



Annexure A

NATIONAL FREE BASIC ELECTRICITY (NFBE) RATE METHODOLOGY

Table of Contents

ABBREVIATIONS.....3

DEFINITIONS.....4

EXECUTIVE SUMMARY.....5

1. INTRODUCTION.....6

2. LEGAL BASIS.....7

3. PROPOSED MITIGATION TO CURB OVER FORECASTING.....7-8

4. NFBE RATE MECHANISM.....8

5. INFORMATION TO BE SUBMITTED BY ESKOM.....9

6. APPROVAL OF THE NFBE RATE.....9-10

7. REVIEW AND MODIFICATION.....10

8 . EFFECTIVE DATE.....10

ABBREVIATIONS

FBE	Free Basic Electricity
NFBE	National Free Basic Electricity
EBSST	Electricity Basic Services Support Tariff
DMRE	Department of Mineral Resources and Energy
FBS	Free Basic Services
NERSA	National Energy Regulator of South Africa
IBT	Inclining Block Tariff
CPI	Consumer Price Index
KWh	Kilowatt-hour
ERA	Electricity Regulation Act

DEFINITIONS

Free Basic Electricity:	Limited free amount of electricity supply deemed necessary to support the basic energy services of a typical poor household as determined by Government from time to time. <i>(FBE Policy: 2003.)</i>
Household:	Residential premises with an official point of supply. <i>(FBE Policy: 2003.)</i>
Free electricity:	Electricity supply at no cost. <i>(FBE Policy: 2003.)</i>
NFBE rate:	The NERSA-approved rate at which Eskom is reimbursed by municipalities for providing FBE units to qualifying customers.
Vending Commission:	The rate that vendors charge Eskom to administer the FBE on its behalf.

EXECUTIVE SUMMARY

- a) Municipalities have the constitutional responsibility to provide basic services, and the equitable share allocation enables them to do so. In areas where Eskom is the supplier, the FBE is provided on behalf of the municipality by Eskom. In such areas, the municipality enters into an agreement with Eskom that covers households that are in the Eskom supply areas within the municipal jurisdiction.
- b) The National Energy Regulator of South Africa (NERSA) developed a methodology to determine the National Free Basic Electricity (NFBE) rate. The tool is used annually to determine the NFBE rate that Eskom charges the municipalities for supplying FBE on its behalf. The methodology was approved in May 2011, and reviewed in 2013 and 2017.
- c) The purpose of the review is to enhance FBE regulation. Certain sections of the mechanism have been revised to align objectives and ensure that the process of determining the FBE rate is fair and transparent.
- d) One lesson learned through the previous methodology was that some of the sections were not clear on their intended objectives, particularly on when volume forecasts submitted by Eskom are not met.

1. INTRODUCTION

- 1.1. The National Free Basic Electricity Rate Methodology is developed for the determination of the NFBE rate that Eskom charges the municipalities to supply Free Basic Electricity (FBE) to households in the Eskom supply areas within the municipal boundaries. The Department of Mineral Resources and Energy (DMRE) (the then Department of Energy) introduced the Electricity Basic Services Support Tariff (EBSST) Policy in 2003, which makes provision for 50kWh per month of electricity to indigent households identified by municipalities and connected to the national grid. In support of this policy statement, the National Electricity Regulator of South Africa (NERSA) approved the first NFBE rate on 20 September 2003.
- 1.2. The FBE funding is provided by the National Treasury to local authorities through equitable share allocation as identified by the Department of Cooperative Governance and Traditional Affairs (CoGTA). The Local Government Equitable Share refers to the funds that flow from the National Government and are equitably distributed to local authorities to supplement their internally generated revenues and provide basic services to poor households. In areas where Eskom is the supplier, Eskom provides the FBE on behalf of the municipality. In such areas, the municipality enters into an agreement with Eskom. Each month, Eskom bills the municipality for the FBE allocations that it provided to approved customers. The NFBE rate is the NERSA-approved rate at which Eskom is reimbursed by municipalities for providing FBE units to qualifying customers on their behalf.
- 1.3. Eskom appoints principal agents to roll out the FBE units to sub-agents, and finally to consumers. Each principal agent enters into a fixed contract with Eskom, which contains conditions for providing the service and payment. The contract stipulates, among others, a fixed vending commission, and is payable to the principal agent by Eskom over the term of the contract. The vending commission is a rate that the vendors (principal agents) charge Eskom for Administer the FBE on its behalf.
- 1.4. NERSA annually reviews the NFBE rate that Eskom charges the municipalities for supplying FBE to qualifying households that are in the Eskom supply areas within the municipal boundaries. In accordance with section 16(2) of the ERA, a licensee may not charge a customer any tariff other than that determined or approved by the Energy Regulator as part of its licensing conditions. It is for this reason that NERSA determines the NFBE rate at which Eskom is reimbursed by municipalities for providing FBE units to qualifying customers on their behalf.
- 1.5. NERSA does not have the mandate regarding the FBE Policy, but does implement the DME EBSST Policy introduced in 2003 as required by section 4(a)(iv) of the Electricity Regulation Act, 2006 (Act No. 4 of 2006). The NFBE rate is adjusted annually using a methodology that was reviewed and approved by the Energy Regulator.

