

TERMS OF REFERENCE FOR THE NATIONAL ENERGY REGULATOR OF SOUTH AFRICA TO CONDUCT A MARKET INQUIRY INTO THE IMPACT OF FIXED CHARGES, GENERATION CAPACITY CHARGE AND OTHER CHARGES LEVIED BY ELECTRICITY DISTRIBUTORS

1. INTRODUCTION AND CONTEXT

- 1.1 The National Energy Regulator of South Africa (NERSA) intends to conduct a market-wide inquiry into the impact of electricity charges imposed by the licensees including private distributors, municipalities and Eskom Holdings SOC Ltd (Eskom). In particular, the market inquiry will focus on municipal fixed charges and the split of Eskom's generation charge into a generation capacity charge, a legacy charge and the variable energy charge. The inquiry will be conducted in terms of section 4(b)(ii) of the Electricity Regulation Act, 2006 (Act No. 4 of 2006) as amended (ERA), read with sections 2(b) and 4(a)(viii) of the ERA.
- 1.2 NERSA is initiating this inquiry on the basis that certain features of the electricity distribution segment of South Africa's electricity value chain may be hindering the attainment of key objectives set out in the ERA. These features may compromise the Act's objectives of safeguarding the interests of present and future electricity customers, ensuring efficiency and transparency in tariff-setting, promoting the financial sustainability of licensees, and supporting the broader socio-economic stability of the Republic. Accordingly, the objectives of this market inquiry include the following:
 1. **Ensuring Compliance:** Verify whether licensees are adhering to approved tariffs and regulatory requirements.
 2. **Protecting Consumers:** Safeguard consumers from unfair, excessive, or unauthorized charges.
 3. **Promoting Transparency:** Enhance clarity in pricing structures and communication to consumers.
 4. **Assessing Cost-Reflectivity:** Ensure that charges are based on actual costs and are justified.
 5. **Identifying Market Failures:** Detect and address any practices that distort competition or harm consumer interests.
 6. **Improving Regulatory Oversight:** Strengthen mechanisms to monitor and enforce compliance effectively.

Regulator Members:

Mr T Bukula (Chairperson) Ms Z Mpungose (Deputy Chairperson) *Adv NP Sithole (Chief Executive Officer)
*Ms N Maseti *Mr MW Mkhize Ms T Semane Mr FK Sibanda Ms PN Sibiya
*Full-Time Regulator Members

7. **Balancing Stakeholder Interests:** Achieve a fair balance between the needs of consumers, licensees, and the broader public.
 8. **Supporting Policy Goals:** Align pricing structures with broader economic, environmental, and social objectives, such as affordability and sustainability.
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- 1.3 NERSA has also noted disputes lodged by customers and other stakeholders concerning the structure, fairness, and justification of electricity charges. While it is incumbent on NERSA to address disputes referred to it, the similarities among the concerns raised regarding charges imposed by licensees have led NERSA to deem it necessary to initiate an inquiry within the scope of its powers. This intervention is intended to safeguard the integrity of the regulatory framework while addressing a significant source of consumer dissatisfaction and potential market distortions, and abuse of market power, within the electricity supply chain.
 - 1.4 NERSA's concerns arise in the context of the reconfiguration of the regulatory framework, designed to oversee and facilitate an evolving electricity industry. The transition towards cleaner variable energy sources and competitive market structures has introduced new tariff designs and unbundled charging mechanisms. While such changes may be necessary, they must be carefully managed to ensure that they meet the principles of fairness, transparency, and equitability. An imbalance in the unbundled tariff designs threatens affordability, reliable service delivery, and broader socio-economic resilience.
 - 1.5 When NERSA considered Eskom's proposal in the Retail Tariff Plan (RTP), the shock on low volume residential users was judged to be too extreme and NERSA reduced it to 20% of their proposal. This reduction was an overarching decision, and therefore, it changed the MegaFlex tariff components as well. In retrospect, it appears that the impact of this on MegaFlex customers has been different to that of residential customers.
 - 1.6 Therefore, it is important for NERSA to gauge the impact of these components on Eskom customers and how it has changed their costs and what impact it has on affordability and competitiveness.
 - 1.7 In the case of the municipalities, the court has ordered NERSA to approve their tariffs based on cost of COS studies and this brings with it additional pressure for municipalities to separate out the fixed costs. NERSA has taken note of the concerns regarding the application of the municipal tariffs and seeks to gauge the impact of these changes on customers.

