SUBMISSION BY BOARD OF ESKOM HOLDINGS SOC LIMITED
(REGISTRATION NUMBER 2002/015527/30)

TO

THE PORTFOLIO COMMITTEE ON PUBLIC ENTERPRISES INQUIRY INTO
CORPORATE GOVERNANCE AT STATE OWNED COMPANIES
1. INTRODUCTION

1.1. Thank you for the invitation and the opportunity to share with the Portfolio Committee on Public Enterprises and fellow South Africans, the evidence on issues related to the Governance of Eskom

2. DISCLAIMER

2.1. This submission is made to the Committee subject to the conditions set out in this paragraph 2.

2.2. Due to the pressures of time as more fully set out in Eskom’s letter dated 16 November and previous correspondence to the Portfolio Committee from Eskom, there may be information that is not available at the moment of making this submission. Eskom undertakes to provide such information before the end of the enquiry.

2.3. This submission is made reserving all Eskom’s rights as a Company and that of Board members individually and collectively including without limitation their rights in terms of the Constitution of the Republic of South Africa 1996, the Powers, Privileges and Immunities of Parliament and Provincial Legislatures Act No. 4 of 2004 and the Rules of the National Assembly.

2.4. Myself and any other current board member or official that gives evidence in this Inquiry may not be able to recall events from memory during question time and will attempt after the hearing to submit any further documents requested by the Committee. Failure to recall an event should not be interpreted as a refusal to respond to the question.

2.5. In the preceding weeks various former officials and one former Board member have made serious false and unsubstantiated allegations about the board and individual current and past board members. I would like to draw the Committee’s attention to the fact that while in some instances in our written submission we refer to a few of these inaccuracies, the failure to deal with such inaccuracies or to counter them in this submission or in the oral evidence should not be interpreted as acceptance by myself or the Board either individually or collectively, that such allegations are truthful.
3. CHALLENGES FACED BY ESKOM

3.1. In order for the Committee to appreciate the current challenges around liquidity and governance at Eskom, it is important to give some background of how these challenges emerged. These challenges are interrelated and related to structural and historical problems.

3.2. The importance of Eskom to the country, its people and economy cannot be overstated. Eskom generates approximately 95% of the electricity used in South Africa and approximately 45% of the electricity used in other parts of the African continent. Eskom generates, transmits and distributes electricity to industrial, mining, commercial, agricultural and residential customers and re-distributors.

3.3. I will deal firstly with the structural challenges. The challenges that the Board found when I was first appointed as a Board member in 2014, date back to the beginning of Eskom.

3.4. Eskom as a Company is 94 years old.

3.5. The Electricity Commission (Escom) was established in terms of the Electricity Act of 1922 to “stimulate the provision, wherever required, of a cheap and abundant supply of electricity for the economic advancement of the Republic of South Africa”. While it was run along strict business lines, the objective was largely the provision of service for public benefit and not for profit. The organisation was directed by a chairman and six other commissioners, all appointed by the State President for their knowledge and experience in the various sectors of the economy and in the electricity supply industry. The entity was non-regulated and set pricing according to its business requirements at the time.

3.6. On 1 July 2002, when Eskom was converted from a statutory body to a public company, known as Eskom Holdings Limited in terms of the Eskom Conversion Act, 13 of 2001. Eskom’s two-tier governance structure of an Electricity Council and a Management Board was replaced by a Board of Directors.

3.7. Today, Eskom is also regulated under licences granted by the National Energy Regulator of South Africa, originally under the Act (41 of 1987), replaced by licences under the Electricity Regulation Act (4 of 2006) and by
the National Nuclear Regulator in terms of the National Nuclear Regulatory Act (47 of 1999).

3.8. Unlike its non-profit mandate at inception, Eskom today operates with a commercial, compliance, and socio-economic mandate in keeping with achieving social, financial, and environmental sustainability. Fulfilling its commercial mandate, Eskom must ensure that it is financially viable to continue to operate and to raise debt to fund its business operations and capital expansions.

3.9. In fulfilling its compliance mandate, Eskom needs to comply with the various licences and also live by the various government policies that govern state-owned enterprises and companies in general.

3.10. Finally, Eskom’s socio-economic mandate helps South Africa achieve its broader developmental objectives of rural electrification, free basic electricity, job creation, and skills and supplier development.

3.11. Ladies and gentlemen, at this point, allow me to pause for, at this point, many may question whether it was these governance shifts that led Eskom down its current path?

3.12. On the surface, it may appear so, but the deep-rooted reality is that the answers lie in its boom and bust cycle – consistently moving in waves of excess capacity and capacity constraints, in line with economic fluctuations, over the decades. The boom cycle is typically represented by excess capacity, increase in sales, and excellent plant performance, while the bust cycle manifests itself through a shortage of capacity and poor plant performance.

3.13. So, while it may appear that Eskom recently took a stumble, the reality is that its operational and financial performance is expected in line with the bust and boom of the national economic flux.
3.14. A story that sounds overly familiar is the bust of the early 1980s. Complying with a request made in the mid-seventies and in the interest of the national economy to delay certain capital projects, Eskom lost three to four years of generating expansion, leading to the spate of power outages in the early eighties and an expensive capacity expansion programme, supported by government guarantees.

3.15. The 1983 De Villiers Commission of Enquiry was established as a result of concerns around the process and progress of the capital expansion programme and associated costs and impact on the economy. Power outages were frequent as a result of the unavailability of capacity and poor plant performance. At the time, plant availability was recorded at 72%. The new build at the time housed technology that was able to accommodate low-quality burn as a result of the poor sustainability of mines and poor quality of coal mined then. This followed the boom of the nineties and excess capacity due to the economic downturn experienced in the country. Plant performance was operating optimally, with 90:7:3 achieved, that is, 90% availability of plant, 7% planned outages, and 3% unplanned outages achieved in 1998. Eskom responded by driving a marketing initiative to increase sales and established Eskom Enterprises in 1999 to transition to new business operations and to grow new markets.

3.16. It was during this boom cycle that the new democratic government finalised the Energy White Paper in the late 1990s, outlining additional principles relating to Eskom’s monopoly status and the proposition of breaking up the sector into a separate system and market operator and regional electricity distributors. This also included the fateful decision of cancelling the construction of new generation plant in anticipation of private investment by independent power producers. It, furthermore, kick-started the process to develop regional electricity distributors or REDS, as per a Cabinet decision. The REDS were subsequently cancelled in 2008, despite Eskom having ring-fenced its operating units in preparation for the transition.

3.17. The bust that followed in 2007/2008 is well known – labelled by Eskom’s PR fraternity and engineers as load shedding. Load shedding was a consequence of a combination of events arising from the earlier deferral of planning and investment decisions by the new government, a similar unsound decision made by the Government in the mid-seventies. These
were a low energy reserve margin, inadequate coal supply, an increase in plant breakdowns in an ageing fleet, and insufficient generation capacity, coupled with a high demand due to economic growth and customer inefficiencies, thus resulting in load shedding – the controlled balancing of the power grid.

3.18. Eskom called for business, commercial, and residential customers to save 10% of electricity and to engage in energy efficiency measures.

3.19. Eskom’s strategy at the time included:

3.19.1. demand-side initiatives, with integrated demand management calling all customers to manage demand by using less electricity and adopting energy efficiency products such as compact fluorescent lights and solar water geysers; and

3.19.2. supply-side initiatives to increase capacity. This included implementing the build programme, improving generation plant performance, utilising gas turbines to supplement capacity, and securing sufficient coal to generate electricity.

3.20. Eskom’s financial stability was noted as a central challenge despite receiving a R60 billion equity loan from government. The average tariff failed to recover the full cost of producing electricity, with escalating primary energy costs and embedded derivative-linked contracts resulting in an accounting loss of R9.5 billion.

3.21. In addition, the funding model was inadequate for raising funds to finance the build programme. The capital costs of the build programme had escalated considerably due to an increase in global construction costs prior to the global economic crisis. The Board, under the then Chairmanship of Mr Bobby Godsell, had introduced a cost management programme that could see Eskom breaking even at an operating level.
3.22. During the latter part of 2009, Eskom experienced a leadership vacuum by losing its Chief Executive and Chairman, which impacted its reputation even further.

2010-2014

3.23. From 2010 to 2014, Eskom drove a recovery programme, achieving an increase healthy profits. Nersa had granted above-inflation tariff increases of an average of 31% in July 2009 and 24.8% in April 2010. Government’s support included R430 billion in financial support, with R350 billion in guarantees, to deliver the country’s electricity capacity expansion programme.

3.24. The country hosted a successful FIFA World Cup to which Eskom contributed by keeping the lights on. A new chief executive was appointed, and all vacancies in the executive management committee were filled.

3.25. The 2010 IRP was promulgated, providing guidance on the new expansions and diversification opportunities for greater regional development and electricity imports. The IRP provides a medium- to long-term plan that directs the expansion of electricity supply (including private and own generation) and power purchases from regional projects and demand initiatives in South Africa over the period 2010 to 2030. The IRP determines the timing and mix of the projects and provides the basis according to which NERSA will license projects.

