

# Tariff Application Financial Year 14/15



**Tariff application to the Ports Regulator in terms of the National Ports Act,  
2005**

**(Act No. 12 of 2005)**

**September 2013**

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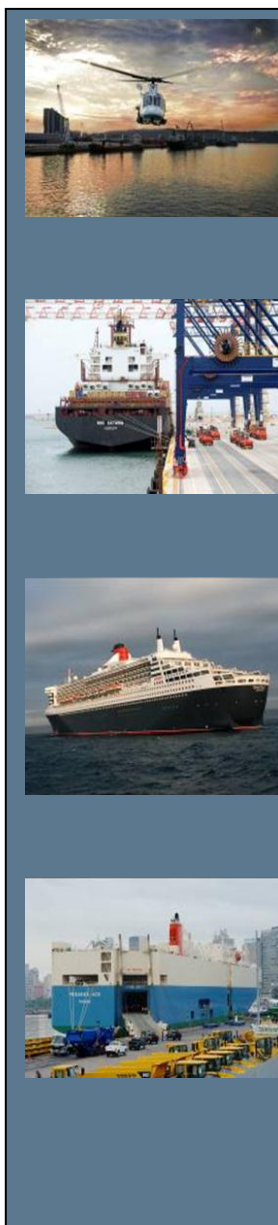
## ABBREVIATIONS AND ACRONYMS

AFS	Annual Financial Statements
APDP	Automotive Production Development Program
CAPEX	Capital Expenditure
CAPM	Capital Asset Pricing Model
CMEO	Chief Marine Engineering Officer
CPI	Consumer Price Index
CPT	Cape Town
CSI	Corporate Social Investment
CWIP	Capital Work In Progress
DBN	Durban
DBT	Dry Bulk Terminal
DCT	Durban Container Terminal
DIA	(Old) Durban International Airport
DMS	Dimson, Marsh and Staunton
DORC	Depreciated Optimised Replacement Cost
DRS	Dredging Services
ECICS	East Coast Integrated Cargo Strategy
EL	East London
ETIMC	Excessive Tariff Increase Margin Credit
FEL	Front End Loading
GDP	Gross Domestic Product
GRT	Gross Registered Tonnage
IAS	International Accounting Standards
IC	Interim Clawback
JSE	Johannesburg Stock Exchange
m	Million
MDS	Market Demand Strategy
MIDP	Motor Industry Development Plan
MPT	Multi-Purpose Terminal
MRP	Market Risk Premium
MSC	Mediterranean Shipping Company
Mtpa	Millions tonnes per annum
NBV	Net Book Value
NGQ	Ngqura
NPA	National Ports Authority
NPCC	National Port Consultative Committee
OD	Operating Divisions
Opex	Operating Expenditure
PCC	Port Consultative Committee
PE	Port Elizabeth
RAB	Regulatory Asset Base
RR	Revenue Requirement
RBCT	Richards Bay Coal Terminal
RCB	Richards Bay
ROD	Record of Decision
SARB	South African Reserve Bank
SLD	Saldanha Bay
SRAB	Starting Regulatory Asset Base

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TCC	Transnet Corporate Centre
TEU	Twenty-foot Equivalent Unit
TOC	Trended Original Cost
TOPS	Terminal Operator Performance Standards
TPT	Transnet Port Terminals
TSHD	Trailing Suction Hopper Dredger
WACC	Weighted Average Cost of Capital



## 1. Executive summary

In terms of Section 72 (1) (a) of the National Ports Act, 2005 (Act No. 12 of 2005) ("the Act"), Transnet National Ports Authority, a division of Transnet SOC Limited ("the Authority") is required, with the approval of the Ports Regulator ("the Regulator"), to determine tariffs for services and facilities offered by the Authority and to annually publish a tariff book containing those tariffs. The Port Directives were approved on 13 July 2009 (gazetted on 06 August 2009) and amended on 29 January 2010. In terms of these Directives, when considering the proposed tariffs for the Authority, the Regulator must ensure that such tariffs allow the Authority to:

- a) recover its investment in owning, managing, controlling and administering Ports and its investment in port services and facilities;
- b) recover its costs in maintaining, operating, managing, controlling and administering Ports and its costs in providing port services and facilities; and
- c) earn a return commensurate with the risk of owning, managing, controlling and administering ports and of providing port services and facilities.

