounting firms) accepted these “limited review” assignments which were designed to clear Eskom officials of wrongdoing or “rubberstamp” activities as legally compliant.

12.8. This is identical to the KPMG action at SARS, in the now discredited report on the “rogue” unit. We urge Parliament to amend PFMA to stamp out this behaviour.

13. 2006 – MISMANAGEMENT OF COAL SUPPLY AGREEMENTS

13.1. In early 2006, Deloitte & Touche conducted a forensic investigation into irregularities at coal analysis laboratories. These laboratories were used by Eskom’s coal suppliers to conduct quality verification on coal that was to be supplied to Eskom in terms of the various coal supply agreements (CSAs). The investigation identified a series of fraudulent conduct over a particular period and recommended that Eskom take the appropriate action against suppliers that had manipulated coal quality test results.

13.2. In a letter dated 31 July 2006 to Rob Lines, Eskom’s GM Generation Primary Energy, it is stated Eskom had not addressed the irregularities timeously. Eskom’s failure to properly verify the coal samples (of the coal which was due to it) and deal with the fraudulent conduct, removed mitigation of damage that would ensue from receiving (and burning) such coal.

- 13.3. It is alleged in the Deloitte report that Eskom's coal suppliers forged and/or manipulated their coal quality results, misrepresenting that the coal supplied conformed to Eskom's specifications. Such specifications are agreed upon contractually.
- 13.4. As a result of Eskom's inability to mitigate further damage, the following claims allegedly arose from Eskom against the suppliers, based on under-delivery from suppliers:³
- Ingwe, approximately R80 million;
 - Liketh, approximately R22 million;
 - Kumba, approximately R663 686,22; and
 - Xstrata Zingisa (Witcons), approximately R162 885,40.
- 13.5. Had Eskom taken reasonable steps to assure conformity to the expected coal quality and complied with the relevant provisions of the PFMA, the claims would not have escalated to the above-mentioned amounts and the need for an investigation would have been eliminated.
- 13.6. It should be noted that Eskom (as with any claimant at common law) cannot claim damages from suppliers for problems that can be attributed to its own failure to mitigate

³ These figures are detailed by the Deloitte Report and are based on the difference in price surrounding the quality of coal delivered – not the quantity.

damages. Eskom's acceptance of sub-standard coal in itself equals financial loss – it received a lesser product while paying a premium price.

13.7. Eskom's acceptance of a lesser product is not in the best interest of the entity. Moreover, the actual consumption of the coal exposes the power station (in which it is burnt) to severe maintenance issues. Coal from a single source cannot be universally burnt at all Eskom's power stations.

13.8. Many of Eskom's power stations, such as the Hendrina power station, are tailor-made to burn the specific coal in its proximity. Simply put, there is a direct correlation between a power station's coal-burn specifications and the quality of coal of the surrounding coal reserve.

14. 2008 – LOAD SHEDDING (ALPHA)

14.1. In January 2008, Eskom implemented load shedding. This strategy resulted in widespread electricity outages across the country. The repercussions of load shedding included substantial financial loss including to businesses, industry and the public service.

14.2. On or about 12 May 2008, the National Energy Regulator of South Africa (NERSA) published a report entitled: "Inquiry

into the National Electricity Supply Shortage and Load Shedding”. NERSA aimed to establish the reason for Eskom’s recourse to load shedding.

14.3. The report drew the following conclusions relating to the cause of load shedding, which include:⁴

- Eskom had failed to anticipate future growth rates and did not return mothballed generation plants to service;
- Eskom failed to implement a co-generation programme in anticipation of an increased consumption rate;
- Eskom failed to adhere to its maintenance strategy, which resulted in plant availability below 90%;
- Eskom failed to address unplanned maintenance adequately, resulting in reduced generation capacity;
- Eskom failed to maintain sufficient coal stockpiles that fell within its coal-fired power plants’ specifications, resulting in the use of lower grade coal which contributed to plant outages;
- Eskom failed to implement a proper coal procurement system, resulting in coal insecurity;
- Eskom failed to inform NERSA of its coal stockpile deterioration;

⁴ Ad paragraph 14 of the report, at page 38.

- Eskom exported large quantities of electricity to neighbouring countries that exceeded its contractual obligations.

14.4. NERSA recommended, *inter alia*, that further investigation be conducted into Eskom' coal procurement. Such a report has never been published.

15. 2008 – RENEGADE PROCUREMENT – MEDIUM-TERM COAL PROCUREMENT MANDATE

15.1. During the course of August 2008, Eskom's Primary Energy Division submitted a request to the Exco for the extension of the medium-term coal procurement mandate (MTCM). This proposal envisioned the inclusion of medium-term coal supply agreements (CSAs), as Eskom had allegedly experienced under-delivery from its long-term suppliers.

15.2. The primary reason for procurement under such a dispensation was to secure coal supply for generation purposes. Efficient supply from long-term CSAs would only emerge at later state in the life of the agreement. The Primary Energy Division further motivated, according to the Dentons Report of 2015, that short-term CSAs "*are not long*

enough to abate the effects of an emergency situation...”.⁵

This necessitated the procurement of medium-term CSAs.

- 15.3. The MTCM was extended in 2010 to include so-called life-of-mine CSAs. On 14 April 2014, Eskom’s Primary Energy Division approached and updated the Eskom Board’s Tender Committee and motivated for the MTCM to be kept “open” and for the Divisional Executive to be granted the authority and powers of delegation to give effect to this.
- 15.4. The Board Tender Committee resolution reflects only that *“feedback on the results of negotiations and Coal Supply Agreements is noted”* as per the PricewaterhouseCoopers (PWC) report.
- 15.5. The Primary Energy Division misinterpreted this statement as a further extension of the MTCM, resulting in the mistaken assumption that Eskom’s Procurement and SCM procedures could be ignored. The PWC report noted that *“Management interpreted the Board minutes which read ‘noted’ as providing approval as requested”*.
- 15.6. This would appear to give rise to unauthorised, unlawful and unconstitutional procurement practices that contravene numerous provisions of the Promotion of

⁵ Ad paragraph 3.3.5 (d) of the Dentons Report, at page 182.

Administrative Justice Act 3, 2000 (PAJA) as well as section 217 of the Constitution. Any purported approval would thus appear to be *ultra vires* the applicable procurement regime (32-1033 and 32-1034).

15.7. OUTA was unable to obtain a copy of Eskom's 2008 MTCM. However, it appears from the Dentons Report, the mandate provided that Eskom:⁶

- only negotiate delivered price contracts;
- elect to make use of rail transportation as first choice for coal haulage/transport (subject to rail availability);
- assume in terms of the mandate that road transport be used due to unavailability of rail transport at the time;
- include an average of R85 per tonne in the transporting cost calculation as detailed quantifying factors (i.e. distance between supplier's source and power station) had not been determined;
- will review all CSAs procured in terms of the mandate within GPE and its corporate legal department;
- would only accept coal that conforms to the specific power station's quality specifications for which the CSA had been procured;
- would present any changes to the transport mandate to the Board Tender Committee;

⁶ Ibid.

- will under no circumstances contract with a trader of coal – only with owners of a source or where there is a joint venture between the parties (suppliers).

15.8. According to the Dentons report alone, a substantial amount of CSAs were awarded in terms of the MTCM. The significance of this is that Eskom had policies in place at the time of the awarding of the CSAs, which addressed procurement procedures to be followed. Notwithstanding such framework, it would seem that Eskom applied the MTCM where it deemed fit, whether negligently or intentionally.

15.9. It should be pointed out that, firstly, the mere approval for the extension of the MTCM is in itself unlawful and aims to circumvent Eskom's procurement procedures applicable at the time. Secondly, the question is raised as to the validity of the CSAs awarded in terms of the MTCM, even it was found to be extended lawfully.

15.10. OUTA wishes to emphasise its concerns regarding the concurrence of two distinct procurement regimes, which completely undermines the principle of transparency as enshrined in section 217 of the Constitution. This appears to be ongoing, is a key factor in corruption and we urge the committee to put a stop to this.

16. 2010 – DETERIORATION OF MAINTENANCE AT ESKOM'S POWER PLANTS

- 17.1. As a consequence of the anticipated 500 000 visitors to the Soccer World Cup tournament in 2010, Eskom resolved to “keep the lights on at all costs”.
- 17.2. Plans included cutting all maintenance projects so as to not take plant offline for maintenance, and keeping it available for the anticipated increase in demand.
- 17.3. Whilst Eskom could easily cope with increased average demand, it envisaged problems with additional 500 000 people chasing up peak demand, especially in the afternoon.
- 17.4. Eskom thus resolved to stall all maintenance until further notice.
- 17.5. The surplus cash from non maintenance appears to have evaporated as Eskom did not show it in its financial reports.
- 17.6. A full forensic review needs to identify where this amount of around R10 billion per year flowed to.