2. LEGAL BASIS FOR THE INQUIRY

- 2.1 Section 3(1) of ERA as amended entrusts NERSA as the custodian and enforcer of the regulatory framework for the electricity industry. Such power is linked to the licensees in the spheres of generation, transmission, distribution and trading and to also enable the regulatory exercise to achieve the objectives of section 2.
- 2.2 ERA defines a *tariff* as “a charge to a customer or end user in respect of a licensed or registered activity, other than a surcharge, tax, levy or duty imposed by a municipality in terms of section 229 of the Constitution of the Republic of South Africa, 1996.” This definition clarifies the scope of NERSA’s authority: while the Regulator exercises oversight over tariffs relating to licensed or registered electricity activities, municipal surcharges, taxes, levies, or duties imposed under section 229 of the Constitution fall outside NERSA’s regulatory mandate.
- 2.3 The ERA establishes several regulatory tools linked to licensed activities. Licensing decisions, tariff approvals, and rules or methodologies carry immediate legal force, whereas inquiries, investigations, and information-gathering exercises are exploratory. Their findings acquire legal effect only once formally adopted and implemented through the appropriate regulatory processes.
- 2.4 Section 4(b)(ii), read with 4(b)(iii), of the ERA empowers NERSA to undertake regulatory interventions in respect of matters that, if left unattended, may undermine the achievement of the Act’s objectives. Because the mandate under these provisions is discretionary, the Energy Regulator must hold a reasonable apprehension that a material issue exists which warrants a formal response. In this instance, the submission has demonstrated widespread customer dissatisfaction regarding charges imposed by licensees, providing a clear basis for the exercise of these powers.
- 2.5 The inquiry proposed in this submission is distinct from the investigation contemplated in section 32 of the Electricity Regulation Act, which is directed at a specific licensee in respect of suspected contraventions. Instead, the proposed inquiry is a broader regulatory exercise aimed at examining the principles underpinning the formulation of the relevant charges, their impact on customers, and the extent to which these charges differ from, or align with, tariffs formally approved by NERSA.
- 2.6 There is no administrative action that will arise from conducting the inquiry and NERSA will be acting within its powers.

3. FEATURES OF THE MARKET

- 3.1 The electricity industry’s shifts toward decarbonisation, renewable energy, the ensuing liberalisation, prosumers and a wholesale market, necessitates a change in tariff structures. Among these adjustments is the requirement for accurate cost separation. In response to these changes, Eskom split the composite energy charge into three components. These three components were intended to add up to the previous single composite element.

