TRANSACTION ADVICE AND DEVELOPMENT OF ENERGY PERFORMANCE CONTRACT PROCUREMENT DOCUMENTS FOR PUBLIC SECTOR ENERGY EFFICIENCY (“Project”)

REGULATORY FRAMEWORK REVIEW

Prepared for Deutsche Gesellschaft für Internationale Zusammenarbeit by Pinsent Masons Africa LLP

Pinsent Masons

TABLE OF CONTENTS

GLOSSARY

Constitution	The Constitution of the Republic of South Africa, Act 108 of1996
DFI	Development Finance Institution
DMRE	Department of Mineral Resources and Energy
DORA	Division of Revenue Act 9 of 2021
EEDSM Grant	Energy Efficiency Demand Side Management Grant
EEPBIP	Energy Efficiency in Public Buildings Infrastructure Programme
EME	An exempted micro enterprise in terms of a code of good practice on black economic empowerment issued in terms of section 9(1) of the Broad-Based Black Economic Empowerment Act
EnPC	Energy Performance Contract
ERA	Electricity Regulation Act 4 of 2006.
ESCO	Energy Services Company
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
MFMA	Local Government: Municipal Finance Management Act 53 of 2003
MSA	Municipal Systems Act 32 of 2000
Municipal Guidelines	Municipal Service Delivery and PPP Guidelines, 2015 issued by National Treasury
Municipal PPP Regulations	Municipal Public-private Partnerships Regulations,
Municipal SCM Regulations	Municipal Supply Chain Management Regulations, 2005
NERSA	National Energy Regulator of South Africa
PFMA	Public Finance Management Act 1 of 1999
PPPFA	Preferential Procurement Policy Framework Act 5 of 2000
PPPFA Regulations	Preferential Procurement Regulations, 2017
QSE	A qualifying small business enterprise in terms of a code of good practice on black economic empowerment issued in terms of section 9(1) of the Broad-Based Black Economic Empowerment Act
SCM Instruction	SCM Instruction No. 02 of 2021/22

TR16	Treasury Regulation 16 (Public-private Partnerships) of the Treasury Regulations to the PFMA
TR16A	Regulation 16A (Supply Chain Management) of the Treasury Regulations to the PFMA

1. INTRODUCTION

1.1 Background and scope of legal inquiry

1.1.1 The Department of Mineral Resources and Energy is the programme manager for EEPBIP, and has been assisted by GIZ in developing various elements required to roll out the EEPBIP across government.

1.1.2 The EEPBIP seeks to achieve greater savings in electricity spend by public institutions or organs of state through the introduction of energy efficiency measures.[1] Initially this was predominantly focused on energy efficiency in government-owned buildings, however it is clear that there are a number of government services, especially at a local government level that could also benefit from the introduction of energy efficiency measures to introduce savings.

1.1.3 The need for the EEPBIP is all the greater given the precarious state of South Africa's energy supply, which will take some years to correct.[2]

1.1.4 Until recently the EEPBIP has been funded primarily through the EEDSM Grant.[3] The grant is open to all government entities and departments, which need to make an application for accessing the grant, a process overseen and administered by DMRE. If granted, the EEDSM allocation has historically been used by institutions to fund energy audits as well as the cost of procuring an ESCO to purchase EE equipment, install the EE equipment and in some instances maintain such EE equipment for a period of time.

1.1.5 The DMRE together with the assistance of the GIZ seek to optimise the use of the EEDSM grant by fundamentally changing the funding model so that instead of the EEDSM being used to fund EE equipment, rather for ESCOs to fund the EE equipment on the basis of an EnPC, be it on a shared savings or guaranteed savings basis. This allows for better leveraging of the available funding in the EEDSM grant, which can assist with the development of a greater number of projects across more institutions whilst transferring the obligations and risks of financing EE interventions to the private sector.

1.1.6 Simply put, the roll out and scalability of the EEPBIP relies on the following funding and contractual model:-

(a) For ESCOs to fund EE equipment being procured by public entities. ESCOs will be required to approach lending institutions and to raise capital to finance EE equipment.

(b) While some ESCO's have balance sheets to secure such lending, for a number of the smaller ESCOs that qualify as SMMEs, they are unable to provide the necessary security. To this end GIZ has assisted in establishing a Partial Credit Guarantee Fund which will

---

[1] Due to capacity and resource constraints, limited awareness of opportunities, lack of comprehensive and accurate data on energy use, and access to finance; potential financial and energy savings, as well as emission reductions, that could be achieved through demand-side EE interventions lack implementation.

[2] South Africa's Greenhous Gas emissions are high due to, amongst other things, a reliance on coal-based power stations and inefficient use of energy. The EEPBIP's objective is to reduce Greenhouse Gas emissions through EE transformation in the public sector.

[3] Section 8 of DORA refers to conditional allocations to municipalities. Various conditional allocations are set out in Schedule 5 Part B of DORA in respect of the 2021/22 financial year. Schedule 5 Part B includes the EEDSM grant and states the purpose of the EEDSM grant as "*to provide subsidies to municipalities to implement energy efficiency and demand side management initiatives within municipal infrastructure in order to reduce electricity consumption and improve energy*". The 2021/22 allocation is at R220 874 000. The forward estimate for 2022/23 is at R231 204 000, and 2023/24 is at R232 092 000.

issue a partial credit guarantee to secure bank loans to purchase EE equipment.[4]

(c) The envisaged payment mechanism under this funding model is a so-called energy performance contract.[5] Very simply, the structure of the EnPC is for the notional saving made by the public institution through the introduction of EE measures, that is the savings on their electricity account compared to their electricity costs prior to the introduction of EE measures, to be used to pay the ESCO which will in turn service any debt incurred by the ESCO to fund the EE equipment and also pay them a fee for the maintenance of such EE equipment. Guaranteed savings EnPC work in a similar but slightly different way.

(d) This mechanism is especially attractive to public institutions that provide services with very stretched capital projects budgets and that seldom have funding available for such EE measures apart from when funded through a grant, or in this instance through private sector funding.

(e) Going forward it is envisaged that the EEDSM grant will be used predominantly to fund technical advisory costs needed to prepare projects before going out on procurement, such as conducting energy audits.[6]

1.1.7 Given the new funding and contracting model for the EEBPIP, it is critical to any programme to determine whether the regulatory environment supports such model, in particular whether our procurement laws allow the EEBPIP to be rolled out and scaled in the above manner. The purpose of this opinion is to interrogate a number of specific procurement-related inquiries as they impact on the EEPBIP.

1.1.8 We have specifically addressed the following regulatory issues:-

(a) Given the envisaged EEPBIP funding and contracting model (as described above) how an EnPC is classified under procurement legislation:-

(i) Is an EnPC regarded as the procurement of a good or a service?

(ii) If an EnPC is externally funded i.e. by the ESCO through debt, is this regarded as a PPP?

(iii) If an EnPC is procured by local government are there additional considerations to bear in mind such as whether

[4] The EEPBIP seeks to achieve its objective of EE transformation in the public sector by implementing appropriate technical and financial support, as well as a programmatic approach to identifying, developing, financing and implementing EE interventions in a consistent manner.