17. 2011 – FIRST DUHVA BOILER MELTDOWN (UNIT 4)

- 18.1. Eskom's Duvha power station, near Emalahleni, has potential generation capacity of approximately 3600 MW. However, only 2400 MW is available due to a series of events that lead to the destruction of two of its generation units.
- 18.2. During the course of February 2011 Eskom conducted a turbine overspeed test. The turbine spun excessively which resulted in severe damage to Duvha's unit 4 turbine. This meant that Eskom lost 600 MW of its generation capacity, due to what it called an "operating error".

18. 2014 – SECOND DUVHA BOILER MELTDOWN (UNIT 3)

- 19.1. On 30 March 2014, Duvha's unit 3 boiler exploded due to apparent over-pressurisation. This put Eskom at a further generation deficit of 575 MW in 2014. Eskom noted in a media statement, dated 31 March 2014, attached hereto and marked "**ANNEXURE OUTA6**", that they did not foresee immediate load shedding.
- 19.2. It is alleged that the coal fed into unit 3 prior to the incident, did not conform to the power station's specifications. This coal did not originate from the source for which Eskom had originally contracted. The coal had been hauled on a road

transport network, as the conveyer system had deteriorated in December 2013.

- 19.3. It should be noted that the haulage of coal entailed sourcing from various suppliers, creating a mixed product detrimental to the power station.
- 19.4. The consumption of “out-of-specification” coal exposes Eskom’s power stations to potential risk, which is in contravention of the PFMA.
- 19.5. It is reasonable to conclude that the destruction of Duvha’s unit 3 could have been averted, had Eskom taken appropriate steps to repair the deficient conveyer system. OUTA reiterates that Duvha’s unit 3 incident can be attributed to Eskom’s failure to assure that it received the correct specification coal from its suppliers.
- 19.6. As Eskom received low-quality coal for Duvha, no reasonable steps were taken to avoid further damage (i.e. use such coal for a different power station). Eskom nevertheless proceeded to burn the incorrect quality coal, while knowingly or reasonably ought to have known that such coal would damage the turbine.

- 19.7. Not only did Eskom's negligence cause damage to a state asset, but it also affected the economy as electricity generation for the power station plummeted by 600 MW.

19. 2016 – PROCUREMENT FOR DUVHA UNIT 3 BOILER

- 20.1. Following the disaster that ensued at Duvha power station, Eskom issued the first tender for the replacement of the unit 3 boiler in December 2015.
- 20.2. Eskom was forced to sign a settlement agreement with its insurers in February 2016. The parties agreed that Eskom be fined a penalty of approximately R1.7 billion if it did not procure the replacement of unit 3 before 31 March 2017.
- 20.3. On or about 22 June 2016, Eskom stated that it would proceed conclude an agreement on a FEDIC basis upon awarding of the tender.⁷ Moreover, all costing relating to the agreement will also be based on FEDIC. It is further stated that Eskom's contracting strategy seeks to "contract on a turn-key basis where potential suppliers assume all construction and interface management risks".
- 20.4. Shortly after the tender had been advertised, Eskom cancelled the negotiation that followed, allegedly due to

⁷ Eskom media statement, *An update on the replacement of Unit 3 of the Duvha power station*, 22 June 2016 – "ANNEXURE OUTA7".

noncompliance with the conditions precedent by the bidders that applied for the tender.⁸ On or about 18 August 2016, Eskom issued a new request for proposals. Eskom had received a response from six bidders.

- 20.5. In line with its contracting strategy, Eskom identified two potential suppliers amongst the bidders – General Electric (GE), and Murray and Roberts Holdings Ltd (M&R). These bidders quoted R2.77 billion and R2.85 billion respectively. A Chinese bidder, Dongfang, quoted a staggering R6 billion for the bid.
- 20.6. On or about 23 December 2016, Eskom’s Group Capital Division (GCD) recommended that the negotiations be limited to GE and M&R. However, Eskom indicated that these bidders (among four) had material deviations in their bids, thus a fair price comparison would be impossible.
- 20.7. Dongfang revised its price and brought it down to approximately R5.2 billion – still beyond the price offered by GE and M&R. A report to the tender committee also shows that Dongfang scored far lower than the other three bidders in the safety, health and environment category because it failed to submit key documents. When it came

⁸ Eskom media statement, *Eskom to restart process for a contract to rebuild Duvha 3 boiler*, 30 June 2016 – “ANNEXURE OUTA8”.

to local content, Dongfang fell short of the mandatory minimum requirement too.⁹

- 20.8. In order to facilitate negotiations with Dongfang, Eskom became adamant to identify irregularities with the bids of GE and M&R. On 18 January 2017, Eskom's acting commercial GM signed a submission requesting the board to allow for negotiations with four bidders, as opposed to only two. The submission was approved. It should be noted that, by this time, Eskom had shortlisted GE and M&R.
- 20.9. By 3 March 2017, Dongfang (now part of the negotiations) further reduced its price to approximately R4 billion. Notwithstanding the fact that Eskom had already vetted the bidders in November 2016, which is ostensibly the gatekeeping phase, further issues with GE and M&R were identified.
- 20.10. It should be noted that the narrowing down of potential suppliers, ought to entail adjudication based on pricing differences, as pre-qualification processes had already commenced. Affirmative pre-qualifications were the reason behind funnelling the bidders down to four (initially two).

⁹ BusinessDay, 'How Dongfang won R4bn 'cooked' Eskom tender', 26 June 2017.

- 20.11. On or about 8 March 2017, the Board tender committee received a submission that the contract be awarded to Dongfang, citing M&R's reputation and fraud on the side of GE as contributing factors. This disqualification was done retrospectively after negotiations had started. KPMG noted that such considerations should have been dealt with in the evaluation phase (November 2016).
- 20.12. The awarding of the contract to Dongfang entails a loss of approximately R800 million to Eskom, as the contract should have been awarded for a mere R3 billion.
- 20.13. OUTA reiterates that Eskom's conduct falls short of the procurement principles and that the awarding of such contract is not in Eskom's best interest as the national power utility. It should be noted in this regard, that Eskom's awarding of the contract to Dongfang amount to irregular expenditure. However, when Eskom apply for an increase in its electricity tariffs with NERSA, it cites its financial difficulties as justification for an increase, where in actual fact such difficulties are self-inflicted.

20. **2014 – LOAD SHEDDING (BRAVO)**

- 21.1. It was inevitable that the lack of maintenance since the Soccer World Cup in 2010 would catch up with Eskom.

Together with the expiry of the second medium-term coal mandate, and the positioning of hungry diesel suppliers, Eskom was set up for more pillaging.

- 21.2. With hindsight, it becomes clear that this crisis was also fabricated to open up coal supply agreements for Gupta suppliers and also to build momentum for the nuclear bid.

21. 2014 – ESKOM PROCUREMENT AND SUPPLY MANAGEMENT PROCEDURE (“32-1034 PROCEDURE”)

- 22.1. The 32-1034 Procedure sets out the various procedures to be followed relating to procurement and supply chain operations within Eskom and its Group: Technology and Commercial division. It further intends to achieve accuracy and consistency in decision making, customer satisfaction and the fulfilment of the Eskom’s overall strategic objectives.
- 22.2. Moreover, the 32-1034 Procedure aims to give effect to the Eskom’s Supply Chain Management Policy, which in turn gives effect to section 217 of the Constitution.
- 22.3. The primary purpose of this procedure is to ensure application of the Approved Procurement Framework results that is commercially, financially, and technically sound and which in addition, does not contravene the

constitutional principles of fairness, equitability, transparency, competitiveness and cost effectiveness.

- 22.4. Deviation from the provisions of the 32-1034 Procedure may only be implemented upon approval by the Executive Committee Procurement Subcommittees or a higher delegated authority – not disregarding constitutional principles.
- 22.5. The 32-1034 Procedure applies uniformly throughout Eskom, its various divisions, subsidiaries and entities in which it has a controlling interest as contemplated in clause 2.1.2 of the 32-1034 Procedure.
- 22.6. The current 32-1034 Procedure was approved on 19 May 2014 by Eskom's then Acting Group Executive: Technology and Commercial (GE: T&C), Matshela Koko. Review of the procedure was set for April 2017, although OUTA is unaware of whether such review had occurred.
- 22.7. In addition to the application of the 32-1034 Procedure, any procedures duly followed, remain subject to the 32-1033 Policy, the Constitution, the PPPFA, the PFMA and a series of relevant normative and informative frameworks as contemplated in clause 2.2 of the 32-1034 Procedure.