- 3.2 The goal of this modification was to separate the fixed component of the generation costs and separate the additional expenses incurred by the legacy Renewable Energy Independent Power Producer Procurement (REIPPP) contracts from the costs of Eskom Generation. The two main catalysts for this change are Eskom Generation's need to compete in the wholesale market and effectively manage prosumers and other feed-in tariffs.
- 3.3 Any change in the tariff structure introduces risks regarding the equitable balancing of costs and the consequent effect on specific tariff components, as well as the allocation of costs to different customer categories. The relative impact of any change on the various tariff components may be reflected in the final bill to the end-user. This impact is relative to the discretionary income of an end-user, or to the ability to pass this change through to customers, as in the case of commercial goods and services retailers, where electricity costs represent a relatively small portion of the overall cost of sales.
- 3.4 In the past, both the fixed and variable components of energy costs were recovered through a combined variable energy charge, calculated based on the average customer usage within that tariff category. Thus, the average customer would correctly cover both the fixed and variable costs of the energy. Those who used more than average would contribute more to the fixed charge, while those who consumed less would contribute less and would be subsidised by those who used more. This approach, which has been successful in the past, is now facing challenges due to several factors that have come into play, rendering it inefficient.
- 3.5 Focusing on the residential segment, it is noted that the high price of electricity, energy efficiency drives, and the rise of rooftop solar photovoltaic (PV) installations are significant factors. The high price of electricity and the energy efficiency drives have contributed to a reduction in overall consumption or a shift to alternative energy sources. The advent of rooftop solar PV installations has seen above-average users (and generally more affluent ones) transition to below-average users. This transition resulted in above-average users becoming subsidised users since their lower energy consumption did not reduce the fixed costs of electricity supply. Consequently, the overall electricity price has had to be increased to compensate for this.
- 3.6 The result is that low-volume users, who previously were predominantly the less affluent, now have to pay proportionally more towards the fixed charges to the extent that they start to subsidise those who have installed solar PV.
- 3.7 This situation necessitated the separation (or unbundling) of the fixed charge from the variable portion of the energy charge. This unbundling of tariffs ensures that all users contribute to the fixed costs if they remain connected to the grid, which is a 'fixed' component of the bill. Variable costs are billed based on actual consumption, where varying consumption is the 'variable' component of the bill. This principle applies to both Eskom and municipal customers.

4. PURPOSE OF THE INQUIRY

- 4.1 The electricity sector is undergoing significant restructuring in pursuit of decarbonisation and competitive market development. These changes have introduced new unbundled tariff structures and fixed charges, which, if not implemented fairly and transparently, risk discriminating against certain customers while benefitting others, both in terms of Eskom pricing and that of municipalities.
- 4.2 Information asymmetry, compounded by the complexity of elasticity markets and pricing, is a perennial problem for regulators. Monitoring and investigation after the fact (*ex post* review) is a recognised approach to ensure that what regulated entities applied for translates into fair prices, especially when consumer dissatisfaction suggests this is not happening.
- 4.3 The purpose of this inquiry is to assess the implementation, fairness, and impact of the identified charges, as applied for in the respective tariff structures and applications, with specific reference to the following:
 - 4.3.1 Whether the changes have been effectively managed.
 - 4.3.2 The extent and adequacy of communication with customers.
 - 4.3.3 Whether any tariffs implemented are unlawful or unauthorised.
 - 4.3.4 The impact of these charges on different customer categories.
 - 4.3.5 Whether the charges are reasonable, cost-reflective and justified.
- 4.4 The inquiry will provide NERSA with a clearer understanding of consumer concerns, market sentiment, and the drivers behind current challenges, as well as greater insight into the market structure and how this structurally impacts price outcomes and ensure that consumer interests are not only met but safeguarded against abuse. This will enable evidence-based decisions and identification of areas requiring further regulatory action.

5. SCOPE OF THE INQUIRY

- 5.1 The scope of the inquiry is intentionally focused to ensure depth and relevance. At this juncture, NERSA seeks to prioritise areas of great concern to consumers and stakeholders while avoiding dilution of the process.
- 5.2 Accordingly, the inquiry will be limited to municipal fixed charges and the split of Eskom's generation charge into a generation capacity charge, a legacy charge and the variable energy charge.
- 5.3 Other tariff components and related market developments, while important, fall outside the primary scope of this inquiry. However, they can be included in the response and may be considered should they provide evidence that complements the primary scope of this inquiry.

- 5.4 Although the inquiry is not targeted at investigating any particular licensee, nor does it intend to make allegations against any licensee, Eskom will be included in the inquiry due to the imposition of significant fixed charges following the approval of its Retail Tariff Restructuring Plan in March 2025. Customer concerns have already been received regarding the implementation of these charges, including the generation capacity charge.