The regulatory framework does not set a tariff methodology nor does it constrain the Ports Regulator from adopting one different from the Authority. The Authority submitted its tariff methodology position paper to the Regulator which has been consulted with stakeholders. The Regulator has considered the Authority's position paper as well as the submissions received from interested parties and is currently reviewing the tariff methodology. The resultant outcome of such review aims to define a standard approach to determining components which would inform the appropriate revenue for the Authority.

The Regulator, after consideration of the Authority's proposal, and keeping in line with previous determinations decided to issue an interim Regulatory

Manual, applicable to the 2014/15 tariff year. The Regulator is of the view that the guidelines will assist in narrowing the historical gap between what is requested by the Authority and subsequently granted by the Regulator.

The approach (applicable to the 2014/15 Tariff year) decided upon is based on the Revenue required methodology. The formula for the Revenue Required methodology is as follows:

### *Revenue Requirement*

*= Regulatory Asset Base (RAB) X Weighted Average Cost of Capital (WACC) + Operating Costs+ Depreciation + Taxation Expense – (+) Claw back +(-) Excessive Tariff Increase Margin Credit (ETIMC)*

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In summary, the key principles included in the Regulatory Manual are as follows:

- a) **Regulatory Asset Base (RAB):** The RAB represents the value of assets that the National Ports Authority (NPA) is allowed to earn a return on.
- b) **Vanilla Weighted Average Cost of Capital (WACC):** A real Weighted Average Cost of Capital will be applied, given that the RAB is indexed for inflation.
- c) **Operating Costs:** The NPA is required to provide detailed and complete motivation for each of the expenses applied for.
- d) **Depreciation:** The depreciation of the assets in the RAB will be calculated as a straight line 40 year on the opening balance of the RAB.
- e) **Taxation Expense:** The Regulator will use the pass-through tax approach where the vanilla WACC will be applied to the average RAB for the period under consideration, less the interest cost of debt and the corporate tax rate to determine the tax liability to be treated as an expense in the RR calculation.
- f) **Claw Back:** The Regulator will spread the total impact of over/under recovery of revenue over a period of two tariff determinations.
- g) **Excessive Tariff Increase Margin Credit (ETIMC):** The Regulator considers it prudent to avoid future tariff spikes by retaining and increasing the NPA's Excessive Tariff Increase Margin Credit (ETIMC).

The tariff application for FY 2014/15 has been prepared using the aforementioned Revenue Required methodology, in line with the prescribed interim Regulatory Manual. The application of the methodology is illustrated in the table below:

**Table 1: Revenue requirement**

	FY 2014/15
	Rm'
<b>RAB</b>	64 694
Real Post WACC	5.83%
Return on Capital	3 772
Plus: Depreciation	1 671
Plus: Operating Expense	4 329
Plus: Taxation Expense	1 057
Plus: Clawback	118
Revenue Requirement	10 947
Less: Real Estate	-2 113
Marine Revenue	8 834

Application of the Revenue Requirement formula results in a revenue requirement of R10 947m (**Table 1**) comprising of Real Estate business revenue of R2 113m and Marine Business revenue of R8 834m. In order to determine Marine Business revenue to be derived from tariff adjustments, the



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required revenue of R8 834m is compared with the expected revenue of R7 462m for FY 2013/14 increased for the expected growth in volumes of 3.5% for FY 2014/15.

**Table 2: Marine Revenue (Based on 14.39% increase)**

Marine Revenue	Rm'
Latest Estimated Revenue for FY 2013/14	7 462
Estimated Volume Growth for FY 2014/15	3.50%
	7 723
FY 2014/15 Required Revenue	8 834
Tariff Increase	14.39%

This translates into an average tariff adjustment of 14.39% for FY 2014/15.