[5] EnPCs have been utilised by ESCO's internationally, as well as in South Africa. However, the use of EnPC in South Africa has been limited and restricted. The EEPBIP has identified a need for an up-to-date analysis of best practice and experience on EnPC, locally and internationally; with the aim being able to attract private investment through ESCOs and financial institutions, as well as to respond to the needs of public sector property managers.

[6] The EEPBIP aims to build on existing public sector programmes such as the EEDSM grant, and the approach taken is that the latent EE investment potential of the public sector can support rapid and sustainable growth of the local ESCO market, as well as stimulate EE implementation.

the EnPC amounts to a "municipal service" for purposes of the application of the MSA?

(b) An overview of the procurement process applicable to EnPC at a national, provincial and local government level, including:-

(i) The bid evaluation and scoring system as envisaged in the PPPFA and PPPFA Regulations – and in particular pre-qualification criteria, functionality requirements, price and BBBEE scoring; and

(ii) The role of local content and designated sectors applicable to EE measures.

(c) Any additional consents and approvals needed to procure an EnPC, including:-

(i) Whether an ESCO is required to be licensed under the ERA if the EE measures constitutes SSEG;

(ii) Whether the payment provisions under an EnPC amount to a "future financial commitment" for purposes of the application of section 66 of the PFMA or have a future budgetary effect in terms of section 33 of the MFMA; and

(iii) The applicable regime under the MFMA and the PFMA where a payment guarantee is requested by a lender from a public institution, or where a lender requires that electricity revenues collected by municipalities be ring-fenced from the municipality's ordinary revenue account.

2. PROCUREMENT AND SUPPLY CHAIN MANAGEMENT INQUIRIES

2.1 Overview of procurement framework

2.1.1 The regulation of procurement under South African law is broadly derived from the requirements of the Constitution. Section 217(1) of the Constitution requires that where an organ of state is contracting for goods and services, it must do so in accordance with a system that is fair, equitable, competitive, transparent, competitive and cost-effective.

2.1.2 This requirement is given effect in different pieces of legislation governing different spheres of government (whereby organs of state are required to maintain and adhere to a procurement policy that meets the Constitutional demands of being fair, equitable, transparent, competitive and cost-effective when contracting for goods or services.[7]

2.1.3 At the national and provincial level, procurement is primarily regulated by (i) the PFMA and (ii) the Treasury Regulations to the PFMA, in particular Treasury Regulation 16A TR16A applies to all government departments, constitutional institutions and public entities listed in Schedules 3A and 3C of the PFMA (being national and provincial public entities). It does not, therefore,

[7] Sections 38(1)(a)(iii) and 51(1)(a)(iii) of the PFMA require that the accounting officers of departments and constitutional institutions and accounting authorities (usually the board of directors) of public entities respectively must maintain a supply chain management system which meets these requirements. At the municipal level,

apply to major public entities and national/provincial government business enterprises.

2.1.4 TR16A specifically requires that these institutions must develop and implement an effective and efficient supply chain management system for, among other things, the "acquisition of goods and services".[8] It also imposes certain requirements for the procurement of goods in terms of the process which must be followed (being quotations or a bidding process). Further details on competitive bidding are set out at paragraph **Error! Reference source not found.** below.

2.1.5 For major public entities and national/provincial government business enterprises, although TR16A does not apply, the general requirement of the PFMA itself to maintain a procurement and provisioning system which is fair, equitable, transparent, competitive and cost-effective still applies. Accordingly, although such public entities have more freedom when contracting for goods or services, this will still have to be in compliance with the entity's relevant supply chain management policies and procedures.

2.1.6 Overall, at the national and provincial level, the framework does not draw any distinction between procurement of goods versus services – the process is the same whether what is being procured is good or services or both goods and services, as is the case with an EnPC. Accordingly, the classification of energy efficiency interventions under an EnPC will not impact the processes to be followed under conventional procurement.

2.1.7 At municipal level, municipalities are required to comply with a number of statutes. Chapter 11 of the MFMA (Goods and Services) is the key statutory basis. To give effect to Chapter 11 of the MFMA municipalities must, per section 111, have and implement a supply chain management policy in compliance with the Municipal SCM Regulations.[9]

2.1.8 Apart from the MFMA, procurement of municipal services is also regulated under the MSA as read with the Municipal PPP Regulations. The MFMA delineates its applicability and that of the MSA in section 110(1) wherein it states that Chapter 11 applies in the following circumstances:-

(a) when procuring goods or services or for disposal of goods;[10]

(b) when selecting contractors to provide assistance in the provision of municipal services "*otherwise than in circumstances*" where the provisions of Chapter 8 of the MSA dealing with municipal services apply;[11] and

(c) when carrying out a competitive procurement process to appoint a so-called "external mechanism" to provide a municipal service under section 83 of the MSA;.[12]

2.1.9 Each of these scenarios and whether they apply to the procurement of ESCOs is addressed in the paragraphs that follow.

[8] Regulation 16A3.1(a).
[9] The Municipal Supply Chain Management Regulations, GN 86 of 30 May 2005.
[10] Section 110(1)(a) and (b).
[11] Section 110(1)(c).
[12] Section 110(1)(d).

2.2 **When energy efficiency measures are procured in terms of an EnPC, how is this categorised under procurement law?**

2.2.1 The first issue which we consider is the treatment of the procurement of ESCOS under a EnPC from a procurement perspective, and in particular whether it constitutes contracting for goods or contracting for services or both.

2.2.2 Considering the terms of an EnPC, they include both a contract for goods and a contract for services. For example, under a shared savings model where the ESCO purchases EE equipment which is transferred to the institution at the end of the contract term, this entails the supply of goods. On the other hand, it is also clear that an EnPC regulates the provision of a number of services ranging from installation to (potentially) design, commissioning, operations, maintenance and monitoring and verification.

2.2.3 At its most basic an EnPC is a contract for both goods and services from a procurement perspective, however unlike ordinary contracts for goods and services, under an EnPC there is substantially financial, technical and operational risk transferred to the ESCO. This is what is known as a performance-based contract which links the service provider or ESCO's payment terms to the operational and financial performance benefits realised by the institution. Whereas most service contracts will set out performance requirements or service levels (with potential penalties for poor performance) and most contracts for goods will contain warranties underlying or supporting the product or good provided, the output risk is still retained by the institution. By contrast, the ESCO under an EnPC assumes full risk in respect of the contractual output.

2.3 **If an EnPC is externally funded i.e. by the ESCO through debt, is this regarded as a PPP?**

2.3.1 Although the actual procurement process followed under a PPP is the same as for conventional procurement, PPPs at both the national/provincial as well as municipal level have more onerous approval requirements prior to and after procuring such an arrangement (in particular at feasibility stage and then again at contracting stage).

2.3.2 For institutions in the national and provincial sphere of government, PPPs are governed by TR16. This applies to any projects which fall within the definition of a PPP under TR16 and which have been identified for implementation as a PPP.[13]

2.3.3 TR16 defines two types of PPP's, these being; (i) where the private party performs an institutional function and (ii) where the private party acquires the use of state property for its own commercial purposes. It is also a requirement that the private party assumes substantial financial, technical and operational risk and receives a benefit in the form of funds from the institution and/or user charges or fees.[14]

2.3.4 TR16 also defines an "institutional function" as either (i) a service, task assignment or other function that an institution is entitled or obliged to perform in the public interest or on behalf of the public service generally; or (ii) any part or component of or any service, task, assignment or other function performed

[13] Treasury Regulation 16.3.1.
[14] Limbs (a) and (b) of the definition of public-private partnership in TR16.1.

or to be performed in support of such a service, task, assignment or other function.