6. METHODOLOGY

The inquiry will adopt a structured, evidence-based approach to collect, analyse, and verify information relevant to municipal fixed charges and the unbundling of Eskom's generation tariff. The process will include the following components:

6.1 Documentary and Data Requests

- 6.1.1 Issue formal written notices to all relevant licensees (Eskom, municipalities and other distribution licensees) requesting detailed tariff schedules, supporting calculations and any relevant documentation.
- 6.1.2 Obtain from Eskom its detailed methodology and datasets behind the generation capacity, legacy charge and variable energy charges.
- 6.1.3 Request historical and current fixed-charge data, including methodologies for escalation or review.
- 6.1.4 Issue targeted requests only where additional data, clarifications, or updates are needed, such as in relation to recent adjustments and reconciliations to financial statements.
- 6.1.5 Require all licensees to confirm the accuracy and completeness of any new or supplementary information provided, in accordance with section 35B(d) of the ERA.

6.2 Document Analysis

- 6.2.1 Review distribution licensees' approved tariff schedules, COS studies, supporting calculations, financial statements, and regulatory submissions.

6.3 Stakeholder Engagement

- 6.3.1 Invite written submissions from customers, industry bodies, labour organisations and civil society groups on the impact of fixed charges and the Eskom tariff split.
- 6.3.2 Hold public hearings or workshops, where appropriate, to clarify evidence and obtain qualitative insights.

6.4 Comparative Analysis

- 6.4.1 Benchmark fixed charge structures and unbundled generation charges against those applied by other provinces or utilities.
- 6.4.2 Analyse trends in the ratio of fixed to variable charges, affordability metrics, and recovery of network costs.

6.5 Data Verification and Auditing

- 6.5.1 Cross-check information received from licensees against audited financial statements, regulatory returns, and approved tariff determinations.
- 6.5.2 Where discrepancies arise, request clarifications or conduct on-site verifications if required.

6.6 Quantitative and Qualitative Assessment

- 6.6.1 Use tariff-modelling and statistical tools to assess revenue adequacy, cost-reflectivity, and affordability impacts.
- 6.6.2 Consider socio-economic data, including income levels, inflation and unemployment rates, to evaluate the public-interest implications.

6.7 Compliance Verification

- 6.7.1 The inquiry will determine whether any licensees are applying charges, escalation mechanisms, or tariff adjustments that fall outside of NERSA's approval process.
- 6.7.2 Where evidence of non-compliance is identified, the inquiry team will:
 - i. document and quantify the extent of the unauthorised charges or adjustments;
 - ii. present preliminary findings to the affected licensee for comment and rectification, where appropriate; and
 - iii. include confirmed instances of non-compliance in the Draft Market Inquiry Report, with recommendations for corrective action.
- 6.7.3 Confirmed non-compliance will be escalated to the Energy Regulator for consideration of remedial measures, which may include:
 - i. issuing formal directives to cease or adjust the offending practice and application of claw-backs for affected customers where necessary;
 - ii. imposing administrative penalties in accordance with the ERA;
 - iii. publishing compliance findings where warranted to enhance transparency; and

- iv. referring persistent or material breaches to the appropriate enforcement structures, including possible licence suspension or revocation, subject to due process.

6.8 Data Synthesis and Reporting

- 6.8.1 Integrate findings from all streams into draft and final reports, clearly indicating evidence sources, analysis, and recommendations.
- 6.8.2 Ensure that confidential information is handled in compliance with NERSA's information-management protocols.
- 6.8.3 Once the draft report has been prepared, it will be released for stakeholder review and comment as part of the report-finalisation process.
- 6.8.4 After considering all stakeholder inputs, the final report will be submitted to the Energy Regulator for approval and, once approved, will be published on the NERSA website.

7. THE INQUIRY PROCESS

- 7.1 NERSA hereby invites all affected stakeholders including licensees, industry associations, consumers, and other interested or affected parties, to submit information, evidence, or experiences relating to municipal fixed charges and Eskom's restructured generation charges.
- 7.2 The specific responses sought are detailed in **Appendix 1**.
- 7.3 The inquiry will be undertaken in three structured phases, guided by the following indicative timelines:

Table 1: Indicative Timelines

| INDICATIVE TIMELINES | |
|---|-------------------|
| INQUIRY ACTIVITY | DATE |
| Phase 1: Commencement of the inquiry | |
| Publication of notice and call for written submissions | 25 September 2025 |
| Closing date for written stakeholder representations and submission of relevant information | 25 October 2025 |
| Public hearings | November 2025 |
| Phase 2: Draft Market Inquiry Report | |
| Publication of the draft report and invitation for comments | 12 December 2025 |
| Closing date for written stakeholder comments on the draft report | 12 January 2026 |
| Public hearings | January 2026 |
| Phase 3: Finalisation of the Market Inquiry Report | |
| Recommendation of the final Market Inquiry Report by the Electricity Subcommittee to the Energy Regulator | February 2026 |
| Approval of the final Market Inquiry Report and its publication by the Energy Regulator | February 2026 |
| Publication of the Final Report on the NERSA website | March 2026 |

8. EXPECTED OUTCOMES

The inquiry is expected to result in the following:

- 8.1 A clear, evidence-based understanding of fixed charge structures across the electricity distribution sector.
- 8.2 Identification of any non-compliance with approved tariffs or regulatory requirements.
- 8.3 Recommendations to ensure that fixed charges are lawful, cost-reflective and transparent.
- 8.4 Proposals for improving regulatory oversight and enforcement.
- 8.5 Where warranted, initiation of enforcement action against non-compliant licensees, which may include public disclosure of findings and, in severe cases, recommendations for licence revocation subject to tribunal processes.

9. CONCLUSION

- 9.1 NERSA invites stakeholders to submit written representations and supporting information on the matters outlined in this Terms of Reference document within 30 calendar days from the date of publication to:
electricity.marketinquiry@nersa.org.za
- 9.2 Submissions should also indicate whether stakeholders wish to make oral representations, should the Regulator elect to convene public hearings.

APPENDIX 1: QUESTIONNAIRE AND INFORMATION REQUEST

Guidance for Respondents

- Where possible, provide information in both quantitative form (tables) and brief narrative responses (≤150 words per question).
- Customers on prepaid meters who do not receive monthly bills should submit clear images of purchase receipts, together with meter readings before and after each purchase.
- Please ensure that all data submitted covers corresponding billing periods for the 2024/25 and 2025/26 financial years, unless otherwise specified and historical information is requested.

A) Customer Information and Consumption Data

A1: Responses sought from Eskom Residential Customers

- 1) Tariff name and supply address.
- 2) Average monthly consumption (kWh) and total bill for 2024/25. Please provide a copy.
- 3) Average monthly consumption (kWh) and total bill for 2025/26. Please provide a copy.
- 4) Consumption and bill in 2 and 3 above should be for the corresponding billing periods.
- 5) Do you have a solar PV or other embedded generation system? If yes, state the installation date.
- 6) Briefly describe (≤150 words) how changes in fixed charges have affected your costs or energy use.
- 7) Mention any other tariff issues you would like to raise.
- 8) Were the changes to charges communicated to you in advance by your supplier? If yes, how (e.g. letter, email, SMS, etc.)?

A2: Responses sought from Municipal Residential Customers

- 1) Tariff name and supply address.
- 2) Average monthly consumption (kWh) and total bill for 2024/25. Please provide a copy.
- 3) Average monthly consumption (kWh) and total bill for 2025/26. Please provide a copy.
- 4) Consumption and bill in 2 and 3 above should be for the corresponding billing periods.
- 5) Do you have a solar PV or other embedded generation system? If yes, state the installation date.
- 6) Briefly describe (≤150 words) how changes in fixed charges have affected your costs or energy use.
- 7) Mention any other tariff issues you would like to raise.
- 8) Were the changes to charges communicated to you in advance by your supplier? If yes, how (e.g. letter, email, SMS, etc.)?

A3: Responses sought from Eskom MegaFlex and Large Power Users

- 1) Location, tariff name, voltage level of supply and Notified Maximum Demand (NMD).
- 2) Average monthly consumption and bill for 2024/25. Please provide a copy.
- 3) Average monthly consumption and bill for 2025/26. Please provide a copy.
- 4) Consumption and bill in 2 and 3 above should be for corresponding billing periods.
- 5) Describe (≤ 150 words) how the splitting of the Time-of-Use (ToU) energy tariff into the three components has affected you with reference to the Generation Capacity Charge and the revised ToU charges.
- 6) Raise any other tariff concerns you may have.
- 7) Were these changes communicated to you ahead of time by your supplier? If yes, indicate how.