- 22.8. Section 3.4.2 of the 32-1034 Procedure warrants the execution of limited or unsolicited tendering. This procedure involves limiting the number of participating tenderers within large market participation, which entails that public advertising would not be required.
- 22.9. Subject to strategy approval, the procurement practitioner, assisted by an end-user/cross-functioning team and the relevant Supplier Development and Localisation (SD&L), functionary must confirm a list of at least three (emphasis added) capable and independent suppliers, preferably more, who will be invited to participate.
- 22.10. Furthermore, these suppliers would then have to be invited to participate in the tender, subject to the outcome of the relevant Requests for Information (RFI), EOI, pre-qualification enquiry, and / or the supplier's existing profile on the Eskom Supplier Database, provided that selection of the closed list can be justified against the constitutional principles of fairness, equitability, transparency, competitiveness and cost-effectiveness.
- 22.11. A closed tendering process may only be applied if:
- There is an approved strategy authorising sourcing via closed/limited tender, and authorising the suppliers selected for participation;

- It has been established through market research that there are only a few known suppliers that are capable and available to provide the assets, goods or services, due to the specialised field they operate in; and
- The market is too large and suppliers may be pre-qualified against specific criteria before participation in a closed tender process, in order to avoid a lengthy and costly evaluation process.

22.12. Notwithstanding the option to facilitate unsolicited tendering, Eskom, however, is not obliged to consider such process. In terms of section 3.4.5.8 of the Eskom's SD&L, only two types of unsolicited tenders may be received:

- firstly, where an offer is made by a supplier when there is no procurement process in place for the particular service required;
- secondly, where an uninvited supplier submits an offer during a closed/limited tender process.

22.13. Where no procurement process is in place, any employee from Eskom must refer the supplier that submitted the offer to the SD&L Department within Group Technology and Commercial. Upon referral, the supplier may then be given a vendor number confirming registration on Eskom's

Supplier Database and may be considered for any future tenders.

- 22.14. The Procurement Practitioner should then refer the matter to the relevant general manager for Commercial, for decision-making. A management decision, documented for audit purposes, should then be taken as to whether to allow the unsolicited offer if it is made before the official closing time for submissions, or before conclusion of closed mandated negotiations.
- 22.15. An unsolicited offer may be allowed if it will not in any way compromise the fairness, transparency, equitability, cost-effectiveness and competitiveness of the process. If any of the aforementioned principles will be compromised, an unsolicited offer should not be allowed (emphasis added).
- 22.16. If permission is granted to the supplier to submit a tender/offer, then the same rules regarding the issuing, receipting and deadline of tender submissions will apply. If there is a possibility that pricing information may have been shared, or there are suspicions of collusion, then an unsolicited offer should not be allowed.

22.17. Should the relevant general manager decide to consider an unsolicited tender, the following must be taken into account:

- The assets, goods or services offered in terms of the unsolicited tender/offer is a unique innovative concept that is proven to be exceptionally beneficial to, or proven to have exceptional cost advantages for Eskom; and/or
- The supplier making the offer is the sole provider of the assets, goods or services in the circumstances; and/or
- The need for the assets, goods or services by Eskom has been approved during its strategic planning, budgeting and/or investment processes.

22. EMERGENCY PROCUREMENT IN TERMS OF THE 32-1034 PROCEDURE

23.1. Section 3.5.2 of the 32-1034 Procedure states that “emergency procurement” should be differentiated from an “urgent” requirement not necessarily foreseeable or immediate as opposed to an immediate and unforeseeable requirement.

23.2. Where urgent requirements could be foreseen, the tendering process must still be conducted through a Purchase Requisition (PR) in the Systems Application

Processes (SAP) system, using “normal” procurement and sourcing mechanisms.

23.3. A situation is regarded as an emergency, when it may imminently give rise to the following, with little to no means of alleviation through any other means, unless the relevant assets, goods and services are procured:

- threats to human life or safety;
- threats to interruptions in the supply of electricity to customers or load loss;
- threats of substantial ecological damage;
- the threat of major consequential expense to Eskom;
- the threat of serious damage to Eskom’s reputation and good name.

23.4. Should one or more of the above-mentioned situations become imminent, the following procedure must ensue in the stipulated order:

- the end-user must contact the most senior available official of Eskom responsible for the particular site and notify him or her of the situation accordingly;
- the senior official must then decide what action needs to be taken in order to prevent the emergency situation from materialising, and should such official deem procurement as a necessity to circumvent possible materialisation of proliferation, he or she

may then authorise the procurement without any further authorisation from a Delegated Approval Authority;

- the end-user must then contact the applicable supplier to deliver the proposed assets, goods or services;
- the end-user and the official is then required to formally request ratification of the emergency procurement on the relevant Commercial Transaction Approval Form, for approval by a delegated Procurement and Tender Committee;
- upon ratification of the emergency procurement (and once received by the end-user), and only then, can a purchase requisition be created by the end-user and routed to the relevant procurement practitioner to create a purchase order – thereby enabling payment for the invoice;
- condonation must be sought to the extent that the procurement and tender committee determines that the procurement is not warranted by an emergency.

E. RECENT FINDINGS AGAINST ESKOM

23. DENTONS REPORT

- 24.1. On or about 20 April 2015 an investigation commenced by Dentons South Africa, based on a request from Eskom. The terms of reference for this investigation described the exercise as a “Forensic Fact-Finding Enquiry... into the business and challenges experienced by Eskom”.
- 24.2. The Request for Proposal highlighted that the investigation address, *inter alia*:
- The poor performance of Eskom’s power stations;
 - Delays in streamlining Eskom’s new generation programme;
 - High costs relating to primary energy;
 - Eskom’s financial challenges;
 - Integrity of Eskom’s procurement procedures and compliance with relevant legislation and procurement policies;
 - The effectiveness of Eskom’s contract management systems.
- 24.3. Notwithstanding the broad nature of the mandate given to Dentons, Eskom limited the operational aspects of the investigation for reasons unknown. Some of these hindrances include, *inter alia*, that:
- Only certain relevant documentation was to be consulted, with the exclusion of significant evidence;

- Certain documents were only to be consulted on Eskom's premises under the supervision of its onsite security;
- Access to emails was completely denied;
- Interviews with suspended employees was denied.

POWER STATION DECLINE

- 24.4. With regards to the deterioration of Eskom's power stations, as from 2009, Dentons identified the age of Eskom's generation fleet as a contributing factor which resulted in an array of failures. Furthermore, the fact that Eskom failed to address this issue by deferring mandatory maintenance prolonged the negative impacts of this.
- 24.5. The failures experienced by the power stations resulted in severe load losses and prolonged power outages. This in turn meant an increased load on the remainder of the electricity grid, which entailed additional strain to the transmission and generation systems. Such strain was accompanied by additional maintenance requirements as Eskom's generation capabilities were stressed – affecting the infrastructure in the process.
- 24.6. Maintenance on the grid thus became necessary to maintain security of supply. This resulted in escalated cost.

Although most of the mandatory maintenance was deferred, Dentons noted that where maintenance had been performed, it was of poor quality.

- 24.7. Dentons recommended that Eskom's management of outages be reviewed with regards to procurement, planning and ownership. Moreover, it was stressed that maintenance funding be prioritised and ring-fenced in the process.

DELAY IN NEW BUILD PROGRAMME

- 24.8. Eskom's new build programme aimed to eliminate power outages and secure supply of electricity for increasing demand and the decommissioning of some of the older assets in its generation fleet. Dentons noted that Eskom set unrealistic goals for completion of its new build programme in an attempt to avoid supply shortages.
- 24.9. The construction phase for the programme commenced during the course 2007. The projects that formed part of this envisaged programme are Ingula, Medupi and Kusile. The Ingula power station Eskom's second pumped storage scheme, generating electricity through hydro-kinetic energy. Medupi and Kusile, however, are coal-fired power station, with a combined generation potential of 9 600 MW.

- 24.10. It was noted that Eskom possessed insufficient skills to operationalise the new build programme in its initial phases. Dentons also indicated that Eskom had never developed skills regarding its existing coal power station, hindering the migration of its staff to execute the new build programme.
- 24.11. Eskom elected to procure the services required for such a programme on a multi contract basis. This exaggerated Eskom's responsibility to manage and implement the agreements. Given the lack of skills as identified by Dentons, delays in the implementation were inevitable.
- 24.12. No feasibility studies were conducted on the new build programme prior to the construction phases. This entailed that "new" geological issues were identified as construction ensued. In some instances, this delayed construction by approximately 18 months.
- 24.13. It was further identified that Eskom failed to comply with its contract management framework as prescribed by the 1032-34 Procedure. This entailed abuse of modifications to the agreements, specifically that of Medupi. In an independent investigation conducted by OUTA, it was

identified that the Medupi contract (identify work package) alone consisted of various alterations.