2.3.5 In order for TR16 to apply to a particular contractual arrangement, all the requirements as set out above need to be met, and if only one of the requirements is not met, conventional procurement applies.

2.3.6 All PPPs need to be approved by the relevant treasury, at different stages of the PPP lifecycle, being at the end of the feasibility study,[15] when the procurement documents are prepared[16], for the selection of preferred bidder[17] and finally once the PPP agreement is finalised.[18]

2.3.7 PPPs procured at local government level are regulated by section 120 of the MFMA and the Municipal PPP Regulations were issued in order to expand on the requirements of section 120 , which permits municipalities to enter into public-private partnerships provided they represent value for money, affordability and appropriate risk transfer to be established for a PPP (through a feasibility study).

2.3.8 A PPP in the Municipal PPP Regulations is defined as a commercial transaction between a municipality and a private party in terms of which the private party:-

(a) performs a municipal function for or on behalf of a municipality, or acquires the management or use of municipal property for its own commercial purposes, or both performs a municipal function for or on behalf of a municipality and acquires the management or use of municipal property for its own commercial purposes. A "municipal function" is defined as a municipal service or any other activity within the legal competence of a municipality; In respect of the second part of the definition, which is an "activity within the legal competence of a municipality", the courts have viewed this as being something falling within the functional areas assigned to municipalities under the Constitution.[19]

(b) assumes substantial financial, technical and operational risks in connection with the performance of the municipal function, the management or use of the municipal property, or both; and

(c) receives a benefit from performing the municipal function or from utilising the municipal property or from both, by way of consideration to be paid or given by the municipality or a municipal entity under the sole or shared control of the municipality, charges or fees to be collected by the private party from users or customers of a service provided to them, or a combination.

2.3.9 We don't believe that the procurement if an ESCO in terms of an EnPC would constitute a PPP under the PFMA for the following reasons:-

(a) With regards to the requirement of the private party (ESCO) assuming substantial financial, technical and operational risk, depending on how prescriptive the EE interventions are under the procurement document, this requirement may be met. If an

[15] Regulation 16.4.2, termed Treasury Approval I.
[16] Regulation 16.5.1, termed Treasury Approval IIA.
[17] Regulation 16.5.4, termed Treasury Approval IIB.
[18] Regulation 16.6.1, termed Treasury Approval III.
[19] *Altech Radio Holdings (Pty) Ltd and Others v City of Tshwane Metropolitan Municipality* [2020] ZASCA 122 at [63].

institution allows the ESCO to determine the technology and nature of the EE interventions being made, and procures the ESCO purely on a performance output basis (which is generally assumed in a EnPC), then it would be correct to conclude that under an EnPC arrangement, substantial technical operational and financial risk is transferred to the private party ESCO. However, in under a guaranteed saving contract, this requirement may not be met as the institution itself funds the EE interventions, and therefore substantial financial risk transfer will not be present.

(b) In connection with the requirement that the private party (ESCO) receives a benefit in the form of funds from the institution and/or user charges or fees, again a key term of an EnPC is that the institution reimburses the ESCO for its EE interventions through the saving generated by such interventions. This is still public expenditure, but directly not to settling a large electricity account, but partly to making payments to an ESCO. Accordingly, this requirement of a PPP is also met.

(c) In respect of the last requirement, namely whether the scope under an EnPC amounts to an institutional function, it is necessary to review this definition in TR16. An "institutional function" means "a service, task, assignment or other function that an institution is entitled or obliged to perform in the public interest or on behalf of the public service generally. It can also refer to any part or component of or any service, task assignment or other function performed or to be performed in support of such a service, task, assignment or other function.

(d) We don't believe that a EnPC in terms of which an ESCO supplies, finances, installs and maintains EE equipment meets the test of an "Institutional function" or a part or a component of such a function. The benefit of an EnPC is not the rendering of a public service, task or assignment to the public at large. Rather, the benefit is to the institution by reducing its energy consumption and therefore its electricity expenditure and presumably to re-direct those funds to delivering on its mandate. In other words, an EnPC is not a contract for the performance of an institutional function, even though it may indirectly benefit an institution's ability (through the savings its generates) to deliver on its functions.

(e) Based on the above analysis, our view is that the procurement of an ESCO under an EnPC does not meet the requirements of a PPP as defined in TR16 and therefore TR 16 will not apply to any such procurement.

2.3.10 At a municipal government level, similarly, our view is that the arrangement regulated under an EnPC does not amount to a municipal PPP for the following reasons:

(a) As set out more fully below, our view is that the service being provided under an EnPC does not meet the test of a municipal service (as defined in the MSA). We also do not believe that the activities regulated under a EnPC can be classified as "an activity within the legal competence of a municipality". In short, an EnPC is not intended to introduce new services or tasks or take over those services and tasks for which a municipality is ordinarily responsible in terms of the Constitution and applicable law. Rather, it is a contractual mechanism to help a municipality reduce its carbon footprint and introduce savings into its expenditure, and therefore the focus is not on service provision but rather on more efficient expenditure through reduced electricity consumption.

(b) As with PPPs at national and provincial government level, we believe that the other requirements for a municipal PPP, namely that the ESCO under an EnPC assumes substantial financial, technical and operational risks may be met (in particular under a shared savings contract), but for the reasons as set out above, such risk is not assumed "in connection with the performance of the municipal function". Moreover, the requirement that an ESCO receives a benefit is achieved, however the benefit derived form the ESCO is not "from performing the municipal function" as is the requirement in the definition of PPP in the Municipal PPP Regulations.

2.4 **If an EnPC is procured by a municipality are there additional considerations to bear in mind such as whether the EnPC amounts to a "municipal service" for purposes of the application of the MSA?**

2.4.1 The MSA places considerable emphasis on the delivery of "municipal services" by municipalities. Chapter 8 of the MSA sets out certain processes which must be followed by a municipality when selecting a new method of delivery for municipal services. Accordingly, to the extent that an EnPC amounts to the provision of a "municipal service" as defined, then these MSA requirements will be

2.4.2 The MSA defines a municipal service as a service that a municipality, in terms of its powers and functions, provides or may provide to or for the benefit of the local community irrespective of whether (i) such a service is provided, or to be provided, by the municipality through an internal mechanism contemplated in section 76 or by engaging an external mechanism contemplated in section 76, or (ii) fees, charges or tariffs are levied in respect of such a service or not.[20]

2.4.3 Unpacking this definition, we find that a municipal service must be a service which falls within a municipalities powers and functions and which benefits the local community regardless of how it is delivered (internally within the municipality or through a so-called external mechanism) and whether charges are levied to the community for such service.