The roll-out of the Authority's CAPEX programme in terms of Transnet's Market Demand Strategy (MDS) will result in spikes and troughs for future tariff adjustments when applying the Revenue Requirement formula. The Authority's projection of future tariff adjustments (beyond FY 2014/15) using similar parameters for FY 2014/15 will range between 7.0% and 12.89% per annum. In the last tariff application for FY 2013/14, the Authority commenced with discussions on a multi-year tariff application approach which would assist with smoothing the tariff trajectory. This approach would result in a smoothed tariff increase of 9.70% from FY 2015/16 to FY 2018/19. However, the Regulator is yet to make a decision on this approach as part of its review of the Authority's tariff methodology position paper.

The Authority remains firmly of the view that the tariff methodology and approach to determine components thereof, as captured in its tariff methodology position paper is most appropriate for tariff determination purposes. The proposed methodology addresses the financial sustainability of the Authority especially during the critical years of the Transnet MDS which aims to address the needs of customers. Even though the interim Regulatory Manual is based on the revenue required methodology (called upon by the Authority in its position paper) the approach in determining some of the components differs in comparison to the Authority's proposal. The Authority retains its approaches as captured in its proposal. Therefore whilst the tariff application FY 2014/15 has been prepared on the basis of the guidelines contained in the interim Regulatory Manual, this is with the understanding that Authority's tariff methodology position paper is still under review by the Regulator.

The Authority is mindful of Transnet's commitment to reducing the cost of doing business in South Africa and has considered an approach to ensure a sustainable tariff increase which is in the interest of the economy. Through this assessment, the Authority is of the view that it can deliver on the planned execution of the Transnet MDS with Marine Business revenue cash revenue of R8 380m. Based on the interim Regulatory Manual, the Authority therefore applies to the Regulator to release R454m of the ETIMC provision previously created.



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**Table 3: Required revenue post ETIMC**

Marine Revenue	Rm'
Marine Revenue Required	8 834
Less ETIMC	454
Marine Revenue for FY 2014/15	8 380

Which translates to an average overall tariff adjustment of 8.5%:

**Table 4: Marine Revenue based on 8.5% increase**

Marine Revenue	Rm'
Latest Estimated Revenue for FY 2013/14	7 462
Estimated Volume Growth for FY 2013/14	3.50%
	7 723
FY 2014/15 Required Revenue	8 380
Tariff Increase	8.5%

The 8.5% tariff adjustment is consistent with that communicated by the Authority in its Tariff Application FY 2013/14. In the tariff application FY 2013/14 the Authority advised that a smoothed tariff adjustment of 8.5% p.a. would sustain the organisation for the Transnet MDS years FY 2014/15 – FY 2018/19.

The nature of the port authorities' business necessitates investment in long-term infrastructure which is preceded by long lead times for adequate consultation, planning, approvals and delivery. This has all been taken into consideration in preparation of the Authority's tariff methodology position paper which aims to ensure a financially sustainable organisation that is able fulfil its role i.e. management of the national commercial port system as a landlord port authority.

In accordance with the interim Regulatory Manual the Authority hereby applies to the Regulator for revenue of R10 493m comprising of marine business revenue of R8 380m and real estate business revenue of R2 113m for FY 2014/15. This translates to an average overall tariff adjustment of 8.5%:

Translation of this marine revenue of R8 380m into individual tariffs (tariff book) will be informed by the Regulator guideline which will be issued post the tariff determination process.

## 2. Introduction

The Transnet National Ports Authority, a division of Transnet SOC Limited ("the Authority") is the landlord in the South African port system. The Authority is responsible for the safe, efficient and effective economic functioning of the national ports system which it manages, controls and administers. The key business activity of the Authority is to provide and manage port infrastructure and maritime services. In a broader context, the Authority also undertakes to facilitate the development of trade and commerce through market collaboration for the economic benefit of the national economy.

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This application commences by introducing the primary legislation that deals with the Authority's tariffs and progresses to give an overview of the ports business and infrastructure plans. The tariff application for FY 2014/15 has been prepared in line with the interim Regulatory Manual using the Revenue Requirement approach, with the determinants for the Authority's revenue being described accordingly. The Regulator will provide the Authority, after the overall tariff determination, with guidelines in accordance with which the tariff book must be amended.