2. LEGAL BASIS

Section 16(2) of the Electricity Regulation Act, 2006 (Act No. 4 of 2006) ('the ERA') stipulates that 'A licensee may not charge a customer any other tariff other than that determined or approved by the Regulator as part of its licensing conditions'. In support of government policy initiatives, and in line with section 16(2) of the ERA, NERSA has developed a methodology that determines the NFBE rate at which Eskom is reimbursed by municipalities for providing FBE units to qualifying customers on their behalf.

3. PROPOSED MITIGATION TO CURB THE HIGH FORECAST FBE VOLUMES

- a) The forecast FBE volumes supplied by Eskom should be based on the historical audited data (one-year lag) of period between the time when the rate is determined, for example when determining the NFBE rate for 2021/22 financial year, the 2019/20 financial year total number of qualifying customers who collected their FBE allocation for the previous financial year, based on the list of qualifying customers received from municipalities will be used to ensure that the figures used are audited.
- b) The customer collection rate must be supplied per municipality.
- c) Eskom's forecast FBE volumes must reflect the current conditions of the market at the time of the application, such as the audited total number of customers that collected FBE tokens in the previous financial year (one-year lag).
- d) It is impossible to be 100% correct when forecasting. Should there be a difference between the actual and forecast FBE volume, the difference will be subject to the NFBE clawback/payback mechanism. This states that the difference should either be clawed back to Eskom (if the actual is higher than the forecast) or be given back to the customers (if the actual is less than the forecast).
- e) Eskom will submit on an annual basis the forecast as received and NERSA will verify this forecast from the various municipalities. The forecast FBE volumes should be limited to 2% or less than the previous year's (one-year lag) actual volumes. This is based on the past 3 years' data where Eskom forecast more by 4%, 8% and 12% respectively.
- f) The clawback/payback mechanism will only apply should the difference between actual and forecast volumes be 2% above when compared with previous years' (one-year lag) audited volumes. If the clawback/payback is less than 2% it will be passed through to either Eskom or customers.

- g) The clawback/payback mechanism is to allow for changes in the actual conditions for specifically the identified number of customers or forecast sales when compared to the assumptions made when the NFBE rate was approved.
- h) In order to verify the sales forecast, Eskom must furnish the Energy Regulator with the total number of qualifying customers who collected their FBE allocation per municipality for the previous financial year Audited (one-year lag) by 15 April annually.
- i) NERSA will request the Audited (one-year lag) number of customers configured, total number of approved customers to receive the FBE, and the total number of customers who collected their FBE allocation from the municipalities to verify the information supplied by Eskom.
- j) NERSA shall review and adjust the information submitted by Eskom before the determination of the NFBE rate annually.
- k) The implementation date for the NFBE rate is 1 July annually.