3.26. Eskom subsequently signed on independent power producers to boost supply and diversify the national energy mix. Plans were in place to return the previously mothballed power stations and bring new units online. With the intent to ensure that IPPs obtained fair access on the transmission network, the government tabled the Independent System Market Operator (ISMO) Bill. This outlined energy planning, feasibility studies, IPP procurements, and market administration. This was, however, withdrawn in 2014/2015, as global implementation outlined potential risks.
3.27. In March 2011, in an effort to secure an energy-efficient future, Eskom, government, and business partners launched the biggest long-term countrywide saving movement called 49M. The objective of 49M was to change behaviour and to encourage all citizens to become more energy efficient, thereby protecting the planet, saving power, and sparing one's pocket.

3.28. The campaign was championed by the former Deputy President, Kgalema Motlanthe, and the former Minister of Public Enterprises, Minister Malusi Gigaba. The campaign, driven by Eskom’s Corporate Affairs Division, included advertising across radio, TV, and print media, and it reached South Africans through the participation of corporates and retail partners, who activated the 49M campaign among staff, suppliers, and customers nationwide. The movement urged every South African to “Lift a Finger”, which was all it took to switch off a light when not in use. The symbol of the key messages “Remember Your Power” and “If you are not using it, switch it off” was a yellow reminder string, a thread that tied these messages together. This became the single biggest effort driving South Africans at the time.

3.29. The success of the campaign is, today, evident from the reduction in electricity demand and sales, an increase in off-the grid supplies, an increase in energy-efficient products such as solar geysers, LEDs, and CFLs, and from energy-efficiency ratings on products in the marketplace.

3.30. Despite recording a net profit of R5.2 billion for the 2012/2013 period, Eskom continued to navigate through its financial and operational challenges. Funding new investments and the obligation to assure affordability for households and businesses remained key challenges flowing from the revenue gap resulting from the MYPD3 revenue determination.

3.31. Keeping the lights on, stabilising the short-term finances while managing an 8% annual average tariff increase allowed by Nersa, securing funding for the build programme, making progress on the build programme, and re-engineering the business for more effective performance remained critical in 2012/2013.
3.32. Operational challenges persisted, with the continued escalation of unplanned maintenance. Given a tight supply-demand balance, “Eskom had to frequently defer planned maintenance to ensure uninterrupted power supply, taking its toll on the generation fleet, the performance of which had become volatile”. Unplanned maintenance had increased from 7.97% to 12.12% at the end of March 2013. During this time, Eskom also experienced a significant set-back with the Duvha Unit 3 outage.

3.33. It was in 2013 that the Board approved the 80:10:10 strategy, which called for an 80% availability factor, 10% for planned maintenance, and an allowance for 10% unplanned outages.

3.34. Eskom limited electricity demand, and during 2012/13, demand management initiatives resulted in 2 244 GWh of electricity savings.

2014/15

3.35. On the 11 December 2014, a statement on the meeting of the cabinet of the Republic of South Africa of 10 December 2014 was released.

“Cabinet remains concerned over the disruptive effect the recent power outages are having on the daily lives of South Africans and its impact on households and business across the country. Cabinet adopted a five point plan to address the electricity challenges facing the country. A technical team war room for the implementation of the five point plan is constituted with immediate effect. The five point plan addresses the strain our electricity system faces. The plan covers:

1 The interventions Eskom will undertake in the period over the next 30 days
2 Harnessing the cogeneration opportunity through the extension of existing contracts with the private sector
3 Accelerating the programme for substitution of diesel with gas to fire up the diesel power plants
4 Launching a coal independent power producer programme
At this meeting cabinet appointed and announced a new membership for the Eskom Board of Directors

3.36. When I assumed my role as a board member at the end of 2014, I was surprised to learn that the landscape was more complex than what I perceived it to be as an ordinary citizen.

3.37. The month prior to my appointment, Eskom had yet again announced the development of a turnaround strategy to arrest the operational and financial decline and to stabilise the business. The Turnaround Strategy focused on four key areas: operational sustainability, revenue and customer sustainability, sustainable asset creation, and financial sustainability.

3.38. Eskom was still implementing load shedding, now in stage 3 impacting daily lives and industrial production.

3.39. Eskom’s narrative still read, I quote: “We have communicated for an extended period that the national power system is constrained due to the lack of available generating capacity. To balance and protect the power system, we have to apply demand management practices, which include utilising OCGTs and pumped-storage schemes, as well as relying on independent power producers (IPPs), interruptible load agreements, load curtailment by key industrial customers, and energy efficiency efforts by other customers. When sufficient demand savings are not realised, we have to resort to controlled, rotational load shedding.”

3.40. The company still faced financial challenges despite recording a profit of R3.6 billion (2013/14: R7.1 billion) and recording internal cost savings of R9 billion. Government provided an equity injection of R23 billion and conversion of its subordinated loan to equity (R23 billion + R 60 billion =
R83 billion). The shareholder also granted Eskom R350 billion worth of guarantees to assist with borrowings.

3.41. The build programme was behind schedule and had started later than it should have as a result of government’s attempts to bring in IPPs. Undertaking a capital expansion programme of such a magnitude 20 years after the completion of such previous programmes was met by a loss of skills and a lack of construction experience. The additional challenges of insufficient funding, labour unrest and demands on the build sites, poor contractor performance, and significant cost overruns on the project resulted in significant delays, which ultimately escalated costs even further. Eskom was hopeful at the time that it would synchronise its first unit at Medupi by the end of 2015. The unit was commercialised on 23 August 2015, eight years after starting construction on 14 August 2007. At the start of construction Eskom had optimistically projected that the last unit of Medupi would be commissioned in 2015.

3.42. In addition to these challenges, Eskom experienced a significant safety incident at the Ingula construction site, where six contractors lost their lives onsite. This was painful for the company and resulted in additional time loss, as the Department of Manpower requested a shutdown of the site to conduct the necessary investigations.

3.43. The lessons learnt were expensive to both the company and country and were regrettably experienced at Medupi, Kusile, and Ingula at the time. Only the 100 MW Sere Wind Farm came in on budget and on time, having been commercialised on 31 March 2015.

3.44. In addition, operational performance was also deteriorating. Generation plant availability (EAF) declined to 73.73% for the year 2014/15, compared to 75.13% in the previous year. Unplanned maintenance (UCLF) had deteriorated significantly from 12.61% in 2013/14 to 15.22%, partly due to the Duvha Unit 3 incident and the Majuba silo collapse.
3.45. The financial health of the organisation remained under pressure given the flat demand and rising operating costs particularly in primary energy such as liquid-energy fuel to run OCGTs and the cost of maintenance.

3.46. Despite this, the renewable programme was progressing well as Eskom purchased 6 022GWh from IPPs during the year, at a cost of R9.5 billion.

3.47. Ladies and gentlemen, as the newly appointed Board this was the backdrop which sketched the enormity of the task at hand. It was a responsibility which each of us agreed to shoulder. We had no choice but to take a principled stand and take the necessary action for the benefit of our country.

3.48. Undeterred, we garnered our individual strengths to tackle the challenges and possible irregularities that were brought to our attention through our engagement with the executives.

3.49. The Board agreed to meet more frequently to address operational and financial challenges. We established two-task teams, one a build and the second an operational task team, each chaired by a Board member and which included executives from the business. The objectives were to fast-track the build programme and to arrest load shedding. I have no doubt that it was this hands-on approach and key focus of the Board and the leadership of Mr Molefe at the time that saw the build programme being fast-tracked and load shedding ceased when it did.

3.50. We resolved as a board to take bold and decisive decisions, for the benefit of Eskom, the shareholder and the country at large.

2015/2016:

3.51. With the appointment of a new chief executive and chairman, Dr Ben Ngubane we positioned ourselves to emerge from the current challenges.
3.52. At the end of the financial year 2015/16, slightly more than 12 months from the time that the new Eskom Board was appointed, we had challenged and changed the fundamental assumptions that guide this complex business. Through the Design-to-cost strategy we had made steady progress and had seen notable improvements. This had contributed to operational and financial sustainability for the company and had resulted in reliable electricity supply for the country.

3.53. It was extremely heartening to receive many team based presentations at the Board. Ordinary employees came forward and shared with delight their achievements. Majuba’s collapsed silos was initially planned to be repaired in a few years. After a submission or two, this work was completed in a few months; all three silos were completely recovered and Majuba returned to a full and proud production of 6 x 600 MW of generation output.

3.54. Due to the able leadership of the new chief executive and his team, load shedding was terminated and we had made excellent progress on the new build programme with the commercialisation of Medupi Unit 6 in August 2015 and Ingula Unit 4 on 10 June 2016. To date the programme has been successfully fast-tracked with all four units of Ingula, Medupi Unit 5 and Kusile unit 1 having been connected to the grid.

3.55. We have developed a sustainable capital investment plan that prioritises projects closely aligned to our strategic objectives. These include our new build programme, the recovery of our generation asset base, completion of environmental projects and improvements in our transmission and distribution grid infrastructure.

3.56. We had taken full advantage of the equity injections by the shareholder and the conversion of the shareholder loan to equity.

3.57. We established a cohesive team between Board and Management and made an indelible contribution to achieving our combined success.
3.58. At the end of the financial year 2016/17 the performance reflected a concerted effort by the business to improve efficiencies, resulting in surplus capacity, increase cross-border sales, supported by improved plant performance.