- 24.14. Dentons recommended that risks be evaluated prior to embarking on colossal construction projects and that skills be in line with the projects which Eskom proposes to pursue (internally). It is further noted that Eskom's project management system be reviewed and all ambiguity surrounding implementation and non-performance by suppliers be eradicated.

ESCALATION IN PRIMARY ENERGY COST

- 24.15. Dentons noted that Eskom's escalation in primary energy costs can be attributed to costs Eskom pay to obtain the coal for the required power stations. The change in the coal mix used for its power stations is due to Eskom's failure to secure long-term coal contracts with established suppliers, notwithstanding the drop of supply of the latter's resource.
- 24.16. The lapsing of Eskom's long-term CSAs forced it to procure coal from other suppliers on a medium terms basis. Agreements with such suppliers entailed additional costs with regards to transport, which accounts for an average of 35% of the coal price. Dentons notes that some of these suppliers' collieries are located some 280km from the

power station in question, while the long-term suppliers were within the power stations' immediate vicinity.

- 24.17. The decline in coal quality also resulted in larger quantities of inferior coal required to yield the same energy output as high-quality coal. More tonnages are thus required to achieve the same production goal, which will of course entail additional transport costs per tonne of coal.
- 24.18. It is noted that Eskom failed to facilitate competitive tendering for medium term CSAs, presumably in line with Eskom's emergency procurement mandate. As the tendering process utilised for this purpose was unsolicited and uncompetitive, neither the coal prices, nor transport costs were market related. In some extreme instances, the transport cost of coal from a supplier's colliery to an Eskom power station would exceed that of the coal.
- 24.19. Dentons recommended, *inter alia*, that Eskom changes its approach in the procurement of medium terms CSAs and follow a competitive tender process. It is further suggested that Eskom conduct the necessary feasibility studies and consider the possibility to refurbish some of its long-term CSA's.

INTEGRITY OF ESKOM'S PROCUREMENT PROCESSES

- 24.20. During its investigation, Dentons were informed that the vast majority of Eskom's CSAs were concluded in the absence of any tender process. This section of their investigation covered procurement of coal between 2013 and 2015.
- 24.21. Suppliers were registered on Eskom's supplier database without adequate gate keeping mechanism. Dentons had been told that the only registration criteria were that the coal should be able to burn.
- 24.22. Eskom had allegedly made use of the so-called 2008 emergency medium term coal procurement mandate in the awarding of the CSAs during 2013 to 2015. This mandate runs concurrently with that of Eskom's 32-1034 Procedure. Inconsistencies in this application can be attributed to decisions by Primary Energy Division, according to Dentons.
- 24.23. Notwithstanding the absence of tendering processes, Eskom failed to authenticate documentation submitted by the bidders/suppliers. Furthermore, no due diligence had been conducted on suppliers' legislative compliance, in line with Eskom's "Contracting Requirements for Coal, November 2013". It should be noted that the latter

document is a guideline that gives effect to Eskom procurement policies. Nevertheless, this guideline was never strictly complied with – even though it had been implemented by the Primary Energy Division.

24.24. In the awarding of CSAs (without a tendering process), bidders that met the necessary criteria required for the awarding of the contract had not received it, while bidders that were noncompliant were afforded an opportunity to rectify their bids. It is OUTA's contention that Eskom, in particular its Primary Energy Division, sporadically applied procurement policies in pursuit of securing lucrative CSAs with its preferred candidate(s). Dentons could not determine the exact motive for this preferential treatment of bidders, save that such treatment was not consistent with the provisions of PPPFA and relevant National Treasury regulations (i.e. BEE scoring criteria).

24.25. It was also noted by Dentons that the individual contract pricing was not adequately reported. This created an opportunity for abuse, which inevitably occurred.

24.26. Dentons made recommendations with regards to Eskom's flawed application of its procurement processes and policies, which include, *inter alia*, that:

- Eskom should implement a substantive approach to procurement and adequately train its staff in the objectives and underlying principles as aside from a mere “tick box” exercise;
- Eskom should consider shortfall previously experienced in its procurement policies and adapt its policies in order to avoid problems previously encountered;
- The manner in which Eskom utilises different procurement processes should be reviewed as it leaves room for manipulation of the processes;
- Audit findings need to be institutionalised;
- Forensic investigations into allegations of executive interference of procurement must be prioritised;
- Guidelines should be developed to avoid executive interference;
- The practice of withdrawal and immediate resubmission of tenders should be reviewed in order to mitigate abuse;
- Eskom should consider utilising external services to evaluate and adjudicate tenders received;
- An overall compliance enhancement and enforcement mechanism should be formulated;
- Eskom must realign its SCM policy to synchronise with its organisational structure;

- Eskom should review the applicable procurement processes for coal and diesel to ensure scrutiny.

24. PRICEWATERHOUSECOOPERS (“PWC”)

- 25.1. During the course of 2015 Eskom appointed PriceWaterhouseCoopers Advisory Services (Pty) Ltd (PWC) to conduct a review on its coal quality management. PWC’s focus was on irregularities pertaining to suppliers (in particular the collieries) as well as the various laboratories used for quality testing.
- 25.2. As opposed to the Dentons Report, PWC’s mandate was narrowed down to coal quality and procurement. However, PWC did not encounter the same restrictions with regards to access to records.
- 25.3. PWC identified that certain suppliers were procured on an unsolicited basis with no formal tender initiation phase followed. Some suppliers were, however, procured on a Request for Proposal basis. This raises questions on Eskom consistent application of procurement policies and procedures.

- 25.4. With regards to the contracts awarded on an unsolicited basis, PWC identified shortcomings in non-conformance to registrations and prequalification. The inconsistency between such contracts and those that have been awarded previously can be attributed to change of leadership and individual incompetence. Eskom failed to rectify this deficiency. PWC further noted that many interviewees were unfamiliar with the requirements of Eskom's procurement procedures.
- 25.5. Eskom's Primary Energy Division exercised little to no control over the procurement processes, leaving decision making to the team leaders involved in negotiations. It was also found that Eskom's coal stockpile situation (justification for emergency procurement) of 2009 was not prevalent during the time in which the above-mentioned contracts were awarded. Thus, Eskom's so-called 2008 emergency coal procurement mandate was redundant and should never have been applied.
- 25.6. It was also found that Eskom initiated an open tender process for the procurement of laboratory services in October 2013. This process was not managed properly and resulted in suppliers (laboratories) being awarded contracts notwithstanding noncompliance with mandatory requirements.

- 25.7. No proper records were kept for contract management purposes, hindering PWC's investigation in determining the extent of the procured services. PWC identified some 131 non-conformities that had not been addressed and remedied accordingly by Eskom.

- 25.8. The lack of proper contract management entailed potential threats of sampling manipulation, as the laboratories could produce quality results manually without the output being vetted by Eskom officials. Furthermore, PWC indicated that the laboratories did not comply with the prerequisite skills needed to conduct proper sampling analyses.

25. PUBLIC PROTECTOR'S REPORT 6 OF 2016/17 – "STATE OF CAPTURE"

- 26.1. Amidst great controversy, the Public Protector (Advocate Thuli Madonsela) compiled the renowned "State of Capture" report on 14 November 2016. The report relates to alleged improper conduct by the president, various SOEs and state officials linked to the Gupta family.

- 26.2. It would be superfluous to discuss each allegation covered in the "State of Capture" report. However, it is necessary to highlight the most significant findings relating to Eskom and its complete disregard for legitimate procurement practices.

OPTIMUM COAL HOLDINGS (PTY) LTD

- 26.3. It is noted in the report that Eskom paid approximately R659 558 079.00 to Tegeta Exploration and Resources (Pty) Ltd (Tegeta) as a prepayment for the acquisition of Optimum Coal Holdings (Pty) Ltd (OCH). Eskom previously noted that such payments are common practice when investing in security of coal supply.
- 26.4. Eskom had effectively engineered its own coal supply emergency – which resulted in the “need” to procure new coal supply contracts.
- 26.5. In pursuit of this illicit *modus operandi*, Eskom terminated its coal supply agreements with Just Coal (Pty) Ltd and Exxaro for alleged non-performance and economic reasons respectively.
- 26.6. On or about 16 July 2015, OCH was unable to supply Eskom with the correct coal for its Hendrina power station, which resulted in penalties and arbitration processes. Eskom issued a letter of demand for the payment of R2,177 billion. OCH could not meet this demand upon which Eskom issued summons in the Johannesburg High Court.