### 3. Legal Basis and Regulatory Requirements

The regulatory framework for the Authority's tariffs is informed by the National Ports Act, Regulations issued under such Act, the Directives promulgated by the Ports Regulator. In terms of the regulatory framework the Authority is required, with the approval of the Regulator, to determine tariffs for services and facilities offered by the Authority and to annually publish a tariff book containing those tariffs.

#### 3.1 Section 72 of the Act sets out Authority's obligations in relation to its tariff book:

##### "Authority's tariff book"

72. (1) (a) The Authority must, with the approval of the Ports Regulator, determine tariffs for services and facilities offered by the Authority and annually publish a tariff book containing those tariffs.
- (b) The Authority may, with the approval of the Ports Regulator, amend the tariff book whenever it is necessary to do so.
- (2) The Authority must, prior to any substantial alteration of a tariff, consult with the National Port Consultative Committee.
- (3) Subject to section 9 of the Competition Act, 1998 (Act No. 89 of 1998), the tariffs contemplated in subsection (1) may vary between ports.
- (4) Notwithstanding the provisions of this section, the Authority may enter into an agreement with a licensed operator or a party to an agreement or a port user for the variation of any tariff contemplated in subsection (1).

#### 3.2 The Ports Directives

- 3.2.1 The Regulator developed the Directives, which were gazetted on 6 August 2009 and amended on 29 January 2010. Of these, the most pertinent to the setting and approval of tariffs are Directive 22 (which deals with the Approval and amendment of tariffs') and Directive 23 (which deals with Tariff requirements').
- 3.2.2 Directive 23(1) requires the Regulator to consider whether the tariffs proposed by the Authority reflect and balance:
  - a) A systematic tariff that is applicable on a comparable basis;
  - b) Fairness;

- c) The avoidance of discrimination save where discrimination is in the public interest;
  - d) Simplicity and transparency;
  - e) Predictability and stability
  - f) The avoidance of cross subsidisations save where cross subsidisation is in the public interest; and
  - g) The promotion of access to ports and efficient and effective management and operation in ports.
- 3.2.3 The opening statement of sub-directive 23(2), reads as follows: In considering the Authority's proposed tariffs, and any subsequent proposed significant variations, the Regulator must enable the Authority to;
  - (a) Recover its investment in owning, managing, controlling and administering ports and its investment in port services and facilities;
  - (b) Recover its costs in maintaining, operating, managing, controlling and administering ports and its costs in providing port services and facilities; and
  - (c) Make a profit commensurate with the risk of owning, managing, controlling and administering ports and of providing port services and facilities.
- 3.2.4 This sub-directive prescribes that the Regulator must enable the Authority to recover its investment, costs and to earn a profit commensurate with the risk it bears.

### **3.3 Tariff Methodology**

- 3.3.1 Having a tariff methodology in place assists in the application of the regulatory framework in order to determine the Authority's overall revenue requirement. The regulatory framework does not set a tariff methodology nor does it constrain the Ports Regulator from adopting one different from the Authority. However it is in the best interest of the Authority and stakeholders that agreement be reached between the Ports Regulator and the Authority on an appropriate tariff methodology as well parameters of the elements contained therein. Such agreement would bring about a higher level of certainty for all parties affected by the tariff determination process.
- 3.3.2 In order to identify an appropriate tariff methodology, the Authority sought guidance on experience with regulatory regimes around the world whilst keeping in mind the local economic landscape and legal framework in South Africa. Port facilities are key infrastructure for economic development and growth. Therefore, a sound approach to economic regulation, which promotes appropriate investment whilst allowing port users to access services at fair and reasonable tariffs, is required. To this end the Authority and the Regulator will need to apply judgement in achieving this balance to promote access and investment within the port system.