3.59. Eskom is now open to support new investments in South Africa and across our borders. The move from a constrained power system to surplus capacity is a result of improved generation plant performance, units from our new build programme being commissioned and independent power producers being included in our mix.

Corporate Governance

3.60. There have been corporate governance challenges in Eskom over the years. One of the major challenges is the frequent turnover of both Boards and Chief Executives. For example in the last 10 years there have been 5 different chairpersons with each of them on average serving for a period of 2 years. Over the last 10 years there were 10 different Chief Executive Officers. This creates instability and a low morale and the inability to execute policies of Eskom to stabilise the situation. A new Board is about to be appointed and it will be the task of that Board to appoint a permanent Chief Executive Officer and I am confident that if the person appointed is the right fit for Eskom, Eskom can stabilise from a governance perspective.

3.61. I am confident that with the right leadership and intervention by the shareholder to try and deal with the structural reasons for the liquidity crisis within Eskom, Eskom can be restored to what it was.

4. ESKOM TRANSACTION WITH TNA MEDIA
4.1. On 14 April 2015, TNA Media (Pty) Limited ("TNA Media") concluded a sponsorship agreement with Eskom in terms of which, amongst others, TNA Media would grant Eskom, amongst others, the following –

4.1.1. live broadcast of events for at least 60 (sixty) minutes;
4.1.2. advertisements in the NEW Age;
4.1.3. two tables, of 10 (ten) guests each at events; and
4.1.4. a sponsorship speech, from the podium, before start of the events.

4.2. The duration of the contract was for 3 (three) years and to terminate on 30 April 2017.

4.3. The sponsorship fee payable by Eskom was R 43 200 000.00 (forty-three million, two hundred thousand rand), excluding Value-Added Tax ("VAT") for 36 (thirty-six) business briefing events at the cost of R 1 200 000 (one million, two hundred thousand rand) each.

4.4. The parties could cancel the agreement in the case where one of the parties breaches any terms of the sponsorship agreement.

4.5. Either of the parties could also, terminate the sponsorship agreement if any of the parties is declared "bankrupt" or any administrative receiver or similar officer, is appointed in respect of “whole or part of the assets of either party.”

4.6. The agreement between Eskom and TNA Media was authorised and signed by Mr Collin Matjila who was the acting group Chief Executive Officer of Eskom.

4.7. Management of Eskom raised its concerns about the sponsorship agreement in light of commitment made by Mr. Matjila to TNA due to his lack of delegated authority, to conclude the sponsorship agreement and the absence of budget from which to pay the sponsorship fees. The Board through its committees, established that Matjila had acted ultra vires and committed Eskom to a sponsorship fee that was not budgeted for in that financial year.

4.8. SizweNtsalubaGobodo were instructed to carry out a forensic review of the sponsorship deal. SNG confirmed that Matjila had exceeded his powers by committing Eskom to an amount of R 3 600 000.00 (three million, six hundred thousand rand) without consulting the Executive Committee ("Exco") of
Eskom and committing Eskom regardless of the absence of budget from which the fee would be paid in that financial year. SNG characterized this expenditure as irregular expenditure.

4.9. SNG, further, found that the sponsorship agreement between Eskom and TNA Media did not have an exit clause for Eskom, despite the fact that the legal department of Eskom had recommended that an exit clause be inserted to protect Eskom.

4.10. The findings of SNG were confirmed by Ledwaba Mazwai Attorneys.

4.11. The Board decided not to take any action against Mr Matjila because he was no longer an employee of Eskom.

4.12. The Board decided to ratify the sponsorship agreement after obtaining taking into consideration the legal and reputational consequences of cancelling this agreement.

5. THE PROCUREMENT PROCESS OF IT SERVICES TO REPLACE T-SYSTEMS SUSPENSION OF SAL LAHER

5.1. The procurement processes which were initiated to replace T-Systems South Africa (Pty) Limited ("T-Systems") were started before December 2014 and therefore, the members of the current Board have no personal knowledge of the procurement processes involved in replacing T-Systems and the suspension of Mr. Sal Laher.

5.2. Eskom’s records reveal that the procurement processes to replace T-Systems were suspended in and around December 2014 because more than 50% (fifty percent) of senior Eskom employees, who were critical to the management of the IT department, accepted voluntary separation packages from Eskom and left the employment of Eskom. This fact would have led to load-shedding because IT department is critical to the business of Eskom.
5.3. The Board decided to suspend the procurement process of replacing T-Systems to enable T-Systems to continue providing services to Eskom because T-Systems was well acquainted with Eskom’s existing IT systems and to discontinue their services, would have had a negative impact on security of supply.

5.4. Eskom saved approximately R 800 000 000.00 (eight hundred million rand) by continuing to use the services T-Systems because T-Systems allowed certain functions which were the responsibility of T-Systems to be carried out "inhouse" by Eskom.

5.5. The agreement between Eskom and T-Systems is valid until April 2018.

5.6. Mr Sal Laher was suspended by Eskom in November 2014. The reason for his suspension was that he failed to follow procurement processes. The Board has been advised that there was an amicable settlement between Eskom and Mr. Sal Laher. Mr. Sal Laher was paid a severance package.

6. THE EMPLOYMENT AND EARLY RETIREMENT OF MR MOLEFE AS GROUP CHIEF EXECUTIVE AT ESKOM

6.1. On or about the 20th of April 2015 Mr Brian Molefe ("Molefe") was seconded from Transnet to Eskom to assist with operational requirements at Eskom. Molefe was initially seconded for a period of 3 months, which initial period was later extended for a further 3 month period. In total, Molefe was on secondment for 6 months.

6.2. On the 28th September 2015 the Minister of Public Enterprises – Minister Lynn Brown announced that the cabinet had approved the appointment of Dr Ben Ngubane as Chairperson of Eskom’s Board and Mr Brian Molefe as the Group Chief Executive and Mr Anoj Singh as the Chief Financial Officer at Eskom.

6.3. On the 24th of September 2015, a draft offer of employment was prepared for Molefe on the basis that the Group Chief Executive - Molefe would be appointed on a permanent basis as a Standard F - Band Executive. The offer of permanent employment became effective from the 1st of October 2015. A formal letter was addressed to the interim Chairperson - Dr Ben Ngubane from the Minister of Public Enterprises on the 2nd of October 2015 in terms of which the Minister formally approved the appointment of Molefe. No mention is made in that letter whether the Molefe employment contract would be on a permanent basis or a fixed term.
contract. In that same letter the Minister requested that the Molefe employment contract be provided to her within 3 months from date of this letter.

6.4. On the 2nd of October 2015 a letter was also addressed from the Minister to Molefe confirming his appointment. It is important to note that no mention is made of the term of the employment contract. The inference drawn based on the letter of the 2nd of October 2015 addressed from the Minister to the Chairman as well as the letter addressed from the Minister to Molefe also on the 2nd of October 2015 that Molefe’s employment was on a permanent basis as no mention is made of a fixed term.

6.5. A standard F-Band contract of employment based on permanent employment was prepared on the 7th of October 2015. This employment contract was not signed by either Eskom as the employer or Molefe as the employee. On the 16th October 2015, a letter was addressed to the Minister from the Eskom Chairman requesting approval for the remuneration of Molefe, in terms of which the proposed total costs to company, was to be increased. This letter is indicative that the understanding by the Eskom board was that the employment of Molefe would be done on a permanent basis.

6.6. On the 1st of November 2015, the Minister responded to the letter of 16 October 2015, where she approved the proposed remuneration package to Molefe. This letter was addressed to the Chairperson and was received by the company secretary on 4 November. In that same letter she further expresses her view that the period of employment for Mr. Molefe be recorded as 5 years subject to annual performance reviews. This is the first time that Eskom is advised that the tenure of Mr. Molefe’s employment be on a fixed term basis and not permanent.

6.7. An offer of employment on a permanent basis which had been prepared was signed by Dr. Ngubane on the 9th of November 2015. The offer of employment was co-signed by Mr. Molefe on the 11th of November 2015. It appears the chairperson may not have been aware of the letter sent to him and the company secretary by the minister on the 4th of November.

6.8. It is important to note that the appointment letter did not state the specific term of tenure of the employment, although it was made clear that the offer of employment would be on a fixed term basis.

6.9. On or about the 16th of November 2015, various retirement issues were discussed between Mr. Molefe and the Chairperson. A specific term to be considered was whether Mr. Molefe would be entitled to early retirement at the end of his fixed term contract should his contract not be renewed. The Eskom Pension and Provident Fund was consulted on or about the 16th of November 2015.
to find out whether Mr. Molefe would be entitled to early retirement. The accepted rule within Eskom was that to be eligible for early retirement, an employee would have to have achieved a minimum age of 50 years and have been in service for not less than 10 years. Eskom Pension and Provident Fund confirmed that the tenure of service can be bought-in without having to serve the full ten year service. In other words, Eskom could pay in the balance of the years or the tenure that Mr. Molefe did not work in order to achieve the minimum 10 year threshold. On the 25th of November 2015 a letter was addressed by Eskom to the Minister in terms of which the specific retirement arrangements of Mr. Molefe were addressed and clarification was requested from the Minister.