2.4.4 A municipality's powers and functions are regulated in terms of section 156 of the Constitution which confers on municipalities the executive authority and right to administer (and legislate on) the matters indicated in the functional areas of legislative competence as set out in Part B of Schedule 4 (and Part B of Schedule 5 of the Constitution. Looking through the areas of functional competence, it is clear that the provision of energy efficiency measures are nowhere to be found. The reason for this is that energy efficiency is not a power or function per se. The introduction of energy efficiency is to meet policy goals of the Government and to meet the constitutional imperative of promoting effective financial management[21] by introducing savings to its expenditure.

2.4.5 With respect of the second requirement of the definition that the service must benefit the local community, while a reduced carbon footprint and savings to the municipal budget undoubtedly have an indirect benefit to the community,

---

[21] Section 215(1) of the Constitution.

our view is that the definition presupposes a direct benefit flowing to communities form the provision of a specific service. That is not the case with energy efficiency.

2.4.6 In the light of the above analysis, our view is that to the extent that a service is provided under an EnPC, this does not meet the requirements of a municipal service and that the provisions of the MSA will not apply to the procurement of an ESCO under an EnPC.

2.4.7 We note that, although not defined in the MSA itself, the National Treasury in the Municipal Service Delivery and PPP Guidelines distinguishes between a municipal service, and a "municipal support activity", which is the term given in the Municipal Guidelines for the powers conferred under section 8(2) of the MSA to "*do anything reasonably necessary for, or incidental to, the effective performance of its functions and the exercise of its powers*". The Municipal Guidelines further clarify that where a project involves a municipal support activity but not a municipal service, then the MSA is not applied.

2.4.8 The question is whether the services provided under an EnPC can be viewed as a "municipal support activity". To do so, it would need to be demonstrated that the EE interventions are required or needed in order to support a municipal service or function. It is not our understanding that this is what the EEPBIP aims to achieve. A key objective of the programme is to reduce public institutions' reliance on electricity drawn from the national grid though a reduction in energy consumption. This is achieved largely through EE measures being introduced into existing municipal buildings and infrastructure. Introducing EE measures however should not impact the delivery of a municipal service or be necessary to support the delivery of a municipal service or function. The EEBPIP has a different objective to supporting or enhancing municipal service delivery and therefore we do not believe that a EnPC constitutes a municipal support activity.

3. AN OVERVIEW OF THE PROCUREMENT PROCESS APPLICABLE TO ENPC AT A NATIONAL, PROVINCIAL AND LOCAL GOVERNMENT LEVEL

3.1 The next section of our opinion canvasses the regulation of the procurement process that will apply to the procurement of an ESCO under an EnPC, specifically focusing on:

3.1.1 Procurement methods as prescribed under TR16A;

3.1.2 The bid evaluation and scoring system as envisaged in the PPPFA and PPPFA Regulations, 2017 – and in particular pre-qualification criteria, functionality requirements, price and BBBEE scoring; and

3.1.3 local content requirements and designated sectors applicable to EE measures; and

3.1.4 the status of the PPPFA Regulations.

3.2 Competitive procurement methods under the PFMA/ TR 16A

3.2.1 In terms of TR16A, procurement for good or services must be carried out either through quotations or a bidding process, subject to the thresholds value set by National Treasury.[22] The current threshold values are set in terms of PFMA SCM Instruction No. 02 of 2021/22 issued by National Treasury .

[22] Regulation 16A6.1.

3.2.2 The SCM Instruction stipulates that for any procurement between R2,000 and R1,000,000, price quotations must be called for by the institution (from at least 3 potential suppliers registered on the Central Supplier Database). For procurement over R1,000,000, the institution must carry out a competitive bidding process. Depending on the value of EnPCs being procured by a national or provincial institution, it will therefore be possible to either proceed with price quotations or a full competitive bidding process. The SCM Instruction allows for competitive bidding to be used for contract values below the R1,000,000 threshold.

3.2.3 TR16A does allow for procurement by other means, but this is in limited circumstances where it is "impractical" to invite competitive bids.[23] In such instances, the reasons for deviating from a competitive procedure must be recorded and approved by the accounting officer / authority of the institution.[24] However, we do not anticipate that this approach is necessary or appropriate for the EEPBIP.

3.2.4 Where a competitive bidding process is carried out, TR16A provides for certain requirements that must be followed, including that bids must be evaluated by a Bid Evaluation Committee and then adjudicated through a Bid Adjudication Committee.[25]

3.2.5 TR16A also requires that when an institution prepares bid documentation, this must specify the evaluation and adjudication criteria, and further that the PPPFA must be adhered to (as dealt with below).[26]

3.3 Competitive procurement methods under the Municipal SCM Regulations

3.3.1 The Municipal SCM Regulations provide for a range of procurement methods which municipalities must a dhere to in their supply chain management policies. This is based on various threshold values for the goods and services being procured.[27]

3.3.2 The most relevant for the purposes of procuring EnPCs under EEPBIP is that formal written price quotations must be used for transactions between R10,000 and R200,000 in value, and for transactions over R200,000 in value or "long term contracts", competitive procurement must be used.[28]

3.3.3 "Long terms contracts" are defined as those which have a duration of more than one year.[29] Accordingly, irrespective of the monetary threshold, it is likely that any EnPC being procured by a municipality would have to proceed through a competitive tender.

3.3.4 The structure of a municipal competitive bidding process would look essentially the same as for the national/provincial level (i.e. compliance criteria, functionality criteria, and then evaluation criteria made of price and specific goals).

[23] Regulation 16A6.4
[24] Regulation 16A6.4.
[25] Regulation 16A6.2.
[26] Regulation 16A6.3.
[27] Regulation 12(1) of the Municipal SCM Regulations.
[28] Regulation 12(1)(c) and (d) of the Municipal SCM Regulations.
[29] Regulation 1 of the Municipal SCM Regulations.

3.4 **Application of PPPFA and PPPFA Regulations, 2017 when procuring EnPCs**

3.4.1 The PPPFA provides that an organ of state must determine its preferential procurement policy and implement it within the framework of, amongst other things, a preference point system.

3.4.2 The PPPFA sets out this framework as follows:-

(a) for contracts with a Rand value above a prescribed amount of R50 000 000 (fifty million Rands)[30]: a maximum of 10 points may be allocated for specific goals provided that the lowest acceptable tender scored 90 points for price. The PPPFA specifies what the specific goals may include; however these are usually based on the bidders B-BBEE Contributor Status Level as determined in accordance with the Broad-Based Black Economic Empowerment Act[31] and the codes published thereunder;

(b) for contracts with a Rand value equal to or below R50 000 000 (fifty million Rands): a maximum of 20 points may be allocated for specific goals (as above) on the basis that the lowest acceptable tender scores 80 points for price; and

(c) the contract must be awarded to the highest scoring tenderer (combined price and specific goals) unless other objective criteria can justify the award to another tenderer.[32]

3.4.3 Accordingly, where any institution (including at national, provincial and municipal spheres) procures an ESCO under an EnPCs, it must rely on the above preference point system to a the successful ESCO.

3.4.4 The PPPFA Regulations give further content to the scoring requirements contained in the PPPFA. It makes provision for the use of pre-qualification criteria in a tender process, implements mandatory sub-contracting for EMEs/QSEs and disadvantaged groups for contracts above R30 million in value, prohibits sub-contracting to sub-contractors with a lower B-BBEE Contributor Status Level than the preferred bidder, and also provides for mandatory local content obligations. The following requirements are worth noting:-

(a) The PPPFA Regulations include a concept of pre-qualification criteria which is intended to advance designated historically disadvantaged groups (although this was one of the aspects which was challenged before the Constitutional Court as discussed below).