- 26.7. OCH was then placed under business rescue in terms of the Companies Act, 2008 in August 2015. During this process, Tegeta was identified as a possible buyer, but it required additional funding to conclude the agreement. It was for this reason that Eskom effected the prepayment of R659 million to Tegeta to complete the acquisition.
- 26.8. Upon gaining control over OCH, Tegeta supplied Eskom with additional coal from OCH's colliery – Optimum Coal Mine (Pty) Ltd (OCM). It should be noted in this regard, that Eskom invested in a source of coal that it had previously deemed as unfit for its power station.
- 26.9. OUTA reiterates Eskom's bias towards Tegeta as it waived the penalty claim initiated against OCH in July 2015. This was only waived after Tegeta had acquired OCH – to the total benefit of the former. For a detailed illustration of the events surrounding the acquisition of OCH, see attached hereto OUTA's criminal complaint against Matshela Koko (**"ANNEXURE OUTA5"**).

26. G9 REPORT

- 27.1. During 2017, Eskom's Assurance and Forensic was requested to conduct an investigation into allegations of

regularities pertaining to Eskom's relationship with Trillian Management Consultants (Pty) Ltd (TMC).

- 27.2. Assurance & Forensic's primary scope of work was to investigate allegations of financial and procurement irregularities against certain senior officials. During its investigation, Assurance & Forensic identified a significant number of implicated individuals. See the G9 executive summary for a more detailed illustration on the conduct of those individuals implicated.
- 27.3. Assurance & Forensic noted in its executive summary, that Eskom officials continued to do business with TMC, knowing that the latter had no contractual relationship with Eskom. Following this *mala fide*, Singh, Mabelane and Govender facilitated payment of some R170.72 million to TMC. Such payments constitute irregular expenditure as contemplated in the PFMA.
- 27.4. OUTA understands that Eskom has since initiated disciplinary proceedings against individuals such as Singh, Mabelane and Govender.
- 27.5. Nevertheless, Eskom has failed to indicate whether any action will be taken to recoup the financial losses suffered. OUTA agrees with the recommendations as per the G9

report for action against TMC, however, the implicated individuals should also be held liable for the losses – both civilly and criminally.

- 27.6. The damage inflicted by TMC (with or without complicit Eskom officials) was directed at an SOE. As such, OUTA urges the Minister of Public Enterprises to fulfil her ministerial role over Eskom and implement the necessary sanctions in accordance with the PFMA and Companies Act.

F. ESKOM'S OWN REPORTING

27. QUERIES ARISING FROM ESKOM'S OWN REPORTING

- 28.1. Eskom's public reporting involves publishing annual reports – the Integrated Reports (IRs) – with annual financial statements. While these are lengthy and have detailed narratives, there is an absence of crucial information on big spending; indeed, the long narratives seem to be a way of obscuring the absence of those crucial details. What's missing are clear operating expenditure and capital expenditure, clarity on what was spent in the previous year, clear forward budgets and timelines, approved total budgets for projects and key contractors. The inadequate reporting has allowed confusion over the

capital expansion programme (the new build spending), with spending that seems open-ended and sometimes confused with general capital expenditure. The Eskom reports highlight a number of problems.

28. **RUNAWAY COSTS: EMPLOYEE BENEFIT EXPENSES**

- 29.1. Eskom now has 47 658 employees, with a total “employee benefit expense” of R33.178 billion for 2016/17. After deducting training, temporary and contractor costs, this is an average cost of R684 145 per employee for the year, which seems high. There’s another R2.952 billion for temporary and contract staff but it’s not clear why Eskom would need those extra contractors with 47 658 staff, so this is an area which raises questions about the legitimacy of the spending.

- 29.2. Executive pay is improved with bonuses. While these may be legal, the morality of providing these while the entity is in such trouble should be considered. Some of these bonuses may be legally questionable: the Eskom integrated reports for 2016 and 2017 indicate that Brian Molefe and Anoj Singh received incentive shares on 1 April 2015, which vest in 2018, and on 1 April 2016, which vest in 2019. At the R1.26 a share valuation in the 2017 report and apparently vesting at 50% of their value, Molefe’s

share is worth R13.5 million and Singh's R8 million. But that first tranche of shares was handed out on 1 April 2015, before either was employed or even seconded to Eskom. Molefe was seconded there from Transnet on 20 April 2015 and Singh on 1 August 2015; both were employed by Eskom from 1 October 2015.

- 29.3. The saga of former Eskom CE Brian Molefe's R30 million "pension" pay-off is now well known. What is not so well known is that not only did Eskom fail to lay charges against those involved in this, but Eskom has failed to get this money returned to it. "The Eskom Pension and Provident Fund advised Eskom on 15 June 2017 that the amount of R30 million paid to the fund in relation to Mr Molefe's early retirement agreement will only be refunded to the company pursuant to a court order," said the Annual Financial Statements in the Eskom IR 2017. Eskom's failure to act to recover this money makes it clear that Eskom management and Board condoned this R30 million pay off, despite the illegality.

29. THE CAPITAL EXPANSION PROGRAMME

- 30.1. The capital expansion programme involves expanding Eskom's generation power, with return-to-service builds

(Camden, Grootvlei and Komati), two new open-cycle gas turbines (Gourikwa and Ankerlig), refurbishments, a pumped storage power station (Ingula) and two coal fired base load stations (Medupi and Kusile), plus associated transmission network expansion. This programme appears to be out of control, with Eskom hiding the real cost of the new power stations. Costs and timelines have changed over the years, with no clear delivery details. Power stations are years delayed and billions over “budget”.

- 30.2. In 2005, Eskom said new power stations would cost R93 billion over five years.
- 30.3. In 2007, Gourikwa and Ankerlig were online and Eskom said the full programme would cost R150 billion over five years. Eskom said it would borrow R100 billion and fund the rest from electricity prices.
- 30.4. In 2011, Eskom said it would cost R340 billion and finish by 2018. Eskom had spent R140 billion by then.
- 30.5. In 2014, Eskom’s then interim CE Collin Matjila said: “When the build programme is completed in 2019/20, Eskom will have increased its capacity by 17 384MW¹⁰”.

¹⁰ Chairman’s report, Eskom Integrated Report 2014

- 30.6. In 2017, Eskom's integrated report didn't give details. The national Budget says it will cost R436 billion.
- 30.7. Eskom's total capital expenditure from 2005/6 to 2016/17 is R539.1 billion or R548.6 billion (depending on which version of capital expenditure statistics are used from Eskom's reports), excluding borrowing costs. This is way beyond all admitted budgets for the capital expansion programme. While Eskom may have capital expenditure in addition to that programme, such a substantial amount extra should have been clearly explained and budgeted. Eskom's revenue application currently before the National Energy Regulator (NERSA) says another R125 billion will be spent in 2017/18 and 2018/19, which means a total capex spending of R664.1 billion to R673.6 billion from 2005/6 to 2018/19.
- 30.8. Some of these amounts (eg 2015/16 and 2016/17) appear to include the electrification funds from the Department of Energy but Eskom's reports unclear on this funding. The National Treasury's accounting of Eskom's infrastructure spending for the seven years from 2013/14 to date and projected to 2019/20 totals R203.8 billion and largely matches Eskom's where the years overlap.¹¹ The Treasury notes that its information is sourced from Eskom.

¹¹ Budget Review 2017, Annexure D: Public sector infrastructure update

	Eskom's records	Treasury's records
2005/06	R10.8 bn	
2006/07	R17.5 bn	
2007/08	R24.0 bn	
2008/09	R43.7 bn	
2009/10	R48.7 bn	
2010/11	R47.9 bn	
2011/12	R58.8 bn	
2012/13	R60.1 bn	
2013/14	R57.1 bn	R57.8 bn
2014/15	R53.1 bn ¹²	R54.4 bn
2015/16	R60.328 bn	R57.0 bn
2016/17	R66.578 bn ¹³	R63.1 bn
TOTAL to date	R548.6 bn	
2017/18	R59.009 bn	R67.2 bn
2018/19	R66.367 bn ¹⁴	R71.4 bn
2019/20	No record	R65.1 bn
	R674.0 bn	R747.5 bn

¹² Figures for 2005/06 to 2014/15: "Total capital expenditure – group (excluding capitalised borrowing costs)" in the Ten-year technical statistics in the Eskom Integrated Report 2015

¹³ The first (lower) figures for 2015/16 and 2016/17 listed as "Capital expenditure (excluding capitalised borrowing costs)" for the Eskom group in the Eskom Integrated Report 2017. The second set of higher figures are in the footnotes to the Annual Financial Statements in the same report; these second figures appear to exclude borrowing costs as those are listed separately as R7.919bn for 2015/16 and R19.589bn for 2016/17.

¹⁴ Capital expenditure for 2017/18 and 2018/19 is listed in Eskom's "Revenue Application FY 2018/19", submitted to NERSA on 25 August 2017.