6.10. In that letter Eskom specifically requests the following:

6.10.1. Regardless of Mr. Molefe’s age after the five year termination date he be allowed to retire from Eskoms service on the basis that he is deemed to be aged 63.

6.10.2. That the penalty prescribed by the Eskom Provident Pension Fund for retirement prior to age 63 be waived.

6.10.3. That Eskom carries the costs of such penalties (to be paid over to the Eskom Pension and Provident Fund).

6.10.4. In the event that Mr. Molefe’s contract is not extended beyond the initial five year fixed term, he will not be allowed to subscribe to any other SOC or Government Pension Fund;

6.10.5. Should the contract be extended however, it is important to note the costs of any subsequent penalties will decrease proportionately.

6.11. It is important to note that as at the 9th of February 2016 a formal response to the letter addressed to the Minister on the 25th of November 2015 had still not been forthcoming and at that time there was no formal contract of employment with Molefe.

6.12. On the 9th of February 2016, the People and Governance Committee meeting resolved that the early retirement of Mr. Molefe be approved within the rules of the Eskom Pension and Provident Fund with the benefit of buying-in additional years’ service to enable him to retire. It was also highlighted in that same meeting that a fixed term contract of 5 years for a Group Chief Executive was unheard of and unprecedented for Eskom, and that this was the first time a fixed term contract was being implemented at this level. Due to the loss of benefits Mr. Molefe suffered as a result of being on a 5 year contract as opposed to being a permanent employee the early retirement was seen as an effort to mitigate some of these losses and
incentivise him. The resolution provided that in cases where a Director who is appointed on a fixed term basis decides to take early retirement and has a shortfall in respect of the number of years prescribed to be served by the Eskom Pension and Provident Fund, Eskom shall:

6.12.1. Bridge the gap and pay the balance of the tenure or remaining years required to make up the entire ten year tenure;
6.12.2. Waive penalties applicable to early requirement;
6.12.3. Refund the Eskom Pension and Provident Fund the applicable costs for additional service added plus penalties applicable to early retirement.

6.13. On the 7\textsuperscript{th} of March 2016 a formal employment contract was drafted and signed by both Eskom and Mr. Molefe. This contract was based on a five year fixed term and on the basis of the resolution dated 9\textsuperscript{th} of February 2016, in terms of which early retirement would be permissible upon termination of the fixed term contract. On the 6\textsuperscript{th} of September 2016 it was decided to increase the long term incentive award for Mr. Molefe to two times the annual pensionable earnings as the amount was relatively low based on the benchmark against similar long term incentive awards to Chief Executive at this level.

6.14. On the 24\textsuperscript{th} of October 2016, the Eskom People and Governance Committee approved the additional award in the form of an increase of Molefe’s long-term incentive to two times the annual pensionable earnings.

6.15. On the 11\textsuperscript{th} of November 2016, Mr. Molefe formally submitted his request for early retirement in term of the rules of the Eskom Provident and Pension fund read together with the resolution of the 9\textsuperscript{th} of February 2016. In that same letter he indicated that his last day of service would be the 31\textsuperscript{st} of December 2016.

6.16. Mr. Molefe’s retirement letter was discussed at the special People and Governance Committee meeting on the 21\textsuperscript{st} of November 2016. The meeting was not quorate and could not make any decision. During that meeting the terms of the retirement letter requesting early retirement was noted and supported to be taken further through the process.

6.17. On or about the 13\textsuperscript{th} of April 2017, the Chairperson of the People and Governance Committee was made aware by a Journalist that alleged payments in the amount of R30 000 000.00 were made to Mr. Molefe from the Eskom Pension and Provident Fund. This is the first time that Eskom became aware of a potential leakage of confidential information regarding Molefe’s early retirement.
6.18. On or about the 19\textsuperscript{th} of April 2017, a request was made to meet the Minister. The meeting was attended by the Chairman Dr Ngubane, the Chairperson of the People and Governance Committee, the Company Secretary, the Minister, the Director General and three advisors from the Department of Public Enterprises and the Senior Manager dealing with Executive remunerations. Eskom explained that because Molefe was on a fixed term contract, Eskom had approved that at the end of the fixed term that Molefe be entitled to early retirement principally due to the fact that his tenure was on a fixed term basis and it was uncertain whether it would be renewed, and on the basis that he had in fact over a period of time served various stints of short duration on a fixed term basis with various other state owned entities such as Transnet. The net effect was that his pensionable salary did not have sufficient time in the form of years of service to accrue during his period of employment. The Minister was adamant that the funds in an amount of R30 103 915.62 paid to the Eskom Pension and Provident Fund in respect of Molefe’s early retirement would not be permissible and should be repaid.

6.19. In a letter from the ministry of Public Enterprises to the media dated 27 April 2017, the Minister formally declines payment of Molefe’s early retirement pension pay-out. In her communication to the media, the Minister indicates that the proposed pension payment pay-out is not justifiable in light of the current financial challenges faced by state owned entities and the country as a whole. The Eskom Board thereafter took the decision and then engaged with Mr. Molefe with a view to re-appointing Molefe and reinstating him as Group Chief Executive in accordance with the Minister’s directive not to pay out his early retirement pension. The effect of a reinstatement would be that Molefe is restored as Group Chief Executive and that he would in turn have to refund all monies paid to him as at the end of December 2016, in respect of his early retirement. In terms of a meeting held on the 2\textsuperscript{nd} of May 2017 the Eskom Board discussed various options available to them regarding Molefe’s retirement decision and the Minister’s directive not to pay-out his early retirement pension. It was decided that the Board would engage with Molefe with a view to rescinding the Board’s prior decision to accept his application for early retirement. The meeting confirmed that considering it did not have the support of its principal for the approval of the early retirement application and that they were legal risks associated with other options, the proposed option to rescind the previous decision would be a fair and clean solution in the interest of all concerned. It was therefore resolved that the Board elects to rescind the decision to approve the application in November 2016 of the Group Chief Executive Mr Molefe for early retirement. On the 11\textsuperscript{th} of May 2017 a letter was addressed to the Minister in terms of which the Eskom Board’s position regarding Molefe’s early retirement was communicated.

6.20. In that same communication Eskom communicated to the Minister that a decision had been taken by the Board to rescind Molefe’s application for early retirement. With this option Molefe would be required to pay-back any funds
received by him back to Eskom, as well as any Eskom Pension and Provident Fund funds paid pursuant to his early retirement and resume his employment as the CEO of Eskom, and he would additionally be re-instated as a Director on the Board of Directors.

6.21. In the same letter a second option considered was a non-consensual rescission in terms of which in the event that Mr. Molefe did not consent to a rescission of the decision taken to provide him with early retirement, Eskom would have to launch a court application to overturn its decision taken on the 21st of November 2016 (to approve early retirement for Mr. Molefe, as well as attempt to overturn the Eskom Pension and Provident Fund’s decision made pursuant to rule 28.3 of the EPPF rules. If Eskom does not bring this application, the Minister may institute an action against Eskom on the basis that its decision of 21st November 2016 to accept early retirement was irrational and unreasonable. This option would only be considered if Mr. Molefe did not agree to a rescission of his approval for early retirement.

6.22. The third scenario envisages resignation in terms of which Mr. Molefe’s application for early retirement be rescinded and thereafter Mr. Molefe retains the option to resign from Eskom’s employ. In this scenario he would be entitled to his normal retirement benefits in terms of the Eskom Pension and Provident Fund Rules. Eskom agreed that the employee may return the monies paid to him which were linked to his early retirement. Under the final option being a settlement payment, the parties may agree that Mr. Molefe’s approval of his early retirement be rescinded and in that instance they would pay him a settlement amount to be agreed on.

6.23. On the 11th of May 2017 a letter was addressed to Mr. Molefe by Eskom in terms of which it is recorded that the Board has taken a decision to rescind the initial decision to approve his early retirement. It is further recorded that the Board requests Molefe to resume his duty as Group Chief Executive by the 15th of May 2017 on the basis of a reinstatement agreement to be signed.

6.24. On the same date, namely the 11th of May 2017, Molefe concluded a contract to be reappointed as Group Chief Executive Officer. In that reinstatement agreement Molefe agrees that he resumes his duties as Group Chief Executive Officer and to pay to the Eskom Pensions and Provident Fund all the amounts due to the Fund which were paid to him pursuant to his early retirement. The period between 1 January 2017 and 15 May 2017 is regarded as unpaid leave.

6.25. It should be noted that in terms of the Eskom Pension and Provident Fund member’s guide to benefits clause 3.3(d) provides for early retirement with separation benefits. The following is recorded:
“a member between the ages of 50 and 65, who has contributed to the fund for a minimum of ten years, may go on early retirements with separation benefits and without penalties. By mutual agreement with the employer”.

6.26. The attainment of at least 50 years of age and the completion of at least continuous pensionable service rule is again confirmed in the Eskom remuneration and benefits practices policy dated 6 of November 2015.

In terms of the revised rules of the Eskom Pension and Provident fund, Rule 24 records the following under the heading Early Retirement:

“Notwithstanding the provisions of rule 23, a member may retire from the service after attaining the age of 55 years of age, in which case he shall be entitled as from the date of his retirement to a pension in respect of his pensionable service to the date of retirement calculated in terms of Rule 22 reduced by a factor equal to thirteen fortieth of one percent for each month by which the period from the date of his retirement to the date on which he would have attained the pensionable age exceeds 24 months.”