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- 3.3.3 The Authority submitted its tariff methodology position paper to the Regulator in September 2012. This paper was published by the Regulator and was consulted with stakeholders during March 2013. The Regulator has considered the Authority's position paper as well as the submissions received from interested parties and is currently reviewing the tariff methodology. The resultant outcome of such review aims to define a standard approach to determining components which would inform the appropriate revenue for the Authority.

### 3.4 The Interim Regulatory Manual for the Tariff Year 2014/15

- 3.3.4 The Regulator, after consideration of the Authority's proposal, and keeping in line with previous determinations decided to issue an interim tariff methodology, applicable to the 2014/15 tariff year. The Regulator is of the view that the guidelines will assist in narrowing the historical gap between what is requested by the Authority and subsequently granted by the Regulator.
- 3.3.5 The approach (applicable to the 2014/15 Tariff year) decided upon is based on the Revenue required methodology and the building blocks are set out below. The Regulator retains some degree of regulatory space to respond to unforeseen economic or other events, which may impact on the sustainability of the South African Ports system. This has been captured in the guidelines.
- 3.3.6 The components of the Regulatory Manual are discussed as follows:-
- 3.3.6.1 **Regulatory Asset Base (RAB):** The value of total assets in the RAB is indexed to inflation each year - the Trended Original Cost ("TOC") approach. Each year, estimated capital expenditure and depreciation is added to the closing balance for the previous year to arrive at an updated closing balance for the current year. The expected working capital balance is added to arrive at a total RAB estimate, which is averaged over the year to account for the progressive spending of CWIP over the period. The RAB formula applicable to the FY 2014/15 tariff year is as follows:

Diagram 1: RAB Formula

$$RAB_y = \frac{1}{2} [RAB_{c,y} + RAB_{o,y}] + W_y$$

$$RAB_{c,y} = RAB_{o,y} (1 + CPI_y) - D_y + CWIP_y$$

**Where:**

$RAB_y$  is the value of the RAB that is used to determine the returns for the period  $y$ ;

$RAB_{o,y}$  is the opening value of the RAB for the period  $y$ ;

$RAB_{c,y}$  is the closing value of the RAB for the period  $y$ ;

$W_y$  is the forecast working capital over the period  $y$ ;

$CWIP_y$  is the value of expected capital investment over the period;

$D_y$  is the depreciated allowance for assets within the opening RAB held to the end of period  $y$ ;

$CPI_y$  is the annual rate of inflation expected over the period  $y$ .

- 3.3.6.2 **Depreciation:** The depreciation of the assets in the RAB will be calculated, as straight line 40 year depreciation.
- 3.3.6.3 **Inflation trending:** The inflation rate for calculating the trend in the value of assets will be the general CPI forecast for FY 2014/15. The same inflation rate will be used in the calculation of the weighted average cost of capital.
- 3.3.6.4 **Capital Works in Progress (CWIP):** Detailed projections for the FY 2014/15 per asset class, service and project must be provided to motivate the CWIP to be included in the RAB.

3.3.6.5 **Working Capital:** The estimate of working capital, equates to the actual Net working capital as per the latest available NPA annual financial statements (not the change in working capital as per previous applications), consisting of accounts receivable plus inventory less accounts payable (i.e. operating cash is excluded), adjusted by forecast volume growth and CPI inflation for FY 2014/15. In addition, capital work in progress payables, which are estimated at 1/12<sup>th</sup> of the capital expenditure projected for that year is included.

3.3.6.6 **Weighted Average Cost of Capital (WACC):** In general, the weighted average cost of capital ("WACC") is the minimum return that a company must make on its investment in order to continue to attract capital, given the risks that investors carry when they commit funds to the business.

- **Vanilla WACC:** A real Weighted Average Cost of Capital will be applied. Also, the WACC will be expressed in Vanilla terms (i.e. post-tax cost of equity and pre-tax cost of debt) and accordingly, a separate allowance for tax expense in the revenue requirement formula is required.

$$WACC_{vanilla} = k_d \cdot g + k_e(1 - g)$$

Where:

*k<sub>e</sub> - cost of equity (post tax, real).*

*k<sub>d</sub> - cost of debt (pre-tax – i.e., free of any adjustments for the tax shield on interest, real).*

*g - gearing (defined as the ratio of debt over debt plus equity).*

- **Risk Free Rate:** The twenty year government bond is an appropriate measure of the risk free rate, and, in particular, the R186 bond instrument (yield) as it adequately reflects the market's perception of sovereign risk and inflation going forward. The average risk free rate calculated over a 5 year period (from August 2008 to July 2013).