- 30.9. The Treasury records in the table above provide something of a breakdown in spending each year. The spending on Medupi over those seven years is R72.7 billion, on Kusile is R90.2 billion, on Ingula is R13.5 billion. It also includes Matla refurbishment (R2.1 billion), Majuba rail (R4.6 billion), Duvha (R2.0 billion, although Eskom seems confused about insurance payouts on Duvha), transmission and substation projects, and “other” which is “projects to enhance the system at generation, transmission and distribution level including maintenance projects” (R226 billion).
- 30.10. The Treasury records note a key point: Eskom dips into the capital expenditure budget for “maintenance”. This is one of the ways in which Eskom makes it difficult for the public to understand how much the capacity expansion programme actually costs.
- 30.11. The available spending records mean that the Eskom capacity expansion programme started in 2005 with a budget of R93 billion and a timeline of five years. By 2017 this has expanded uncontrollably to 12 years with no end in sight and a “budget” of R436 billion, but still with no clear indication of a deadline for delivery and finality on spending. And that R436 billion “budget” has long ago been

blown, with actual spending over the past 12 years of up to R548.6 billion. By the end of 2018/19, Eskom will have spent at least R674.0 billion over 14 years with no end in sight. Using the Treasury's numbers takes that total to R747.5 billion over 15 years.

30.12. Ingula pumped storage power station is finished. Medupi and Kusile coal-fired power stations are not finished. Three mothballed power stations (Camden, Grootvlei and Komati) were returned to service from 2005 to 2013, but two are already being closed down again. "Units at Grootvlei and Komati Power Stations have been placed in extended cold reserve with a callback time of five days," said the Eskom IR 2017. "We have identified Hendrina, Grootvlei and Komati as the stations with the biggest cash impact and they will be ramped down to zero production and placed in lean preservation to minimise surplus capacity and optimally manage generation costs: Hendrina in 2018/19, Grootvlei in 2019/20 and Komati in 2020/21." This situation points to a lack of planning in the capacity expansion programme.

30.13. The vagueness and flexibility of spending and timelines, the confusion between "capital expansion programme" and "capital expenditure" has allowed Eskom to get away with spending vast amounts of money, without being held to

account. The amounts spent seem way beyond any admitted spending on the expansion programme, giving rise to concerns about what this money was spent on and the possible existence of a “slush fund” within Eskom.

- 30.14. Eskom’s nominal capacity in 2005 when the programme started was 42 011MW. Twelve years later in 2017, it is 44 134MW, an increase of only 5%.

30. BUDGETING POLICY ON BIG INFRASTRUCTURE

- 31.1. The National Treasury produces guidelines for capital projects, for departments and state-owned entities. These guidelines are aimed at projects funded by the public purse, which includes a substantial part of Eskom’s expansion programme.
- 31.2. The earliest such guide available online is the Treasury’s “Budgeting guidelines for infrastructure and capital projects”, dated May 2008.¹⁵ This sets the guidelines for assessment of projects, before they are approved, by the capital budgets committee (CBC), an interdepartmental task team which “evaluates funding requests for individual infrastructure/capital projects and programmes of

¹⁵ “Budgeting guidelines for infrastructure and capital projects”, National Treasury, dated May 2008. Available online at <http://www.treasury.gov.za/publications/guidelines/2008-10/2009%20MTEF%20guidelines%20-Budgeting%20guidelines%20for%20infrastructure%20and%20capital%20projects.pdf>

departments and state-owned entities” and makes recommendations to the Treasury’s Medium Term Expenditure Committee. Projects or programmes estimated to cost more than R300 million a year or a total project cost of R900 million or more are classified as “mega” projects: Eskom’s expansion programme easily fits that definition. “These projects require a detailed feasibility study and receive a rigorous CBC review,” say the guidelines. This includes estimated construction duration in months, estimated project cost and the potential funding sources. Costs should include annual operating costs, loan repayments and associated interest, and maintenance. The intention of such planning includes “to develop and formulate potential projects precisely and concisely”, “to avoid badly planned projects (‘white elephants’)” and “to promote transparency”, say the guidelines.

- 31.3. There is no indication that Eskom complied with those guidelines. While Eskom may claim that it expected to fund the expansion programme through user-pays arrangements (that is, by loading this onto the price of electricity), Eskom has also used substantial funding from national government. “If funding is required for a public entity, demonstrate why this should be funded by taxpayers and not the users,” say the 2008 guidelines.

- 31.4. The Treasury's update of June 2017 of these guidelines¹⁶ is twice as long and emphasises the need for technical assessment, feasibility studies and a procurement plan.
- 31.5. The Treasury is meant to be watching over this programme, but the first indication of this appears only in 2014. The Treasury's Programme Management for Technical Support and Development Finance, which provides support on major infrastructure projects, noted in the 2014 Budget that it is monitoring both the Eskom build programme and the renewable energy independent power producer procurement programme.¹⁷

31. THE SOLAR PROJECT: DUPLICATE FUNDING, CANCELLED PROJECT

- 32.1. In May 2014, Eskom borrowed €75M (worth about R1.2 billion at 2017 rates) for a concentrated solar power (CSP) project but that project has quietly disappeared. "Eskom and the European Investment Bank (EIB) concluded and signed a €75M loan facility for the partial financing of a 100MW CSP plant in Upington on 15 May 2014," the Minister of Public Enterprises told Parliament in a written

¹⁶ "Capital Planning Guidelines", National Treasury, June 2017. Available online at <http://www.treasury.gov.za/publications/guidelines/Capital%20Planning%20Guidelines.pdf>

¹⁷ National Treasury vote in the Estimates of National Expenditure, 2014

reply in September 2014¹⁸. “Commencement of construction and commissioning of the power plant will become evident on conclusion of the procurement process, the current projection is mid 2016 for construction and early 2019 for feeding power to the Grid. Construction of the power plant is expected to commence in June 2016 with a projected 30 months to complete it. It is anticipated that the power plant will feed electricity into the grid during the first half of 2019.”

32.2. Eskom’s IR 2014 notes briefly: “Eskom secured co-financing loan agreements for the proposed concentrated solar thermal station near Upington.” This was followed by bids. “The concentrated solar plant (CSP) project has advanced with the four bids received having been evaluated in January 2015,” said the Eskom IR 2015 briefly. “The concentrated solar power (CSP) project has advanced, with the two bids received being evaluated,” said the Eskom IR 2016, listing a 100MW CSP in Upington as “under construction”. There was no explanation for the change in bids from four to two.

32.3. Eskom’s IR 2017 refers briefly to funding totalling R942 million from the Agence Francaise de Developpement in 2016 and 2017, for Sere wind farm and “concentrated solar

¹⁸ Reply on 19 Sept 2014 in Parliament by Minister of Public Enterprises, RNW1594-141007

power projects”, with no clarity on what funds were for which project. There’s a brief mention of €75M from the European Investment Bank, received in 2017, but no indication of what this was for. This seems to indicate that there was duplicate fundraising for the CSP, from the European Investment Bank and the Agence Francaise de Developpement.

32.4. Then the CSP project was quietly dropped. It’s not clear what happened to the borrowed euros. “The Board provisionally approved discontinuing the Kiwano concentrated solar power (CSP) project. However, the lenders require an equally transformational renewable project that addresses the CSP project’s objectives and the existing funding conditions. We are in the process of exploring alternative options that will satisfy the lenders’ requirements,” notes Eskom’s IR 2017. Under renewables, the report lists “Concentrated solar power: Upington: cancelled”. A footnote records briefly: “The concentrated solar project (100MW) previously shown as under construction has been cancelled.”

32.5. If this project was indeed “under construction” as reported in both 2016 and 2017 integrated reports, who was awarded the contracts and how much has been paid to

them? Why was this project cancelled? Where is this money?

32. DUVHA AND THE INSURANCE

33.1. On 30 March 2014, Duvha power station's unit 3 was destroyed in an over-pressurisation incident. At the loss of this unit was cited by Eskom as one of the reasons for load shedding during 2014. It is understood to be still offline. According to Eskom's IR 2017, contracts have finally been handed out and repairs have started.

33.2. Eskom claimed on insurance for the Duvha repairs but there are questions around exactly when this money was paid to Eskom and what was paid. Eskom's IR 2017 says this: "The over-pressurisation incident in the boiler of Unit 3 at Duvha Power Station on 30 March 2014, taking the 575MW unit out of service, continues to have a material impact on UCLF, contributing 1.24% to the system total. Following the insurance settlement, we have awarded contracts for structural repairs, demolition of the damaged boiler and construction of the new boiler. Demolition is expected to be completed early during the 2018/19 financial year, and the unit is estimated to return to commercial operation by the end of the 2022/23 financial year."