A4: Responses sought from Non-residential Municipal Customers

- 1) Municipality, tariff name, voltage level of supply and NMD.
- 2) Average monthly consumption and bill for 2024/25. Please provide a copy.
- 3) Average monthly consumption and bill for 2025/26. Please provide a copy.
- 4) Consumption and bill in 2 and 3 above should be for the corresponding billing periods.
- 5) Briefly explain (≤ 150 words) how tariff structure changes have affected your operations.
- 6) Provide any other tariff concerns you may have.
- 7) Were the changes communicated to you ahead of time by your supplier?

B) Specific Tariff Themes: Fixed Charges, Generation Capacity Charge (GCC)

For each of the charges (fixed charges, GCC), please respond to the following, as applicable:

B1: Responses sought from affected consumers

- 1) Describe any challenges or impacts experienced from the implementation of fixed charges and/or GCC.
- 2) Demonstrate and quantify the impact of the fixed charge and/or GCC on your electricity bill or business costs. Provide data where applicable.
- 3) Provide evidence showing the relationship between fixed and/or GCC costs and your overall electricity charges (before and after implementation).
- 4) How would you advise NERSA to ameliorate the impact of fixed charges and/or GCC while balancing the interests of all stakeholders?

B2: Responses sought from distributors

- 1) Explain how you determined and applied fixed charges and/or GCC, providing supporting documentation on cost components.
- 2) What impact did you assess and observed in the billing costs since the implementation of fixed charges and/or GCC?
- 3) What is the portion of the fixed charges and/or GCC relative to the total tariff (network, energy, non-network components)?

- 4) Explain the methodology used to calculate the proportion of fixed charges and/or GCC and demonstrate its accuracy. Provide data where applicable.
- 5) Justify the rationale for recovering associated costs via fixed charges and/or GCC, including evidence from COS studies or other analyses.
- 6) What communication strategy was used to inform customers about these changes? Describe and provide evidence.

C) Information for Electricity Distributors (Eskom, Municipalities and Other Distribution Licensees)

This section is intended for Eskom, municipalities, and other electricity distribution licensees. NERSA seeks comprehensive tariff and cost-related information, covering historical and current periods, to assess the basis, justification, and implementation of fixed charges and the Generation Capacity Charge (GCC).

- 1) Provide complete tariff schedules for the 2024/25 and 2025/26 financial years, together with supporting calculations used to determine fixed charges, GCC, legacy charge, and variable energy charge.
- 2) Submit your detailed methodology and datasets used to derive the GCC, legacy charge and energy charge. Include cost drivers, allocation rules, and any assumptions applied.
- 3) Supply historical data on fixed charges for at least the previous three tariff years (or longer if readily available), indicating how these were reviewed or escalated (e.g. CPI, cost-of-service adjustments).
For the GCC provide all information available since its introduction, including the initial cost build-up, the consultation process, if any, and any planned approach to escalation or review.
- 4) Explain any escalation mechanisms or formulae applied to fixed charges. Provide examples of how they were implemented in practice.
For the GCC, describe any methodology or principles proposed or adopted for future adjustments (even if none have been applied yet). Where no escalation mechanism has been defined, explain how the charge is expected to evolve.
- 5) Where applicable, attach reconciliations between tariff revenues and corresponding financial statement items, highlighting recent adjustments or true-ups.
- 6) Describe internal governance processes for developing, approving, and implementing fixed charges and GCC (e.g. board submissions/resolutions, municipal council resolutions).

Submission Details

- All responses should be sent to electricity.marketinginquiry@nersa.org.za
- Please include supporting evidence (bills, receipts, calculations, or cost analyses with your responses).
- Stakeholders requiring assistance with completing the questionnaire may contact NERSA at electricity.marketinginquiry@nersa.org.za

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