6.27. It therefore appears that in terms of the Eskom Pension and Provident Fund rules Mr. Molefe would have had to attain the age of at least 55 and not 50 before he can apply for early retirement. In terms of Rule 28 of the same rules this provision deals with retrenchment and not early retirement. It is accepted that Eskom and the Eskom Pension and Provident Fund mistakenly interpreted Rule 24.1 and Rule 28 in its interpretation regarding Molefe’s early retirement.

6.28. It is a common error between the parties and Eskom’s approval for Molefe to take early retirement based on the Eskom Pension Fund Rules was a reference to the incorrect clause reference as Molefe would have had to obtain the age of 55 and not 50 before he could take early retirement.

6.29. In conclusion, Mr. Molefe was initially seconded to Eskom for a 6 month period. On the 1st of October 2015 an offer of employment was made to Molefe initially on a permanent basis, however based on the communication from the Minister the contract of employment was changed to a five year fixed term contract.

6.30. The challenge with the five year fixed term contract is that the employee’s Pension does not have enough time to accrue as it is not known whether the employment or the fixed term would be extended for a further period or not. In the circumstances Eskom took a decision to allow Molefe to take early retirement on the basis or understanding that he would have reached the age of at least 50 at the end
of his fixed term contract and to the extent that he has not served a minimum of 10 years’ service.

6.31. It is accepted that Molefe’s employment on a fixed term basis was a first for Eskom and historically all Chief Executives have been employed on a permanent basis. It is further accepted that the Minister has never responded to Eskom’s letter dated 25 November 2015 requesting approval for Molefe’s early retirement.

6.32. It is only on the 19th of April 2017 that the Minister formally confirmed that she would not approve an early retirement and pay out to Molefe. As a result of the Minister’s directive, Eskom was proactive in rescinding its decision taken on the 9th of February 2016 to approve Molefe’s early retirement. Molefe was subsequently reinstated in May 2017 and the parties were restored ante to the same status quo they were in as at 31 December 2016 as a result of the rescission of the decision taken and reinstatement of Molefe.

7. SUSPENSION OF FOUR EXECUTIVES

7.1. The new Board was appointed at the beginning of 2015. During this period Eskom faced severe challenges. The country was experiencing stage 3 load shedding. The Department of Public Enterprises in a presentation to Parliament on 25 March 2015 estimated that stage 3 load shedding cost the economy between R60 to R80 billion per month. Eskom was using R1 billion per month on diesel due to the use of gas generators instead of coal. Eskom advised the Minister that it may not be able to pay salaries and the build programme costs escalated.

7.2. Amidst this crisis faced by the Company, at the second meeting of the new Board the then chairperson Mr Zola Tsotsi asked the then Company Secretary Mr Malesela Phukubje to request an urgent board meeting. This notice was sent out on a Sunday evening at approximately 8 pm in the evening on March 8. The Board meeting was called for the 9th March.

7.3. The notice was accompanied by a Memorandum submitted by the chairperson which referenced the implemented restricted supply of electricity to all areas for a number of months and the problem that notwithstanding the integration of Medupe Unit 1 continued maintenance and unscheduled shutdowns have and will continue to cause ongoing planned and unplanned outages. Reference was also made in the memorandum to the fact that the CEO publicly stated that these unplanned and planned outages would continue for a period of five (5)
years. The other problems mentioned were the fact that the Medupe and Kusile plants were years behind schedule and went billions over budget. The lost revenue as a result of lost sales arising from non-supply ran into billions. This coupled with escalating funding shortfalls had increased interest costs beyond prudential limits.

7.4. All this resulted in Eskom having to seek increasing funding from Treasury and it was also anticipated that funding shortfalls will continue. The memorandum also referenced serious and embarrassing issues relating to tender and other expenditure disputes some which become the subject of court actions which increased negative perceptions of Eskom.

7.5. It was also stated in the memorandum that such problems and failings create consequential risks which extend far beyond the Company and South Africans. It has a serious impact on the economy which covers all sectors and postponed foreign and domestic investments some of which are cancelled outright. In turn this creates increased unemployment and pressure on the fiscus.

7.6. The Board has been reliant on Executives for information. It was felt that the Board is obliged to establish the reasons for the crisis through a factual enquiry so that it could address the causes. It was therefore proposed that an independent external inquiry be held which was referred to a deep dive investigation and that the Board should act immediately given the serious impact of these problems on Eskom and the economy as a whole.

7.7. Based on the severe risk of further outages and little independent understanding of the facts it was felt that the Board should immediately act to establish firsthand the causes of these challenges and intervene to arrest them or deal with them. It was recommended that the Board urgently authorise and mandate an independent external enquiry for this purpose.

7.8. It was also recommended that this enquiry should be unimpeded by the management and the Board and other policy stake holders. It must be credible and objective and it must have a mandate to be penetrating and unhindered. The Board must create the space and environment within the company for the investigators to be unimpeded and with no influence from Management.

7.9. The Chairperson then placed this resolution which was drafted by him before the Board. It was further recommended that the investigation must be mandated to a Board sub-committee who will then draft Terms of Reference and will be mandated with oversight of the enquiry. The resolution proposed that the Board
appoint a Board sub-committee comprising of Mr Tsotsi, Miss Mabude who is chairperson of the Audit and Risk Committee and myself who was at the time chairperson of the People’s and Governance Committee and that they be mandated with delegated authority of the Board to determine the Terms of Reference of the enquiry and to contract the independent investigators. The enquiry must take place within three (3) months and a final report must be presented to the Board, the Minister and the Presidency not later than 30 June 2015.

7.10. At the board meeting, Mr. Tsotsi reported to the Board that the Presidency had expressed concern that the impact of Eskom and the power outages on the country was being understated. It was felt that the Board should get to the bottom of matters and establish the exact causes of the problems so that it could take decisive action. Mr Tsotsi said that he had been requested to ask the Board to authorise an independent external enquiry.

7.11. A discussion among Board members followed and aspects of the Resolutions were changed for example the Board decided that the Finance Director should be approached to fund not the Minister of Finance. Mr Tsotsi reported that an independent resource had already been identified by the Presidency to carry out the resolution and he, the chairperson, had already gotten a document in that regard.

7.12. Board members raised a number of objections including that they were not comfortable with making a major decision such as this based purely on a two (2) page document and the concern that for a period of three (3) months both the Board and Management focus would be taken away from resolving the matters at hand. Others felt that there were insufficient facts placed before the Board to make such a far-reaching decision. Members also felt that if as the chairperson said this was a request from the Presidency it should simply have been a directive to the Board from the Presidency or the shareholder representative in which case the resolution should state that the enquiry was a request from the Presidency. It was also felt that while deviations from procurement processes were allowed when warranted it would be necessary to understand why the Presidency required this deviation for this committee.

7.13. In response to these concerns Mr Tsotsi said that it would be prudent to receive a direct communication from the shareholder representative being the Minister around the issue and he undertook to discuss the feeling of members with the shareholder.
7.14. At the meeting of 9 March it was resolved that the request for the establishment of an external and independent enquiry was noted. Secondly it was resolved that the board should engage with the Minister of Public Enterprises to obtain clarity around the Terms of Reference the Scope of Objective and Achievement of the Board of Enquiry.

7.15. Due to the concerns raised by the board members on the 9th March another board meeting was convened this time with the Minister in attendance in order to clarify the issues raised in the previous meeting. This meeting was held on the 11 March at 12 mid-day. The meeting started at 10 am with the Minister in attendance. At this meeting the Minister once again raised concerns about the Eskom board getting to grips with the operational issues and to try and resolve the underlying reasons for the load shedding and other problems.

7.16. From 12 noon the board held an in-committee session. At this in-committee session Mr Tsotsi once more proposed that an enquiry be done and that certain executives be asked to step aside during the course of this enquiry to ensure that the enquiry remains independent and without interference.

7.17. The Minister made it clear that she has no authority as to instruct the board as to what to do but mentioned certain issues of great concern to her such as the negative developments in the South African economy being the fall of the Rand, the Standards and Poor two (2) year review leeway period granted to the country, the low growth of the economy and the possible effect of a downgrade of the sovereign credit rating. She was also concerned about the February level of load shedding. In the meeting with the Minister various questions were raised by board members such as the cancellation of the meeting of 26 February 2015.

7.18. After further discussion it was agreed that the enquiry would occur and that executives who are responsible for areas which will be the focus of the enquiry should step aside temporarily for the duration of the enquiry in order not to impede it. The meeting with the Minister lasted from 10h00 till 12h00 thereafter the board went into an in meeting. At the meeting further discussions were held about the enquiry. Board members felt that based on the motivation and the concerns around the impact of the challenges at Eskom on the economy that there is a need for a fact finding enquiry. However the board did not accept all the recommendations by Mr Tsotsi on how the enquiry should be conducted. It felt that rather than a committee comprising of the chairperson it should be the Audit and Risk committee that should be the custodian of the process and it should where necessary engage with other committees.
7.19. Mr Tsotsi once more highlighted the fact that he believed it was necessary for the employees to step aside. Board members raised a question regarding what impact this would have on the operations of the business given issues of continuity. Some board members still wanted a fact finding exercise to be undertaken before actual suspension were implemented as this would be necessary to avoid acting against possibly innocent executives. In response to these concerns Mr Tsotsi suggested that some of the executives were involved in wrongdoings and listed these.