- 33.3. This implies that the insurance had been recently paid out. However, that same report lists, under “Insurance proceeds” under “Other income” in the footnotes to the financial statements, only R812 million to Eskom company for 2016/17 and R1.393 billion for 2015/16. The previous reports list payouts of R2.732 billion to the Eskom group and R5.111 billion to the Eskom company in 2015 (bear in mind that this payout involved Eskom’s wholly owned insurance subsidiary Escap paying Eskom and an external reinsurer paying Escap). Payouts for 2014 were minimal (R384 million). It thus seems far more likely that this payout was in 2015.
- 33.4. The Eskom IR 2015 makes it clear that an insurance payout was made in connection with Duvha during 2015 and that it was a welcome windfall. The claim was “estimated at R4.2 billion, including business interruption costs”, said IR 2015. “Insurance proceeds from the Duvha unit 3 claim contributed R4.2 billion to other income recognised for the year under review. At group level, the amount receivable from the external reinsurer is R2.7 billion, after deducting the insurance deductible of R1.5 billion borne by Escap.” The report referred to that revenue as providing “some relief”. On 31 August 2015, The Star reported on this payout and also that Eskom had included the cost of the Duvha repairs in its revenue application to NERSA on 30 April 2015 (a month

after the reporting period for IR 2015 and thus after the insurance payout was received), aiming to add the repair costs to the price of electricity but failing to mention the insurance payout to NERSA. Eskom flatly denied having received this payment at the time, saying it was still in discussion with insurers. However the payouts listed in the integrated reports were not updated to correct this “error”. The delay to repairs at Duvha thus appears to have been deliberately engineered by Eskom, despite the load shedding problems of 2014. This may have been motivated by further claims for “business interruption costs” as this was part of the initial claim.

33. RUNAWAY COSTS: INDEPENDENT POWER PRODUCERS

34.1. Independent Power Producer (IPP) costs appear uncontrolled. In January 2013, Eskom noted in the MYPD3 application that IPP costs increased from 125c/kWh to 232c/kWh. The Department of Energy has said it wants a ceiling price of 77c/kWh, which is currently under discussion and being opposed by the IPP sector.

34.2. The national Budget 2017 noted that the IPP programme has procured 6 376MW of power with 4001MW under development. “Private-sector investment in the programme amounts to R201.76 billion to date, of which R49.1 billion is

from foreign investors and financiers,” said the Budget Review 2017.

34.3. While this R201.76 billion cost is, in theory, carried by the private sector (that’s what the IPP programme is meant to be about), the state is actually carrying the financial risk. And this is a very big commitment. “Aside from debt, government’s major obligations are guarantees to state-owned companies and independent power producers (IPPs), and provisions to multilateral institutions,” says the National Treasury in the Budget Review 2017.^[1] “A guarantee is a commitment to take responsibility for a loan in the event of default; it enables the beneficiary to access funding that would otherwise be unavailable or to borrow at rates that reflect lower risk premiums.”

34.4. The guarantees provide substantial help to the IPPs who, in return, are apparently charging Eskom such punitive rates for their electricity that the government is now trying to renegotiate those deals. This seems to be an extraordinary failure on the part of Eskom and the Department of Energy, particularly given that Eskom is the only customer and the government holds the valuable access to the guarantees. How is it possible that a situation arose where Eskom pays up to 232c/kWh for power from IPPs? Who signed these

deals? Who is benefiting? Are these IPPs also beneficiaries of state capture?

34.5. The guarantees to the IPPs work in two ways, says the Budget Review 2017. “These liabilities can materialise in two ways. If Eskom runs short of cash and is unable to buy power as stipulated in the power-purchase agreement, government will have to loan the utility money to honour its obligations. If government terminates power-purchase agreements because it is unable to fund Eskom, or there is a change in legislation or policy, government would also be liable. Both outcomes are unlikely,” says the Budget Review. “Government has committed to procure up to R200 billion in renewable energy from IPPs. As at March 2017, exposure to IPPs – which represents the value of signed projects – is expected to amount to R125.8 billion.”

34. RUNAWAY COSTS: WRITING OFF CUSTOMER DEBTS, TWICE

35.1. Eskom routinely lists impaired debt costs, relating to customers who don't pay. The cumulative impaired debt by March 2017 was R8.7 billion for all Eskom electricity debtors, increased by the year's net impairment of R1.7 billion. NERSA keeps watch over this debt, capping the amount allowed in terms of the authorised revenue. However three years ago, Eskom introduced another

method of writing of debt, which features only in the footnotes to the financial statements. This is unrecognised revenue. “The IAS 18 principle of only recognising revenue if it is deemed collectable at the date of sale, as opposed to recognising the revenue and then impairing the customer debt when conditions change, has been applied since 2015. External revenue to the value of R3 196 million was thus not recognised at 31 March 2017.” Eskom has written off a total of R5.265 billion in this way in three years including, during the last year writing off twice as much as through the impaired debt method. This needs investigation, as it’s a method open to abuse – who knows if this is an informal settlement whose bills are waived or if it’s a good friend of the Eskom billing department in Sandton?

35. COUNTING THE CONNECTIONS: IT’S ELECTRIFYING

36.1. Eskom’s says it has electrified more than 5 million low-income households on the Integrated National Electrification Programme grant and its annual reported electrification numbers bear this out. These end up as Eskom direct customers (the municipalities run their own programmes with their share of this grant). Eskom has 5 838 794 total residential customers (IR 2017) which means the low-income homes are 86% of the residential customers. Statistics SA reported in its Community Survey 2016 that 7

342 161 households were getting electricity from Eskom (not from the municipalities, which were a different category) including 6 891 183 on prepaid meters. Stats SA thus found many more customers on Eskom connections than Eskom records. Either these are customers who aren't paying or, more likely, these are multiple households (ie backyard shacks) sharing a single electricity connection (from a low-income household). While this is legal, it's means that those consumers all end up paying higher rates because they rapidly get to the higher usage blocks on inclining block tariffs and that they have to share the indigent free basic electricity subsidy. This is effectively a way that Eskom cheats the poor out of a fair price for electricity, probably because it's too much trouble to fix it. This needs action to address this problem.

36. OPERATIONAL EXPENDITURE: WHERE DOES IT GO?

37.1. The average price of electricity has gone from 16.04c/kWh in 2004/05 (when the capital expansion programme started) to today's 89.13c/kWh and Eskom's request for 106.87c/kWh for 2018/19.

37.2. Eskom's electricity revenue from 2005/06 to 2016/17 totals R1 191.012 billion (R1.191 trillion). The total Eskom group revenue was R1 208.066 billion (R1.208 trillion).

- 37.3. Eskom's operating expenditure is not neatly totalled in its annual reports. However, the categories Eskom appears to include in electricity operating costs are: primary energy (which includes coal, water, liquid fuels, the environmental levy, purchases from Independent Power Producers and international electricity purchases); depreciation and amortisation; employee benefit expenses; and "other" operating expenses (which includes repairs and maintenance as the main cost). Thus the total operating expenditure during that period is calculated as R1 081.503 billion (R1.082 trillion).
- 37.4. The electricity revenue for 2005/06 to 2016/17 thus comfortably covered the electricity operating costs, excluding any capital spending, leaving R109.509 billion to spare.
- 37.5. The depreciation and amortisation cost in the electricity operating costs was for 2005/06 to 2016/17 a total of R113.067 billion.
- 37.6. Eskom does not clearly specify the costs of coal. The coal costs are a controversial matter due to the problems of corruption in the coal contracts. Eskom also does not specify the costs of water used. A rough estimation (the primary

energy cost, less the costs of OCGTs, the environmental levy, IPPs and international purchases) gives the coal costs for 2013/14 to 2016/17 as R44.1 billion (for 122.0 megatons of coal purchased), R52.4 billion (121.7 MT), R47.4 billion (118.7 MT) and R50.4 billion (120.3 MT).

37.7. The primary energy costs in the electricity operating expenses include the cost of running the open-cycle gas turbines (OCGTs), which is mainly diesel. Eskom has frequently raised the problem of the expense of the diesel since these two generators came online in 2008 and 2009. In 2006 the government introduced a 100% refund on the fuel levy and the Road Accident Fund levy on the diesel used in Eskom's generators; this is confirmed in the Budget Review 2006. Eskom has failed to mention the benefit of this refund in any of its public reporting. In April 2016, the fuel levy refund was halved. "The current full exemption provides a perverse incentive to use diesel excessively," said the National Treasury in the Budget Review 2015. Those refunds do indeed seem to have provided a "perverse incentive" to use diesel: the refunds were worth R2.35 per litre in 2011, rising over the years to R3.94 a litre in 2015. During the four years from 2012/13 to 2015/16 (the years of extreme OCGT usage and the 2014 load shedding) Eskom recorded OCGT costs totalling R33.806 billion and 4 184.6 megalitres of diesel used, while SARS recorded diesel levy

refunds for OCGT plants worth R13.213 billion for 4 137.6 megalitres of diesel. This is R13.213 billion in refunds that Eskom failed to mention publicly and is not clearly reflected in its annual reports.