The Real risk Free Rate is deduced by using the Fisher Equation.

$$1 + i = (1 + r)(1 + E(I))$$

Where:

*i = nominal rate    r = real rate*

*E(I) = Expected inflation*

- **Market Risk Premium:** The Market risk premium is in essence forward-looking and, as such, it cannot be observed but must be predicted. As a result, the measurement of a market risk premium is problematic. For

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the FY 2014/15 tariff assessment, the Regulator will use the Dimson, Marsh and Staunton (DMS) estimate of the arithmetic mean MRP as measured against bonds for South Africa to determine a MRP for the NPA cost of equity calculation.

- **Beta:** Because the NPA is not a traded company, the choice of comparators used to calculate a beta must be as similar as possible to reflect the risks faced by NPA under the RR methodology. This is to prevent it substantially overestimating (or underestimating) the appropriate return for risk faced.
- The inclusion of a claw-back mechanism, the introduction of the ETIMC and the inherent public nature of the NPA and the existence of an interventionist regulatory regime requires the Regulator to use a Beta substantially lower than proposals such as the JSE top 40.
- For the 2014/15 tariff year, the Regulator will use the 0.50 asset beta decided upon in the previous ROD's.
- Given a D:E ratio of 1:1 (See section 7.5) this equates to an equity beta of 0.86 using the Hamada equation to re-lever the beta.
- **Gearing:** The appropriate gearing for the entity for the 2014/15 tariff year is 50%.
- **Cost of Equity:** The post-tax cost of equity is calculated with reference to the capital asset pricing model (CAPM), which is expressed as:

$$k_e = r_f + \beta \times MRP$$

*Where*

*$r_f$  is the real riskfree rate*

*$\beta$  measures the NPA's exposure to market (non-diversifiable) risk*

*MRP is the market risk premium measuring the premium over and above the risk-free rate that investors might expect to earn*

- **Cost of Debt:** NPA's actual, embedded debt costs should be used to determine the cost of debt applied within the WACC. The average embedded Transnet group cost of debt (pre-tax nominal) of Transnet SOC Ltd should be used for the 2014/15 tariff year, as no current alternative exists.



- 3.3.6.7 **Taxation:** A corporate tax rate of 28% will be used for the 2014/15 Tariff Year. The pass-through tax approach, where the vanilla WACC will be applied to the average RAB for the period under consideration, less the interest cost of debt and the capital expenditure payments impact. The corporate tax rate will be used to determine the tax liability which shall be treated as an expense in the RR calculation.

$$\text{Tax allowance} = (\text{Net revenue before tax allowance}) / (1-t) * t$$

“Net revenue before tax allowance” is the revenue after all costs including interest and depreciation have been accounted for. i.e. it is the net return to equity before being grossed up to make allowances for taxation.

- 3.3.6.8 **Operating Expense:** The NPA is required to provide detailed and complete motivation for the applied expenses.

Transnet group costs will be included in the total allowed expenses subject to the requirement that the NPA submits detailed explanation and motivation for the amount to be transferred to Transnet group.

In addition, the NPA shall provide externally audited financial reports with all supporting documentation and detailed explanations including basis of allocation and policy documents that support such allocations.

- 3.3.6.9 **Claw Back:** The key purpose of applying claw-back is to ensure that the NPA or any port user does not gain or lose out from differences between allowed Revenue (based on a number of forecasts and assumptions) calculated at the time of the tariff application and actual audited figures.

The total impact of over/under recovery of revenue will be spread over a period of two tariff determinations.