7.20. Mr Tsotsi identified people who needed to be requested to step aside, as the Group Executive; Commercial and Technology; Group Executive Group Capital; the Finance Director and Chief Executive Officer. An Aide Memoire was presented by him which contained a draft suspension letter and contained specific instances of alleged wrongdoing by three (3) executives.

7.21. Board members felt that it would be better if subcommittees discussed the matters first and ensure that proper processes were followed. In response Mr Tsotsi advised that a lot of ground work had already been done in this regard and a report can be given to board members at a later stage. He felt that the most important thing is that the enquiry is done and it should be done soon. Board members pointed out that it would be of great concern especially in the market for Eskom to suspend the Financial Director and the Chief Executive at the same time. Mr Tsotsi alleged that the Finance Director had problems about her as because she had allegedly met with Tenderers during a tender process. The board members nevertheless felt that the enquiry should not focus on individuals but rather areas of responsibility which is why people should be allowed to step aside for its duration.

7.22. After further discussion it was then resolved that the enquiry should proceed and that the executives concerned should be placed on leave and that the Audit and Risk committee and the people in Governance Committee should work on the Terms of Reference. The Board also requested that an opinion be sought from a labour lawyer to ensure due process be followed.

7.23. The stepping aside of the Executives were for a period of three (3) months only after which it was understood that they would come back in view of the fact that there were no findings of wrongdoing against them as yet.

7.24. Given the crisis that the country faced and the impact on the ongoing load shedding on the economy and having weighed up all the necessary facts decided
that such an enquiry is necessary and approved the suspensions. The enquiry was conducted by Dentons and was concluded within three (3) months.

7.25. I would further like to point out to the Committee that the report of alleged wrongdoing which Mr Tsotsi referred to in the meeting of 11 March has never been presented by Mr Tsotsi despite such a request.

7.26. The board became even more concerned about Mr. Tsotsi’s after the decision was taken on the 11th March 2015. This concern related to the Terms of Reference of the enquiry and Mr. Tsotsi’s insistence on engaging consultant Mr. Nick Linnell without a proper procurement process.

7.27. During a meeting on 14 March 2015 after Mr Tsotsi left the meeting and Dr Ngubane acted as the chairperson, Board members expressed concerns around the conduct of Mr Tsotsi. Concerns related to the fact that Mr Tsotsi appeared to be involved operationally which was not the role of non-executive directors. It was accepted that Mr Tsotsi is entitled to perform his duties as chairperson but he should not be allowed to sign contracts and engage in operational matters. Other concerns about the chairperson were putting our press statements about the enquiry without the Boards approval.

7.28. In a meeting held on 19 March 2015 Mr Tsotsi acknowledged that he had appointed Mr Nick Linnel without proper processors and he apologised for this. Board members felt that certain actions of Mr Tsotsi had compromised the independence of the enquiry and the Board took certain decisions. The Board resolved that in order to avoid such lapses, the Audit and Risk Committee should deal with the matter to ensure a fair and transparent process. The Board had a long discussion at that meeting and confirmed that they believed based on the crisis faced by Eskom and its impact on the economy that a fact finding investigation was necessary but that it is important that it be done in a manner that ensures independence and integrity. The conduct of Mr Tsotsi up to that point concerned the Board members to such an extent that they discussed two options which either meant that Mr Tsotsi should step aside for the three (3) months as well or based on his apologies for his action the Board could work with him and provided that he obeys the rules of governance.

7.29. A decision was taken to express a lack of confidence in Mr Tsotsi. Board members were very unhappy about the fact he had a report purportedly drafted outside Eskom but had not produced such report. There were othr
reasons why the board felt they have no confidence in him and these were contained in a charge sheet.

7.30. After the enquiry two (2) of the four (4) executives indicated that they would not like to come back to Eskom after the enquiry was concluded and agreed on a settlement with Eskom. Mr Matona took Eskom to the labour court but later settled. One (1) of the executives Mr Koko decided to return. Eskom agreed for Mr Koko to return.

7.31. It has been suggested in the media and here at this committee that the reason for Eskom’s downgrade was based on the suspensions of the four (4) executives. I think it is important to point out that while that was one of the reasons, other reasons were cited by Standard and Poor. In their Standard and Poor stated that in their opinion “material execution risk remains associated with the government’s support plan, and that Eskom’s operating performance has not yet stabilised due to rising costs and the very tight generation capacity margin in South Africa.”

7.32. Faced with a crisis of the magnitude Eskom faced at the time the Board was concerned to bring stability to the Company and applied its mind, had discussions both in board meetings and in Audit and Risk committee and People and Governance.

7.33. In para 4.17 of Mr Tsotsi’s statement he indicated that he was on the line with 52 individuals trying to defend what was essentially an “indefensible” position regarding the suspension of the individuals. Based on the fact that he is the person who came to the Board with the suggestion of the enquiry and the suspension of the individuals Mr. Tsotsi knew that this statement was factually incorrect.

8. PREPURCHASE OF COAL FROM OPTIMUM

Background

8.1. The Committee requested us to comment on the purchase of Optimum Coal Holdings by Tegeta from Glencore. I wish to point out that Eskom was not involved in the purchase of Optimum Coal Holding by Tegeta and is therefore is unable to assist the Committee in this regard as this was a commercial transaction between two private companies. What I can inform the Committee
about is the pre-purchase of coal from Optimum by Eskom and I set out the facts below.

**Eskom Coal Strategy**

8.2. It is important by way of background to briefly speak about Eskom’s coal strategy. In 2008 Eskom implemented its coal strategy which was revised in 2012. The purpose of the strategy was to drive several strategic objectives. However the operating and financial environment had shifted significantly over the past 5 years since 2012 in particular in the following key areas, funding, demand and energy mix, the coal supply landscape, emissions regulations and coal contract performance.

Based on this five (5) objectives were developed to form a revised coal strategy these were:

**Financial Sustainability:**

8.2.1. Attain a delivered cost of coal in line with the NERSA, MYPD determination while managing escalations year on year after that;

**Generation of least cost production:**

8.2.2. Ensure optimal dispatch of coal-fired power stations in least cost merit order;

**Security of Supply:**

8.2.3. Achieve an acceptable balance of security of coal supply and risk exposure, ensuring that generations burn plan is met and prescribed stockholding is maintained;

**Logistics Optimization:**

8.2.4. Optimize road and rail transportation operations to drive cost efficiency while delivering the road to rail migration programme;

**Market Transformation:**

8.2.5. Leverage Eskom’s buying power to enable coal market entrance by Black emerging miners and to drive Eskom’s transformation objectives.
8.3. Financial sustainability is the overarching objective of the Eskom coal strategy, with several Eskom initiatives identified to achieve the cost targets.

8.4. Therefore, the approach of the Eskom Coal Strategy is to optimise value from the existing cost-plus mines by:

8.4.1. Providing the required capital to cost-plus mines where a clear positive business case for Eskom’s long-term coal cost exists;

8.4.2. Implementing initiatives to maximise the volumes of cost-plus mines while minimising unit costs;

8.4.3. Ensuring the optimisation of any approved capital (for example, capital scrubbing and timeous delivery of projects);

8.4.4. ensuring increased cost-plus mine volumes, which also reduce the share of short-/medium-term coal and overall Eskom coal bill; and

8.4.5. using Eskom’s position to support country developmental objectives in a cost-effective way.

8.5. Allow me to provide the context with regard to prepayments. Firstly, prepayment is a common commercial practice that is used widely and is not unique to Eskom contracts. It is used in large projects, coal mining contracts, and emergency supply contracts. The principle of prepayment is prevalent in Eskom’s cost-plus supply contracts with large mining houses such as Anglo American, South 32 (formerly BECSA), and Exxaro. These mining houses supply approximately 80% of Eskom’s coal, while Tegeta supplies less than 5% of the coal volumes required by Eskom.

8.6. History can attest that this was common practice in the industry. For example, in the 1960s, Eskom negotiated a long-term (40-year) contract for Komati Power Station, paying for the actual cost of mining, including an agreed profit margin. Since Eskom could obtain capital at a cheaper rate than the mining house, it also provided most of the capital associated with the colliery. This was done due its costly experience at Klip Power Station, where the colliery had run out of coal before the station had come to the end of its useful life. The lessons learnt over the years is how we achieve a balanced risk exposure to both parties.

8.7. Eskom used the prepayment method in the past when coal stocks were low. This was to secure coal stocks and to avoid load shedding.
8.8. The first Eskom coal emergency arose in 2008 after load shedding due to constrained coal supply conditions. During the 2008 emergency, the Eskom Board approved advance payments to the value of R400 million to enable suppliers to undertake projects needed to supply coal. To this end, Eskom concluded a coal processing contract with prepayment terms. The agreement was with Isambane, who eventually paid off the prepayment.