4. NFBE RATE MECHANISM

- a) NERSA developed a methodology to determine the NFBE rate.
 - i. This tool is used annually to determine the NFBE rate
 - ii. The current formula used to determine NFBE rate is:

$$\text{NFBE rate (c/kWh)} = \text{Total costs to supply FBE (R)} / \text{forecasted FBE volumes (kWh)}$$

- iii. The following revised formula shall be used to determine the NFBE rate:

$$\text{NFBE rate (c/kWh)} = (\text{Total Energy cost (R)} + \text{Total vending commission (R)} \pm \text{Claw back/Payback (R)}) / \text{Forecast FBE volumes (kWh)}$$

Where:

- Total Energy cost (R) = Annual total FBE consumption (kWh) x Eskom IBT 1st block rate for that particular year or the cost of the first 50kWh units for that particular year
- Total vending commission cost (R) = Annual FBE consumption (kWh) x total vending commission (R)
- Clawback/payback (R) = Different between forecast and actual volumes x previous year NFBE rate (c/kWh)

- Forecast FBE volumes(kWh) = forecast total number of customer's x FBE allocated (50/kwh) units x12 months
- b) When developing the mechanism, the following attributes were taken into consideration:
- i. the national number of customers supplied by Eskom as provided by the municipalities;
 - ii. the number of months to supply FBE, i.e.12 months;
 - iii. the amount of the free basic electricity units of consumption, i.e. 50kWh units per month;
 - iv. vending costs for supplying FBE (vending commission); and
 - v. Eskom IBT Homelight 20A residential tariff 1st block rate or the cost of the first 50kWh units for that particular year.

5. INFORMATION TO BE SUBMITTED TO NERSA

- a) The following information must be formally submitted to NERSA by Eskom:
- i. the total number of customers configured, total number of approved customers to receive the FBE as supplied by Municipalities, and the total number of customers who collected their FBE allocation (1 April to 30 March);
 - ii. the abovementioned information will also be submitted by Municipalities for verification;
 - iii. the forecast FBE volumes/number of customers for the next financial year of that particular year by Eskom;
 - iv. the vending commission rate for that particular year as agreed with vendors by Eskom; and
 - v. the signed contract agreements between Eskom and the vendors for verification.

6. APPROVAL OF THE NFBE RATE

- a) Eskom and municipalities submit all required information to NERSA as per the above guidelines.
- b) Failure by Eskom to submit all the required information on time, will result in NERSA not approving the NFBE rate for that particular year and the previous year's rate will be recommended.

- c) Should there be no new contracts between Eskom and the vendors in place in at the time of approval, NERSA will use the previous year's vendors commission when determining the NFBE rate for that particular year.
- d) The information received is then analysed by the responsible Analyst.
- e) Once the analysis has been finalised, the report is prepared and submitted to the Language Editor for editing.
- f) Upon receipt of the report from the Language Editor, the draft document is scrutinised by the Head of Department, then the Executive Manager (EM), followed by the Full-Time Regulator Member Primarily Responsible for Electricity (FTRM-E) and finally the Chief Executive Officer (CEO).
- g) The submission is then submitted to NERSA's Electricity Subcommittee (ELS) for recommendation to the Energy Regulator for approval.
- h) The process concludes with the Energy Regulator's approval of the NFBE rate for that particular financial year before 30 June.
- i) The Energy Regulator's decision is communicated to the relevant stakeholders [Eskom, the National Treasury, and the Department of Corporate Governance and Traditional Affairs (CoGTA)] before the 1 July implementation date, annually.
- j) Variances between the forecast and actual number of customers shall be assessed and analysed to determine the cause of the variance.

7. REVIEW AND MODIFICATION OF THE NFBE METHODOLOGY

The Energy Regulator will review the NFBE Rate Methodology as and when required to ensure that the contents reflect the current regulatory circumstances. The Energy Regulator also recognises that special circumstances may arise that may necessitate changes to be effected to the Methodology. The Energy Regulator will continuously incorporate justifiable changes that are considered necessary to immediately capture clarity, transparency and regulatory efficiency benefits.

8. EFFECTIVE DATE

The effective date of this methodology will be immediate, on approval by the Energy Regulator.

End.