37.8. The environmental levy on electricity is included in Eskom's primary energy costs, in the electricity operating expenses. This levy started in 2009 at 2c/kWh and is now 3.5c/kWh. It is levied on the producer of electricity (ie Eskom) who pays it to SARS. Eskom in turn charges this cost to its customers, initially as a clearly stated levy expense but now bundled into the electricity price. The national Budget (in the statistical tables in the Budget Review 2017) records that R57.221 billion was collected on this levy since it started, while Eskom's integrated reports list this over the years as a total of R55.769 billion. This cost is currently about R8 billion a year, and is included in Eskom's expenses listed in the revenue application currently before NERSA.

37.9. It's not really clear what the point of this levy is. It was initially set up as a punitive measure to discourage consumers from using too much electricity during a time of insufficient generation capacity, but that era now seems to be over with Eskom's current revenue application to NERSA raising the problem of insufficient sales of electricity. It seems nonsensical to punish those who use electricity with both a

levy to push down sales and the threat of higher prices to allow Eskom to recover its wanted revenue from a lower sales base. At the time the levy was introduced, there was mention that it would be used to fund energy efficiency initiatives but this revenue is not ringfenced by the fiscus and there is no indication it is used for anything other than adding to national revenue. It seems pointless for the government to levy punitive costs on Eskom for using coal-fired power stations and at the same time provide bailouts and approve building plans for new coal-fired power stations. The sole purpose of this levy appears to be to use electricity as a way of raising an extra tax on consumers for the benefit of the general revenue fund, which is a questionable practice given the damage the high price of electricity is already doing to the economy.

37.10. Eskom charges VAT on electricity and also on this levy, so consumers are doubly hit by the levy cost. The VAT charges are a problem as they are not specified in the prices set by NERSA. Section 65 of the Value-Added Tax Act requires that final advertised prices include VAT or, if it is excluded, then the vendor must include both the price excluding VAT and the price including VAT.

37.11. Eskom has since 2006/07 received hidden – and apparently forgotten – assistance from the fiscus: it no longer pays

dividends to the shareholder. The last dividends paid were R1.6 billion in 2005/06 and R569 million in 2004/05. It is now so accepted that Eskom doesn't produce dividends that this line item no longer appears in the national Budget (in the Public Enterprises budget). This is effectively an ongoing annual subsidy from the government to Eskom.

37.12. Eskom received R83 billion in bailout funding from the fiscus: R60 billion as a subordinated loan paid over from 2008/09 to 2010/11, followed by the September 2014 decision (finalised in June 2015) to convert this loan to a bailout, add another R23 billion bailout and provide a R350 billion guarantee facility. This R83 billion bailout was legalised in three money bills¹⁹ with the loan legislation gazetted on 28 November 2008 and the bailout pair gazetted on 6 July 2015. All three pieces of legislation stated that the full R83 billion was for "enhanced electricity generation capacity and security of supply". It thus was not for operational expenses, and should not have been needed for that.

37.13. While the R60 billion was a loan (from November 2008 to July 2015), Eskom did not make any repayments on it, apparently as the repayment period had not started.

¹⁹ The Eskom Subordinated Loan Special Appropriation Act (2008/09-2010/11 Financial Years) no 41 of 2008, the Eskom Subordinated Loan Special Appropriation Amendment Act (2008/09-2010/11 Financial Years) no 6 of 2015 and the Eskom Special Appropriation Act no 7 of 2015

37.14. The Eskom Integrated Reports for 2015, 2016 and 2017 list “Subordinated loan from shareholder” under “Finance cost” in the footnotes to the annual financial statements. This cost is listed as R2.228 billion in 2015, R1.208 billion in 2016 and zero in 2017. It is unclear what these costs were for as no payments were made on the “loan”.

G. LEGAL AND REGULATORY FRAMEWORK

37. PUBLIC FINANCE MANAGEMENT ACT, 1999 (PFMA)

38.1. In terms of section 49(2)(a), the Eskom board is the accounting authority. The accounting authority must, in terms of section 50(1):

- *“(a) exercise the duty of utmost care to ensure reasonable protection of the assets and records of the public entity;*
- *“(b) act with fidelity, honesty, integrity and in the best interests of the public entity in managing the financial affairs of the public entity;*
- *“(c) on request, disclose to the executive authority responsible for that public entity or the legislature to which the public entity is accountable, all material facts, including those reasonably discoverable, which*

in any way may influence the decisions or actions of the executive authority or that legislature; and

- *(d) seek, within the sphere of influence of that accounting authority, to prevent any prejudice to the financial interests of the state.”*

- 38.2. In terms of section 50(2)(a) of the PFMA, members of the accounting authority may not act in way that is inconsistent with the provisions of the act.
- 38.3. Section 50(2)(b) states that a member of the accounting authority may not use its position, privileges or confidential information obtained by virtue of being in such position, for personal gain or to the benefit of another person.
- 38.4. In terms of section 50(3)(a), a member of the accounting authority must disclose any direct or indirect personal or business interest that such member may have in any matter before the accounting authority. Section 50(3)(b) states that a member of the accounting authority must withdraw from proceedings in instances where such interests are present.
- 38.5. Section 51(1)(a) states that an accounting authority must maintain effective, efficient and transparent systems of financial and risk management and internal control; a system of internal audit under the control and direction of an

audit committee complying with and operating in accordance with regulations and instructions prescribed in terms of sections 76 and 77; and an appropriate procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective and a system for properly evaluating all major capital projects prior to a final decision on the project.

- 38.6. In terms of section 51(1)(b), an accounting authority must take the appropriate steps to collect all revenue due to the public entity, prevent irregular, fruitless and wasteful expenditure and manage available working capital effectively and economically. Section 51(c) states that an accounting authority must safeguard the public entity against irregular, fruitless and wasteful expenditure.
- 38.7. Section 51(1)(e) states that the accounting authority must take effective and appropriate disciplinary steps against any employee of the public entity who contravenes any provision of the PFMA, undermines the public entity's financial management and internal control and who makes or permits irregular, fruitless and wasteful expenditure.
- 38.8. In terms of section 51(1)(f), the accounting authority must submit all relevant documentation to Parliament or the relevant legislative authority when required to do so in terms

of the PFMA. Section 51(1)(h) states that the accounting authority must comply and ensure compliance with the PFMA and any other applicable legislation.

- 38.9. Should an accounting authority be unable to comply with any responsibilities as set out in the PFMA, it must promptly report its inability to comply together with reasons, to the relevant executive authority and treasury in terms of section 51(2).
- 38.10. In terms of section 83(1), an accounting authority commits an act of financial misconduct when it willingly or negligently fails to comply with section 50 and 51, or where it makes or permits an irregular, fruitless and wasteful expenditure. In terms of section 83(2), every member of the accounting authority is individually and severally liable for the accounting authority's misconduct.
- 38.11. In terms of section 83(4), financial misconduct is grounds for dismissal, suspension or any other sanction, despite any other legislation.
- 38.12. In terms of section 86(2), an accounting authority is guilty of an offense if it failed to comply with section 50, 51 and 55 wilfully or in a grossly negligent way.

38. THE CONSTITUTION OF THE REPUBLIC OF SOUTH AFRICA

39.1. In terms of section 33(1), everyone has the right to just administrative action that is lawful, reasonable and procedurally fair.

39.2. Section 217(1) states that contracts for goods and services procured by an organ of state must do so in accordance with a system that is fair, equitable, transparent, competitive and cost-effective.

H. CONCLUSION

40.1. The Eskom executive management and the Eskom board of directors are responsible for the corporate governance of Eskom but have failed disastrously to block corruption and, in key instances, have encouraged or even participated in it.

40.2. The Minister of Public Enterprises is the shareholders' representative which grants her the appropriate standing to initiate the relevant court action to end such corruption. Her passive behaviour makes her complicit in the proliferation of corruption and mismanagement at Eskom. A series of "further investigations" or "probes" will simply not suffice as an excuse for inaction, as the Minister has more than

enough evidence to liberate Eskom from itself and restore it to its former (efficient) glory.

- 40.3. OUTA urges the Portfolio Committee to act upon the various findings in the numerous investigative reports.
- 40.4. In order to safeguard against future abuse of state funds and, OUTA recommends that the Committee clarify Eskom's applicable legal framework for future procurement. In the light of this, it is recommended that the Committee force Eskom to produce its 2008 Medium-Term Coal Procurement Mandate (MTCM).
- 40.5. From a bigger picture perspective, it is imperative that Eskom's corporate structure be reviewed, especially the composition and structure of the Board.
- 40.6. Previously, Eskom was led by an Electricity Council comprising entities which paid for electricity – these are perhaps the best stakeholders to oversee Eskom's direction and behaviour, and accordingly we plead for the legal structure to be re-instituted.