(b) Thus the Regulations allow for a procuring institution to impose requirements that bidders must either hold a minimum stipulated B-BBEE contributor status level, be an EME or QSE, or subcontract a minimum of 30% of the contract value to various categories of EME or QSE owned by various historically disadvantaged groups.[33] If such requirement is not met, the bid will not be considered acceptable.[34] In this way, procurement of an EnPC could be targeted

[30] Currently R50 million, however as the PPPFA Regulations, 2017 have been declared invalid (subject to an suspended order of invalidity) this threshold may change under the new regulation.
[31] Act 53 of 2003.
[32] Regulation 2(1)(f) of the PPPFA Regulations, 2017.
[33] Regulation 4(1) of the PPPFA Regulations, 2017.
[34] Regulation 4(2) of the PPPFA Regulations, 2017.

at ESCOs which are QSEs or EMEs (subject to the discussion of invalidity below).

(c) Prior to a bid being evaluated on price and preference points, they must first be evaluated on functionality criteria. Such criteria must be objective, and the tender documentation must specify how this will be scored.[35] Only bids which achieve the minimum functionality score can then be assessed on price and preference points.[36]

(d) In carrying out procurement under EEPBIP, it is important to balance the functionality criteria such that they are not too low, and hence jeopardise the quality of service, nor so high as to be unduly restrictive on potential ESCO bidders. This is relevant in particular for targeting ESCOs which are EMEs or QSEs, where requiring proof of a track record dating back, for example, 5 years may exclude the very businesses which EEPBIP should be attracting. In addition, the functionality criteria may be tailored to promote or give advantage to a particular choice of EE intervention or technology. On the other hand, where the institution is not married to any type of technology or intervention, the functionality requirements may be more open-ended and weighted towards performance and innovation.

(e) Local content requirements that require that a certain percentage of the contract value be spent on locally produced or manufactured services or goods in designated sectors are regulated under the PPPFA Regulations. Where an institution advertises for a tender in a designated sector, it must apply these local content requirements.

(f) The Department of Trade and Industry has, accordingly, identified certain sub-sector and minimum thresholds for local content. For the EEPBIP, the most relevant are: (i) solar PV components (varying between 15% for PV modules up to 90% for mounting structures);[37] (ii) solar water heater components (70%);[38] and (iii) pumps, MV motors and associated accessories (varying between 70% and 100%).[39]

3.4.5 The PPPFA Regulations issued in 2017 have recently come under review. In terms of section 5 of the PPPFA, the Minister of Finance is empowered to make regulations regarding any matter necessary or expedient to achieve the objects of the PPPFA. To this end, the PPPFA Regulations, 2017 were promulgated under the PPPFA, repealing the 2011 PPPFA Regulations.[40]

3.4.6 The PPPFA Regulations, 2017 were the subject of a court application wherein the applicant sought that the regulations be declared invalid. On 16 February 2022, the Constitutional Court of South Africa declared the regulations as being inconsistent with the Constitution and therefore invalid..

[35] Regulations 5(1), (2) and (3) of the PPPFA Regulations 2017.
[36] Regulations 5(6) and (7) of the PPPFA Regulations, 2017.
[37] National Treasury Designated Sectors Instruction Number 2 of 2016/2017.
[38] National Treasury Instruction on Invitation and Evaluation of Bids Based on a Stipulated Minimum Threshold for Local Production and Content for Solar Water Heater Components, 2014/2015.
[39] National Treasury Designated Sectors Circular Number 3 of 2017/2018: Invitation and Evaluation of Bids Based on a Stipulated Minimum Threshold for Local Production and Content for Pumps, Medium Voltage (MV) Motors and Associated Accessories.
[40] Regulation 16(1) of the PPPFA Regulations, 2017.

3.4.7 Whether the Constitutional Court's order of invalidity will be suspended for a period to allow National Treasury to draft new regulations is at the date of this opinion being clarified. A suspension of invalidity has the effect of keeping the PPPFA Regulations, 2017 in force until replaced by new regulations or the expiry of the period of suspension. What is certain is that the regime as currently envisaged in the PPPFA Regulations must be replaced in line with the Constitutional Court's ruling and therefore, to the extent possible, the roll out of the EEPBIP would do well to await the publication of the new regulations to prevent the need for a substantial re-draft of the draft procurement documentation prepared for the EEPBIP.

4. ADDITIONAL CONSENTS AND APPROVALS NEEDED TO PROCURE AN ENPC

4.1 In the following section we consider whether any additional consents or approvals from other public institutions or regulators would be required for purposes of concluding a valid EnPC. In particular we consider:

4.1.1 Whether an ESCO is required to be licensed under the ERA if the EE measures constitutes SSEG;

4.1.2 Whether the payment provisions under an EnPC amount to a "future financial commitment" for purposes of the application of section 66 of the PFMA or have a future budgetary implication in terms of section 33 of the MFMA; and

4.1.3 The applicable regime under the MFMA and the PFMA where a payment guarantee is requested by a lender from a public institution.

4.2 **Are any additional approvals required under the ERA for public buildings or infrastructure retrofitted with a SSEG solution?**

4.2.1 The ERA lists several actives which cannot be carried out without a license issued by the National Energy Regulator of South Africa. This includes, among other things, the operation of a generation facility.[41] In order to be classed under this licensing requirement, the following elements will therefore need to be present:-

(a) there must be generation, which is defined as "*the production of electricity by any means*", and the generation of electricity through rooftop solar panels or embedded generation technologies would satisfy this criterion;[42]

(b) there must be a "facility", which is defined as "*the generation facility … located at the Site and comprising all plant, machinery and equipment, all associated buildings, structures, roads on the Site that are not national, provincial or municipal roads, and other appurtenances, together with all required interfaces to be constructed for the safe, efficient and timely operation of that facility and, for the avoidance of doubt, excluding the transmission connection works or distribution connection works, as the case may be*", which would cover the solar panels and related infrastructure; and

(c) there must be "operation" of such facility; although this term is not defined in the ERA, it is our view that whoever causes the facility to generate electricity would be viewed as the operator of the

[41] Section 7(1) of the ERA.
[42] Section 1 of the ERA.

generation facility and where an ESCO provides the service of operating EE equipment, including for example solar panels, under an EnPC it would thus be operating a generation facility for the purposes of the ERA.

4.2.2 However, this does not mean that the ESCO necessarily requires a NERSA license. The ERA provides that certain categories of facilities as listed in Schedule 2 of the ERA are not required to hold a license.[43] However, these facilities may instead be required to register with NERSA, with registration being a much simpler process and in respect of which NERSA does not exercise discretion.[44]

4.2.3 Schedule 2 of the ERA, accordingly, lists several types of generation facilities, dividing them into facilities which:-

(a) require neither license nor registration: the most relevant being (i) facilities of any size which are not grid connected; and (ii) facilities of under 100kW;[45] or

(b) require registration but not a license: this category covers facilities which are under 100MW in capacity and are grid connected.[46]

4.2.4 We understand that the EEPBIP may include EE interventions for embedded generation facilities which will be either (i) solar PV; or (ii) biogas power generation. These will be utilised on public buildings, streetlights, or at water/waste-water treatment facilities to lower electricity consumption from the grid. However, the intention is not for such facilities to be grid connected (and excess generation will not be fed into the national grid).