8.9. Furthermore, a prepayment in the form of a loan was provided in 2008 to buy equipment to process coal. The loan was recovered in 12 consecutive instalments from 1 March 2008.

8.10. Eskom also entered into loan agreements to assist Rand Mines for capital expenditure. The first loan was payable over a period of 20 years until 31 December 2013. The second loan was in 1998, and it will be paid in full by December 2017. Eskom also assisted another Rand Mines operation with a loan, which has since been paid, for bridging finance.

**Prepurchase of Coal from Optimum**

8.11. On 8 December 2016 a round robin resolution was submitted to the Board by management.

8.12. The round robin was accompanied by a submission which contained the motivation for the round robin. The submission was titled: Prepurchase of coal from Optimum Coal Mine (Pty) Ltd.

8.13. The background to this was that Mr Koko in his capacity as Chief Executive Generation on 6 December 2015 wrote a letter to the Department of Mineral Resources. The letter dealt with the security of coal supply to the Hendrina Power Station. Referring to Optimum, the second paragraph of the letter read as follows:

“In rather dramatic fashion, the company was placed under business rescue and Eskom was faced with intermittent veiled threats of liquidation while at the same time, the business rescue practitioners purported sort constructive engagement between the parties”.

8.14. The letter further went on:
“Optimum supplies one of Eskom’s key contributors to the National Power Station as Hendrina Power Station is a stalwart in the Eskom fleet, supplying approximately 2000 MW to the national grid. Glencore was fully aware of the dynamics and history relating to the nature of the coal supply agreement and its structure when it concluded the sale with its previous owners.”

8.15. Referring to a representative of Glencore not insisting on the extension of the Kroonfontein Coal Supply Contract with Eskom, Koko stated further:

“Eskom is perplexed by this about-turn given the events of the past few months and at the blatant disregard Optimum displays for the impact that the threats of liquidation has on the precarious balance of electricity security and commercial viability. As a Glencore operation, Optimum surely cannot be perceived to be acting in the national interest.”

8.16. Mr Koko expressed his concern around the question of business rescue and indicated while they appreciate the turnaround of the business the “erratic display of business stability” may compromise security of coal supply to Hendrina in the short to medium term.

8.17. He indicated given the serious risk of security of supply to Hendrina Power Station, Komatie Power Station and Arnot Power Station is of key national interest which is why he thought it appropriate to bring it to the attention of the Director General in the Department of Mineral Resources. Mr Koko then requested intervention by the Department of Mineral Resources to obtain a resolution of the problem of coal supply.

8.18. The Director General of Department of Mineral Resources responded in a letter indicating that they will engage with parties and will take certain steps to assist considering the significant risk to the country. The Department requested that Eskom play an active role in supporting the rescuing of the mine and in return for securing the honouring of the current contract up to 2018 to consider making a pre-payment for up to one years coal supply. This was to ensure that supply is guaranteed and averting any national crisis.

8.19. The resolution authorized the chief executive officer, and the group executive Generation and the chief financial officer to conclude a pre purchase agreement with to negotiate a prepurchase of coal agreement with the proposed owners of Optimum.

8.20. The motivation for the round robin was stated that Eskom faces a supplier risk of coal to the Hendrina power station of 5.5 Mtpa by OCM as result of the business
rescue proceedings. It also indicated that there was a potential proposal from the business rescue practitioner which was supported by the department of mineral resources and this related to the purchase of coal to the value of R1.86 billion which would mitigate the supplier risk. The counter party risk was to be mitigated via section of the coal to Eskom.

8.21. The funding of the pre-purchase was going to be secured by reducing the working capital inventory from 54 days to 40 days. Eskom was going to achieve a value benefit of R238.9 million.

8.22. The motivation further indicated that the proceeds of the R1.86 billion pre-payment of coal were to be used by optimum to extinguish existing liabilities to ensure the business continues as a growing concern. It further stated that the shutdown of Optimum could potentially result in thousands of job losses.

8.23. Board members had a number of questions including whether the price was the best price. The board also said that the matter must be discussed at an IFC meeting rather than merely via round robin which IFC meeting took place the following day on 9 December.

8.24. After being satisfied regarding this, the board resolved to approve the round robin resolution subject to all the necessary regulatory approvals having been obtained by Eskom and the supplier respectively as and when necessary. The management and company secretary would know that any amount above R1.5 billion has to be approved by the executive authority being the Minister and therefore the board assumed that they would do this.

8.25. Based on all the submissions, the board believed that this payment was for the pre-purchase of coal from the Optimum coal mine. The board was therefore shocked to see in the press sometime in July 2017 that management had converted what was meant to be a pre-payment into a guarantee.

8.26. In her evidence to parliament Ms Susan Daniels made it clear that she was aware from at least 10 December that the prepurchase was converted into a guarantee. She stated that on the 10th of December Ms Caroline Henry who was a senior general manager for the treasury department in Eskom decided that instead of laying out the 1.6 billion in cash she would prepare a note and rather request that a guarantee in favour of the Tegeta to be issued through ABSA. According to her own evidence, she would have worked on the guarantee with Ms. Henry. This guarantee would be for three months and she stated in her evidence that
she understood that it exceeded the borrowing limit of Eskom and needed approval.

8.27. Despite Ms Susan Daniels being aware from as early as 10 December 2015 that a guarantee was issued contrary to what the board resolution stated, she failed to inform the board that this was the case. At the board meeting of 19 April 2016 she again failed to inform the board that contrary to what the board authorised a guarantee was issued without the necessary approvals. This is why in the minutes of 19 April 2016 there is merely noting and confirmation of a prepurchase of coal from Optimum mine. At no stage was the board aware of Tegeta or that it was given a guarantee.

9. **ESKOMS RESPONSE TO PUBLIC PROTECTOR**

9.1. The Public Protector sent questions to Eskom management before she released her report in November 2016.

9.2. Management through Mr. Brian Molefe, Mr. Anoj Singh and Ms. Ayanda Nteta, responded to the questions which were sent to Eskom and the Public Protector does deal with some of the responses from Eskom management in her report.

9.3. The Eskom Board of Directors ("the Board") was not given an opportunity to deal with issues raised by the Public protector in her report. The Company Secretary and head of Legal Services Ms. Suzanne Daniels responded to issues raised in the report but did not consult the board on such responses in spite of the fact that reference was made to some board members and the board. To date Board does not have access to the response which Ms. Daniels sent to the Public Protector.

9.4. The Board, even though it was constituted with new members except the Chairperson, has a few comments regarding some of the observations by the Public Protector on Eskom. The board sought legal advice about any action it could take regarding the report but was advised due to there being no findings, only observations, any review would not be successful. The Public Protector’s comments about Eskom are in pages 310 to 315 of the Public Protector’s report. The one issue which the Public Protector raises in respect of Eskom, is the pre-payment for coal to TEGETA Exploration and Resources (Pty) Ltd ("TEGETA") in April 2016.
9.5. The Public Protector also dealt with the relationship between the Gupta family and individual former Board members of Eskom. I’m not able to comment on this and some of the former members of the Board, have dealt with this issue before this committee.

9.6. The Public Protector seems to suggest in her report that the Eskom Board breached its fiduciary duties to uphold the values enshrined in section 217 of the Constitution of the Republic of South Africa, 1996 ("the Constitution") as well as section 50 of the Public Finance Management Act No. 1 of 1999 ("PFMA") in approving the pre-payment for coal to TEGETA.

**Prepayment for coal from Tegeta**

9.7. The Board Tender Committee ("BTC"), a sub-committee of the Board on 11 April 2016, was approached by management to consider, on an urgent basis the purchase of coal from TEGETA to supply Arnot Power Station for five months.

9.8. This submission by management required the following resolution from the BTC

“1. Addenda to the Short-Term Coal Supply Agreements between various suppliers and Eskom be concluded to extend the supply of coal from various sources to Arnot Power Station for up to a further five (5) months and/or such period as may be requested by the supplier but not later than 20 September 2016;

2. The Chief Financial Officer is hereby authorised to approve the basis for prepayment to secure the fixed coal price for the period of extension provided that there is a discount in the price, the supplier offers a guarantee in favour of Eskom and that the CFO can provide assurance to the committee that the transactions are economically viable for Eskom; and


3. The Group Executive (Generation) is hereby authorised to take all the necessary steps to give effect to the above, including the signing of any consents, or any other documentation necessary or related thereto.”

The “Salient Facts” are inter alia as follows –

“The requirement for the supply of contract coal originates from the April 2016 Supply Plan as presented at the Primary Energy Tactical Control Centre of 8 April 2016: It was identified that supply to Amot will not be adequate to meet the burn requirements of the power station over the winter months and that there is an urgent need for additional coal. This identified requirement is as a result of the need to build up stock days over a short period while the (RFP request for proposal) for Arnot is being finalised. This shortfall of supply amounts to approximately 2.1 million tonnes.

At present, this RFP is in the negotiation phase and it is anticipated that it will take up to a maximum period of 5 (five) months to conclude the supply contracts.

The current short-term portfolio consists of two suppliers, namely Umsimbhi Mining Pty (Ltd) and TEGETA Exploration and Resources (Pty) Ltd. Umsimbithi is contracted to supply Amot with 540 000 tonnes and is currently underperforming due to protracted Industrial action. The current contract supply will then be depleted in and around June 2016, should the Industrial action be stemmed and full mining operations resume. The supplier indicated a willingness to extend from July 2016 until September 2016 on similar terms and conditions.