4.2.5 In such circumstances, the EEPBIP projects will fall under the first of the Schedule 2 categories, being a non-grid connected facility. Therefore, it will not be necessary for the ESCO to obtain a license from NERSA nor is registration with NERSA required.

4.3 Do the payment provisions under an EnPC amount to a "future financial commitment" for purposes of obtaining the Finance Minister's consent under section 66 of the PFMA?

4.3.1 National and provincial public institutions in South Africa are subject to the PFMA which regulates revenue, expenditure, assets and liabilities of these institutions.

4.3.2 Thus, where an institution enters into an EnPC, this will entail expenditure and potentially incurring payment and other liabilities across the lifecycle of the EnPC. Aside from compliance with the supply chain management / procurement aspects as set out in **Error! Reference source not found.** above, it is necessary to determine whether the EnPC contractual model will trigger approvals under the PFMA designed to ensure effective financial management.

4.3.3 In terms of section 66(1) of the PFMA, departments and public institutions in the national and provincial sphere (as set out below) cannot "*enter into any …*

[43] Section 7(2) of the ERA.
[44] Section 9(1) of the ERA.
[45] Paragraph 2 of Schedule 2 to the ERA.
[46] Paragraph 3 of Schedule 3 to the ERA.

transaction that binds or may bind that institution or the Revenue Fund to any future financial commitment" unless authorised under the PFMA.

4.3.4 Where the transaction under an EnPC, and in particular the public institution's payment obligations to the ESCO under the EnPC constitutes a "future financial commitment", then the PFMA requires that such future financial commitments be approved by various named functionaries as follows: -

(a) for the national government (i.e. national departments), the Minister of Finance;[47]

(b) for provincial government (i.e. provincial departments), the MEC for Finance in the relevant province,[48]

(c) for major public entities listed in Schedule 2 (including, for example, Eskom SOC Ltd and Transnet SOC Ltd), the accounting authority of that public entity which in terms of the PFMA is the board of such public entity;[49]

(d) for national government business enterprises listed in Schedule 3, its accounting authority i.e. board, and the entity must also be approved to conclude such transactions in terms of a notice in the Government Gazette issued by the Minister of Finance;[50]

(e) for any other national public entities (that is, neither a major public entity nor a national government business enterprise), the Minister of Finance; [51]

(f) for provincial government business enterprises (listed in Schedule 3), the MEC for finance in the relevant province in concurrence with the Minister of Finance, and such entity must also be expressly authorised by the Minister of Finance to conclude such transactions by notice in the Government Gazette;[52] and

(g) for constitutional entities and provincial public entities not listed in Schedule 3, they are not permitted to borrow monies, conclude transactions that incur future financial commitments etc, except in respect of obtaining bridging loans (i.e. of up to 1 year), but they must be expressly authorised to do so by the Minister of Finance in writing, and this will typically not align well with the structure of an EnPC.[53] Thus, where these types of institutions wish to conclude EnPCs or loan money for EE interventions, this will have to be channelled through the relevant provincial treasury.

4.3.5 Whether the above approvals are required turn on whether or not payment obligations under an EnPC constitute a future financial commitment. The PFMA does not include a definition for "future financial commitment", however, despite the relatively broad wording in section 66(1) of the PFMA itself, the interpretation of this section has been more limited.

[47] Section 66(2)(a) of the PFMA.
[48] Section 66(2)(b) of the PFMA.
[49] Section 66(3)(a) of the PFMA.
[50] Section 66(3)(b) of the PFMA.
[51] Section 66(3)(c) of the PFMA.
[52] Section 66(3)(d) of the PFMA.
[53] Sections 66(4) and (5) of the PFMA.

4.3.6 This limited interpretation is supported both by the Constitutional Court[54] and the National Treasury through the Circular on Contracts Containing Provisions Relating to Indemnities, Limitation of Liabilities and Warranties,[55] and Practice Note 5 of 2006 on Finance Lease Transactions.[56] Thus, it is generally accepted that any financial commitment under a contract which (i) is in its nature "similar to a credit or security agreement"[57]; and (ii) extends beyond the three year budgetary cycle of an institution (as envisaged in the PFMA) will be considered a future financial commitment requiring approval under section 66(1) of the PFMA.

4.3.7 In the light of the above, government departments and public entities in the national and provincial spheres of government will need to determine on a case-by-case basis whether a section 66 approval will be required for their transaction. However, our view is that a typical guaranteed savings or shared savings contract will not trigger this requirement.

4.3.8 It is worth noting that should the institution not comply with this requirement i.e. obtain the approval of the above-mentioned functionaries prior to entering into an EnPC, then section 68 of the PFMA will be triggered. The consequences of non-compliance are that the state and the relevant institution are not bound by that arrangement. This would obviously provide a great deal of risk for ESCO and lenders in entering into such transactions.

4.4 **Do the payment provisions under an EnPC have future budgetary implications such that the process under section 33 of the MFMA needs to be complied with?**

4.4.1 At the local government level, Section 33(1) of the MFMA permits municipalities to enter into contracts which impose financial obligations on the municipality beyond a financial year. However, where the financial obligations under the contract extends beyond the 3 years- covered in the annual budget under which the contract was procured, then certain additional requirements need to be met before such contract can be concluded, as follows:-

(a) the municipal council is required to adopt a resolution approving the contract, and in addition the resolution must confirm that the municipality will secure a significant capital investment or derive a significant economic or financial benefit;[58]

(b) 60 days prior to the meeting of the municipal council where the resolution is adopted, the municipal manager must conduct a public and government consultation process, which entails publishing the draft contract, inviting local community representations, and soliciting the views of National Treasury, the Department of Cooperative Governance and Traditional Affairs,;[59] and

---

[54] *Road Traffic Management Corporation v Waymark (Pty) Ltd* [2018] ZACC 12 at [45].

[55] This circular acknowledges that it is impractical for the National Treasury or relevant provincial treasury to approve every such transaction, and accordingly concludes that where an indemnity, limitation of liability or warranty "*is integral or incidental to expenditure that has already been approved by the relevant legislature or executive authority in the annual budget of the department/constitutional institution or public entity respectively*", then approval under section 66 is not required. This supports the reasoning that it is only transactions falling outside of the 3-year budget cycle that require approval.

[56] This practice note states at paragraph 2.8 that for finance leases that are (i) more economical than an operating lease; or (ii) for a period of less than 36 months, then approval is not required under the Treasury Regulations related to section 66. This again indicates the important of the 3-year time frame.

[57] *Road Traffic Management Corporation v Waymark (Pty) Ltd* [2018] ZACC 12 at [45].

[58] Section 33(1)(c) of the MFMA.

[59] Section 33(1)(a) of the MFMA.

(c) the municipal council is required to take this process and responses / views into account, and must also evaluate the potential impact of the financial obligations on the municipality and its potential future tariffs and revenue.[60]

4.4.2 Therefore, where the term of the EnPC is longer than 3 years, for the EnPC to be validly concluded, it will need to go through a section 33 process, irrespective of the value of the savings generated under the EnPC. Given the impact on timelines this process may have in concluding an EnPC, it seems preferable either to ensure that the EnPc does not extend beyond a 3 year budgeting cycle, alternatively, where a longer term contract is unavoidable[61] for municipalities to consider a bundling approach in terms of which a district municipality leads the procurement of ESCO(s) contracted under an EnPC on behalf of a group or cluster of local municipalities falling under its control.

4.5 What is the regime under the PFMA where a payment guarantee is requested from a public institution by a lender to an ESCO?

4.5.1 There are two scenarios where a payment guarantee may be needed under an EnPC. In the first instance, under a shared savings contract a lender to an ESCO may require an undertaking from the relevant public institution with whom the ESCO (borrower) is contracting that it will make the savings payments committed to under the contract. The second scenario arises under a guaranteed savings contract in terms of which the EE equipment is purchased by the public institution. If for any reason the public institution does not have sufficient capital budget or capital grant such as the EEDSM to cover the full cost of the EE equipment, the public institution may be required to approach an external lender to make up such shortfall. A lender may require the public institution to secure the loan through a government undertaking to repay the loan. [62] Of the two scenarios, the below analysis assumes that the model of EnPC is a shared savings contract.

4.5.2 Under the PFMA, guarantees, indemnities and security are covered by the same requirements, and are treated similarly to transactions which entail either borrowing or other future financial commitments as set out in paragraph **Error! Reference source not found.** above in terms of section 66 of the PFMA, although certain additional requirements are imposed in terms of section 70 thereof.

4.5.3 In particular, for the issuance of a guarantee, indemnity and any form of security by a provincial government (i.e. provincial departments), major public entities listed in Schedule 2, national government business enterprises listed in Schedule 3, and provincial government business enterprises, the same functionaries as set out above at paragraph **Error! Reference source not found.** are required to provide approval for such guarantee, indemnity or security.

4.5.4 Where the guarantee, indemnity or security is issued on behalf of a national government department and seeks to bind the National Revenue Fund, then in terms of section 70(1)(a) of the PFMA, such guarantee, indemnity or security must first be approved by the responsible cabinet member (i.e. the

[60] Section 33(1)(b) of the MFMA.
[61] It may be, under an energy savings contract that in order for an ESCO to recover its capital cost (of supplying EE equipment) and as well as its maintenance costs, that the term of the EnPC needs to endure for a period of longer than 3 years.
[62] Note that in this report, we have not considered the PFMA requirements in relation to Government institutions engaged in borrowing or lending (as regulated under section 66) as the focus is the EnPC and funding of the EnPC through third party debt.

national executive member in the relevant line ministry) with the concurrence of the Minister of Finance. The same requirement applies where a national public entity requests the Cabinet Minister who is its executive authority to issue a guarantee, indemnity or security on its behalf.

4.5.5 The difference between guarantees issued for a national government department in terms of section 70(1) (a) and a guarantee issued for a national public entity under section 70(1)(b) is that guarantees issued for national government departments constitute a direct charge against the National Revenue Fund,[63] whereas guarantees issued for a national public entity is a charge against the entity concerned.[64]

4.5.6 While unlikely, it remains to be seen whether lenders to an ESCO will require payment guarantees for an institution's payment commitments under a EnPC. If so, the above requirements will need to be met for any such guarantee to be valid and enforceable.

4.6 What is the regime under the MFMA where a payment guarantee or other form of security is required by a lender to an ESCO?

4.6.1 Municipal guarantees and payment security are dealt with in terms of sections 48 and 50 of the MFMA. This generally provides for two situations: (i) the municipality providing security for its own obligations (debt or contractual obligations); and (ii) the commitments or debt of another organ of state or person, typically a municipal entity.

4.6.2 In the context of an EnPC, such arrangements could arise where the municipality provides security for its own contractual (payment) obligations under an EnPC. In terms of section 48(1)(c) A municipality can provide security for its contractual obligations through a resolution of the municipal council provided that such contractual obligations are made in connexion with "*capital expenditure by other persons on property, plant, or equipment to be used by the municipality or such other person for the purposes of achieving the object of local government in terms of section 152 of the Constitution*".[65] There is no definition in the MFMA of "property plant or equipment", however on a literal interpretation we are comfortable that the arrangement under an EnPC for the supply, installation and maintenance of EE equipment or measures fall within the purview of what is contemplated in section 48(1)(c). Accordingly, security for a municipality's contractual (payment) obligations under an EnPC is possible provided the council approve this by resolution.

4.6.3 It bears mentioning that a municipality could not provide security for the payment obligations of a municipal entity under its sole control and in terms of an EnPC. Section 48(1)(b) restricts a municipality to providing security for the debt obligations of a municipal entity, but not the contractual obligations.

4.6.4 Section 48(2) of the MFMA specifies the forms of security that a municipality can issue when securing its contractual (payment) obligations under an EnPC. This includes mortgaging and ceding of rights and other forms of collateral, direct payment of monies from certain sources, ceding revenue rights, security deposits and other mechanisms. The list is not closed, and permits "*agreeing*

[63] Section 70(a)(a) of the PFMA
[64] Section 70(2)(b) of the PFMA.
[65] Section 48(1)(c) of the MFMA.

to such other arrangements as the municipality may consider necessary and prudent".[66]

4.6.5 Accordingly, municipalities have a relatively high degree of flexibility when concluding security arrangements. Any structuring of security under an arrangement with a lender will have to respect section 8(2) of the MFMA, which deals with the bank account of the municipality, and requires that any allocations to a municipality and monies collected by a municipality must first be paid into this account, which may have implications where a municipality offers cession over a revenue stream or similar security arrangement.

4.6.6 We do not foresee lenders requiring municipalities to secure their payment contractual obligations, the possibility to do so exists within the framework of section 48 of the MFMA.

4.6.7 Finally, section 50 of the MFMA regulates municipal guarantees. This prohibits the municipality from issuing a guarantee for commitments or debts of any organ of state or person, including in respect the municipality itself, unless the guarantee falls within the budgeted limits on guarantees set in the municipality's budget.[67] This also allows for only the debts (and not contractual commitments) of a municipal entity under the shared or sole control of the municipality to be guaranteed (should the ESCO conclude the EnPC with a municipal entity rather than the municipality itself) provided the stipulated compliance requirements are met.[68]

4.6.8 Thus, a municipality could issue a payment guarantee in respect of its payment obligations to an ESCO under a shared savings contract (in other words, the portion of achieved savings due to the ESCO). However, it could not do so in respect of a municipal entity as it can only guarantee debts and not payment obligations.

5. SUMMARY OF CONCLUSIONS

Key Findings:-

	Issue	Finding / Recommendation
1.	Procurement framework at the national and provincial level	In accordance with the PFMA, institutions are required to maintain and adhere to their supply chain management policy which must be fair, equitable, transparent, competitive and cost-effective. In addition, institutions to which TR16A apply must comply with the competitive tendering requirements thereunder when contracting for goods and services.
2.	Procurement framework at the municipal level	A municipality must comply with its SCM policy in procuring an ESCO to supply, install or maintain EE interventions and Chapter 11 of the MFMA and the Municipal SCM Regulations must be adhered to.
3.	Procurement of goods and services	EnPC's are a combination of both the provision of goods and services. However, the nature of the service is distinct as full risk in respect of the contractual output is transferred to the ESCO.