TEGETA's short-term contracts are for 600 000 tonnes of coal from Optimum's export. Supply for these contracts is due to be completed by the 15 April 2016. The coal from Optimum's export stock is a higher-grade coal that is suitable for Amot and Kriel Power Stations and is difficult to source from elsewhere.
These contracts were entered into in terms of the Medium-Term Mandate granted by the Board Tender Committee (BTCI 11 September 200. The BTC approved a mandate to negotiate and conclude CSAs on a medium-term basis for the supply and delivery of coal to various Eskom Power Stations for the period October 2008 to March 2018 and this included the beneficiation of coal by suppliers or their contractors.”

The benefits for extending these Short-Term Contracts Include the fact that the coal is being mined and can be delivered without delay –

“•TEGETA has the potential to supply approximately 250kt per month and Umsimbithi approximately 180kt per month. It would therefore be in the best interests of Eskom to negotiate and conclude extensions to these Short-Term Contracts to alleviate the coal shortfall at Amot due to the closure of Amot colliery. Additionally, to alleviate the shortfall coal requirements at Kriel Power Station due to the underperformance of Kriel Underground mine;

• By procuring this coal for Amot and Kriel Power Stations, it will assist towards building stock days as according to the April 2016 Supply Plan, as presented at the Primary Energy TCC of 8 April 2016 there is currently an estimated 2.14Mt tonnes shortfall at Amot Power Station for FY2017 and 280 000 tonnes shortfall at Mel Power Station for FY2017.

Both suppliers have indicated a willingness to extend current contracts, however, TEGETA has requested that Eskom consider some form of prepayment to enable it to meet the production requirements from the export component of the mine in lieu of the fact that is subsidises the direct feed to Hendrina Power and this will enable it to meet the coal supply demands for the two power stations in the short term.”

9.9. The document states that the cost of the TEGETA prepayment for the next 5 months will be approximately R 586,787,500.00.
9.10. The above document was approved and signed on 11 April 2016, Ms. Ayanda Nteta, Mr. Edwin Mabelane and Matshela Koko.

9.11. The approval of advance payment, as requested by management on 11 April 2016, is covered in Supply Chain Management Policy 32-1034 Rev 2 of 2014 ("SCM 32-1034").

SCM 32-1034 provides, inter alia, that whilst Eskom does not encourage the provision of advance payments, an advance payment may be an acceptable strategy for Eskom in certain circumstances. This may be considered in cases where the supplier will have to make a big capital outlay before starting with the contract. It further indicates that an advance payment will only be issued on condition that the supplier must provide an advance payment bond/guarantee and that the relevant contractual provisions relating to advance payments also need to be included in the contract. As I indicated in paragraph 9 there are precedents for this practice.

9.12. On 8 April 2016 TEGETA made an offer to supply additional coal for the Arnot Power Station from the Optimum Coal Mine over a period of five months. This offer was made subject to x prepayment for the coal. The purpose of prepayment was to secure coal for Eskom, particularly of the high quality that was required by Arnot Power Station. To ensure TEGETA’s ability to meet the production requirements for both Hendrina and Arnot in the short term, prepayment was requested. TEGETA indicated that the prepayment would enable them to operationalise plant and equipment that had been placed on 'care and maintenance' during the shutting of the export component of the mine.

9.13. The BTC approved pre-payment to TEGETA of R 659 558 079.38 (six hundred and fifty-nine million, five hundred and fifty-eight thousand and seventy-nine rand and thirty-eight cents) inclusive of Value-Added Tax ("VAT").

9.14. The BTC resolved, inter alia, that the Chief Financial Officer ("CFO") is authorised to approve the basis for pre-payment to secure the fix coal price, provided –

   9.14.1. there is a discount of the price;
9.14.2. the supplier offers a guarantee in favour of Eskom; and
9.14.3. the CFO provides assurance to the BTC that the transaction was economically viable for Eskom.

Public Protector’s Observations

9.15. The Public Protector says the following in her report –

“After evaluating the responses received from Eskom, it is clear that they do have the requisite policies in place which provide for a prepayment of coal to be made. This is in line with various agreements put in place by Eskom after the energy crisis in 2008.”

9.16. While acknowledging that the Board had the requisite policies to award prepayment, she made the following comment –

“Eskom had previously done extensive due diligence on OCM which formed part of the Co-Operation agreement, they were aware of exact production outputs for coal and the price of coal being supplied by OCM. At the time of concluding the contract with TEGETA for the supply of coal to Arnot power station, Eskom was fully aware that the sale of all shares in OCH to TEGETA had not gone through. It appears to not make commercial sense for Eskom to contract with TEGETA for a higher price of coal knowing exactly where the coal was being received from.”

9.17. It is clear from the above paragraph that the Public Protector does not make a finding about breach of fiduciary duties by the Board (BTC) but rather, speculates that the transaction may not make “commercial sense.”

9.18. What she fails to take into account is that the price for coal supplied to Arnot was higher than price for coal to other power stations because of the quality of coal required to power Arnot. Eskom paid R 1132/ton (one thousand, one hundred and thirty-two rand per ton) to Exxaro for the supply of coal to Arnot and the amount which Eskom pre-paid to TEGETA was less than the amount paid to Exxaro per ton.
9.19. Furthermore, Ms. Ayanda Nteta, gave the Public Protector reasons for Eskom’s pre-payment to TEGETA instead of Optimum Coal Mine (Pty) Ltd ("OCM"). Ms Ayanda Nteta gave the following reasons –

“TEGETA would be the controlling shareholding of OCM. pursuant to the transaction initiated by the business rescue practitioner with TEGETA to ensure OCM remains sustainable pursuant to its release from business rescue;

As part of the sale of shares agreement with OCH by the business rescue practitioner, OCH had to be substituted by TEGETA to the coal supply agreement between OCM and Eskom; and

TEGETA became the controlling shareholder of OCM on 1 September 2016, when the business rescue practitioner discharged OCM from business rescue.” Page 311 of the Public Protector’s report.

9.20. The Public Protector says that the responses given by Eskom appear to not make commercial sense as it appears that coal could have been sourced directly from OCM at a reduced rate.

9.21. OCM was under business rescue and the business rescue practitioners were not prepared to sell coal to Eskom at a reduced rate because they said that OCM went into business rescue precisely because the purchase price of coal paid by Eskom was low.

9.22. Eskom was not aware of the price at which OCM was selling coal to TEGETA and therefore, it could not negotiate for a lower price than it paid TEGETA.

9.23. The pre-payment of TEGETA was found to be in line with the policies of Eskom and it made “made commercial sense” by the Senior General Manager (Assurance and Forensics) at Eskom (see page 190 of the Public Protector’s report).

9.24. In conclusion, the Public protector did not make any finding in respect of the breach of fiduciary duty by the Eskom Board but speculated about the form of
transaction and price that the coal supply to Arnot was supposed to take. She did not receive expert evidence regarding what constitutes “commercial sense” in those circumstances.

9.25. Furthermore, the Public Protector speculates that the conduct of Eskom Board, in buying coal from TEGETA, was solely for the benefit of TEGETA. She bases her speculation on the analysis of payments made by Eskom to TEGETA in respect of coal supply. TEGETA was supplying coal to Eskom and Eskom was not entitled to tell TEGETA how to spend the money Eskom was paying to TEGETA.

10. THE PURCHASE OF OPTIMUM COAL HOLDING BY TEGETA FROM GLENCORE

10.1. TEGETA Exploration and Resources (Pty) Ltd ("TEGETA") purchased all the shares in the issued share capital of Optimum Coal Mine (Pty) Ltd ("OCM") and purchased claims against OCM from Optimum Coal Holdings (Pty) Ltd ("OCH") for an amount of 2 100 000 000.00 (Two point one billion rand). The Sale and Purchase Agreement for the sale of shares and claims ("SPA") was signed in December 2015.

10.2. The suspensive conditions were, amongst others, that –

10.2.1. Eskom must consent to the sale and purchase of shares by TEGETA;
10.2.2. release of the guarantees provided by OCH to Eskom;
10.2.3. TEGETA to issue a guarantee to Eskom in respect of its obligations in the Coal Supply Agreement ("CSA"); and
10.2.4. cession and assignment of rights in CSA to TEGETA.

10.3. Eskom was not involved in the negotiations of the terms of the SPA. The role which was played by Eskom was to secure its interest in the coal supply by OCM and to that extent the conditions precedent mentioned above, were inserted to protect Eskom’s interests.
10.4. Eskom's involvement in the sale of shares and claims by TEGETA from the BRP of OCM was limited to the approval of the cession and assignment of the coal supply agreement from OCH to TEGETA and this was confirmed by the Public Protector in page 251 of her report.

11. CONCLUSION

I hope the information provided herein will assist the Committee in its deliberations. The board will provide any further information that the Committee may require.

The Committee requested in paragraph 11 whether there are any reports prepared for the board and what steps had been taken. We had requested clarity with regard to this question in our letter of 16 November but we have not yet received such. We have made reference herein to some reports and would be happy to provide further information to the Committee.