[66] Section 48(2)(j) of the MFMA.
[67] Section 50(a) of the MFMA..
[68] Section 50(b) of the MFMA permits a municipality to guarantee a municipal entity's debts under its sole control though a council resolution (in the same way as it issues security). Per section 50(c), it can issue a guarantee for a municipal entity under its shared control on approval from the National Treasury and then only if it maintains a cash-backed reserve or insurance in respect of the guarantee.

4.	Whether ta EnPC is a PPP	PPPs at a national/provincial and municipal level have more onerous approval requirements which are applied across the project lifecycle (inception, feasibility, procurement and contracting). Procurement of an ESCO in terms of an EnPC would not constitute a PPP at the national/provincial or municipal level as it does not satisfy the definition of a PPP under either TR16A or the Municipal PPP Regulations.
5.	Whether an EnPC is a municipal service	To the extent that a service is provided under an EnPC, this does not meet the definition of a municipal service. This is because the financial cost savings and reduced emissions are not a service provided for the benefit of the local community, despite benefits to the environment . An EnPC does not constitute a municipal support activity. Accordingly, the provisions of the MSA will not apply to the procurement of an ESCO under an EnPC.
6.	Competitive procurement methods under the PFMA / TR16A	An EnPC being procured at national level must use written price quotations from at least 3 CSD registered suppliers (contracts between R2,000 and R1,000,000). Above R1,000,000, competitive bidding must be used, although it can also be used for contracts below this threshold. The bidding process must include a Bid Evaluation Committee and Bid Adjudication Committee. Evaluation and adjudication criteria must be specified and PPPFA (i.e. a price and preference points system) must be complied with.
7.	Competitive procurement methods under the Municipal SCM Regulations	An EnPC being procured by a municipality must proceed through a competitive tender process. Formal written price quotations must be used for transactions between R10,000 and R200,000 in value, and for transactions over R200,000 in value or “long term contracts”, competitive procurement must be used. Long terms contracts means any contract of over 1 year in duration, and therefore a typical EnPC will be required to use competitive bidding. The structure of the bidding process must be the same as at national and provincial level i.e.. Include compliance criteria, functionality criteria, and evaluation criteria made of price and specific goals.
8.	The PPPFA and PPPFA Regulations 2017 in procuring EnPCs	Where an institution, either at national, provincial or municipal level; procures an ESCO under an EnPC, it must rely on a price and preference point system as per the PPPFA framework. The PPPFA Regulations permit pre-qualification criteria and local content requirements to be included, and require that functionality criteria must be included in the tender and evaluated in order to qualify for the price and preference points assessment. As the PPPFA Regulations have been declared invalid by the Constitutional Court (and pending confirmation of suspension of this invalidity for one year), we recommend the EEPBIP must await the publication of new regulations to prevent the need to re-draft the draft procurement documentation prepared under the EEPBIP.
9.	ERA requirements	The ERA provides for activities which require a NERSA license, including operation of a generation facility. It also provides for exemptions from this requirement, and requires

		registration with NERSA instead of a license in certain instances, as set out in Schedule 2 of the ERA. A typical ESCO consisting of rooftop solar or biogas facilities which are not connected to the grid are not required to be licensed nor are they required to be register.
10.	Approval of EnPC in terms of Section 66 of the PFMA	Section 66 of the PFMA stipulates the functionaries who must enter into borrowing and other transactions with future financial implications, depending on the nature of the institution. This will cover any transaction similar to a debt or security agreement of longer than 3 years (ie beyond the current budgeting period). Whether section 66 approvals are required must be determined on a case-by-case basis.
11.	Compliance with Section 33 of the MFMA before concluding an EnPC	Section 33 of the MFMA imposes requirements for a municipal council resolution and extensive public and National Treasury / pr consultation procedures to be completed in order to conclude a contract of longer than 3 years in duration. It is preferable to structure an EnPC over a shorter time period where a municipality wants to avoid the onerous section 33 requirements. If a longer term is unavoidable, a bundling approach led by a district municipality should be considered.
12.	Regulation of guarantees, indemnities and security under the PFMA	Although unlikely, a payment guarantee requirement is most likely to arise under a shared savings contract where the lender to an ESCO requests a payment guarantee from the institution. Such guarantee can be issued, with the same approval requirements under section 66 as for future financial commitments. In addition, where the national revenue fund is to be bound, the relevant Cabinet Member with the concurrence of the Minister of Finance must approve the transaction, and a similar requirement arises for a public entity that intends to be issue a guarantee.
13.	Regulation of security and payment guarantees under the MFMA	Where procuring EE equipment, sections 48(1) and (2) of the MFMA allow a municipality to issue a number of forms of security when securing its contractual (payment) obligations under an EnPC. This includes mortgaging and ceding of rights and other forms of collateral, direct payment of monies from certain sources, ceding revenue rights, security deposits and other mechanisms. A municipal council resolution is required to enter into such security arrangements. Section 50 of the MFMA further permits a municipality to issue guarantees in respect of its payment obligations, which may be requested by the lender to an ESCO under an EnPC. This must also be approved by a resolution of the municipal council.

Approvals and consents:-

	Context of Approval / Consent & Applicable Legislation	**Brief Description**
1.	Consents/approvals as per the PFMA	1. Where the national or provincial institution's payment obligations to the ESCO under the EnPC constitutes a "future financial commitment", section 66 of the PFMA requires that the transaction be entered into by the following functionaries:- a) for national departments – by the Minister of Finance;

		b) for provincial departments – by the MEC for Finance in the applicable province; c) for major public entities as in Schedule 2 – by the relevant accounting authority of the public entity; d) for national government business enterprises as in Schedule 3 – its accounting authority (and must be authorised by notice in a Government Gazette, by the Minister of Finance); e) for other national public entities – by the Minister of Finance; f) for provincial government business enterprises – the MEC for finance in the applicable province, (and must be authorised by notice in a Government Gazette, by the Minister of Finance); and g) for constitutional and provincial public entities not listed in Schedule 3 – such institutions cannot conclude such a transaction. This must instead be channelled through the relevant provincial treasury. 2. Where issuing a guarantee, section 66 read with section of the PFMA requires that the guarantee transaction be entered into by the following functionaries:- a) Where national government issues a guarantee, indemnity or security – the transaction must be entered into by the responsible cabinet minister with the Minister of Finance concurring. b) Where a national public entity issues a guarantee, indemnity or security – the transaction must be issued by the responsible cabinet member with the Minister of Finance concurring. c) For all other institutions, the same functionaries as above will be applicable.
2.	Consents/approvals as per the MFMA	1. Section 33 of the MFMA imposes certain requirements where a contract which imposes financial obligations on a municipality extends beyond three years:- a) Resolution by the municipal council; b) A public and government (National and provincial treasury) consultation process conducted by the municipal manager; and c) evaluation by the municipal council on the potential impacts. 2. In order to enter into a) a security transaction (section 48); or b) guarantee (section 50) for the procurement of EE interventions, a municipal council resolution is required.