- 3.3.6.10 **Excessive Tariff Increase Margin Credit (ETIMC):** The Regulator regulates in the long term interest of the industry. This requires that the Regulator not only confine itself to the immediate tariff decision, but also consider ways to ease any future shocks to the system that are capable of being managed sustainably within the space that is available for such intervention. It is generally accepted that capital expenditure will spike at some point in the foreseeable future, but that these projects have not as yet been specified to a level of detail that allows for accurate prediction. As such, the Regulator considers it prudent to avoid future tariff spikes by retaining and increasing the NPA’s Excessive Tariff Increase Margin Credit (ETIMC).

Because the ETIMC is revenue collected from port users before the NPA is entitled to it, it should yield a return for users to compensate them for the opportunity cost of their capital. . The ETIMC will therefore earn a return which is equal to the WACC allowed by the Regulator. The return on the ETIMC will be factored into the balance calculation to be included in the FY 2014/15 ROD.

## **4. The Business of the Authority**

### **4.1 Introduction**

The Authority operates within the port industry, providing services to its target market comprising of port users, which include terminal operators, shipping lines, ship agents, cargo owners and the clearing and forwarding industry. The Authority owns and manages nine ports within South Africa namely, Saldanha Bay, Cape Town, Mossel Bay, East London, Port Elizabeth, Durban, Richards Bay, Ngqura and Port Nolloth.

Port infrastructure and maritime services are provided in five market segments namely, containers, dry bulk, liquid bulk, break-bulk and automotive. The major commodities handled at the ports are coal, iron ore, containers, automotive, steel, fruit, ferrochrome, petroleum products and manganese. Growth of these commodities is a function of global demand, logistics infrastructure capacity and supply chain efficiencies which include port efficiencies.

Port users fall into three main categories, namely, terminal operators, shipping lines and cargo owners. While numerous other parties utilise the port, they do so to a lesser extent than these principal port users.

### **4.2 The functions of the Authority**

The National Commercial Ports Policy requires that the Authority be responsible for the management of the national commercial port system as a landlord port authority. Being a landlord port authority means that the Authority:

- owns, develops and maintains port infrastructure;
- does not engage in port operations (except as operator of last resort);
- does not employ cargo handling labour;
- fulfils a port regulatory and port landowner function; and
- owns all port land.

The Authority's core functions (as set out in Section 11 of the Act) can be summarised in the table as follows:

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**Table 5: The Authority's Core Functions**

Function	Detail
Landlord	Promote the use, improvement and development of ports, and control land use within the ports, having the power to lease port land under conditions it determines.
Master planner	Plan, improve, develop and maintain port infrastructure.
Controller of ports navigation	Make and apply rules to control navigation within port limits and approaches, ensure protection of the environment and ensure safety and security within port limits.
Controller of ports services and facilities	Ensure that port services and facilities are provided, and may enter into agreements or license other parties to provide these.
Marketer and administrator	Ensure that adequate, affordable, equitable and efficient port services and facilities are provided for port users.
Change agent	Ensure non-discriminatory, fair, transparent access to port services and facilities; advancement of previously disadvantaged people; promotion of representation and participation in terminal operations; enhanced transparency in port management.
Coordinator with other State Agencies	Advise on all matters relating to the port sector, and liaise with all stakeholders.

### 4.3 Market Demand Strategy (MDS)

The South African ports occupy a central position in the transport and logistics chain with 98% of cargo volume passing through them annually. Ports are inherently required to play a leading role in influencing economic growth to respond to market conditions.

The MDS will enable growth in key commodities and will position South Africa globally as a key thermal coal exporter, an increasingly important fourth largest supplier of iron ore to China, leading manganese exporter globally, and the leading logistics hub for sub-Saharan Africa.

The MDS anticipates R307.5bn capital expenditure program over 7 years. To enhance its finance and funding strategy, Transnet intends to build the confidence of its funders and develop both new and existing options to optimise and diversify its funding requirements. The Company will need to raise approximately R87.7bn on the debt capital market without the assistance of Government guarantees. The focus remains on cost effective funding for FY 2014/15 and beyond which implies maintaining its investment credit rating by ensuring gearing and cash interest cover rates are maintained within set limits.

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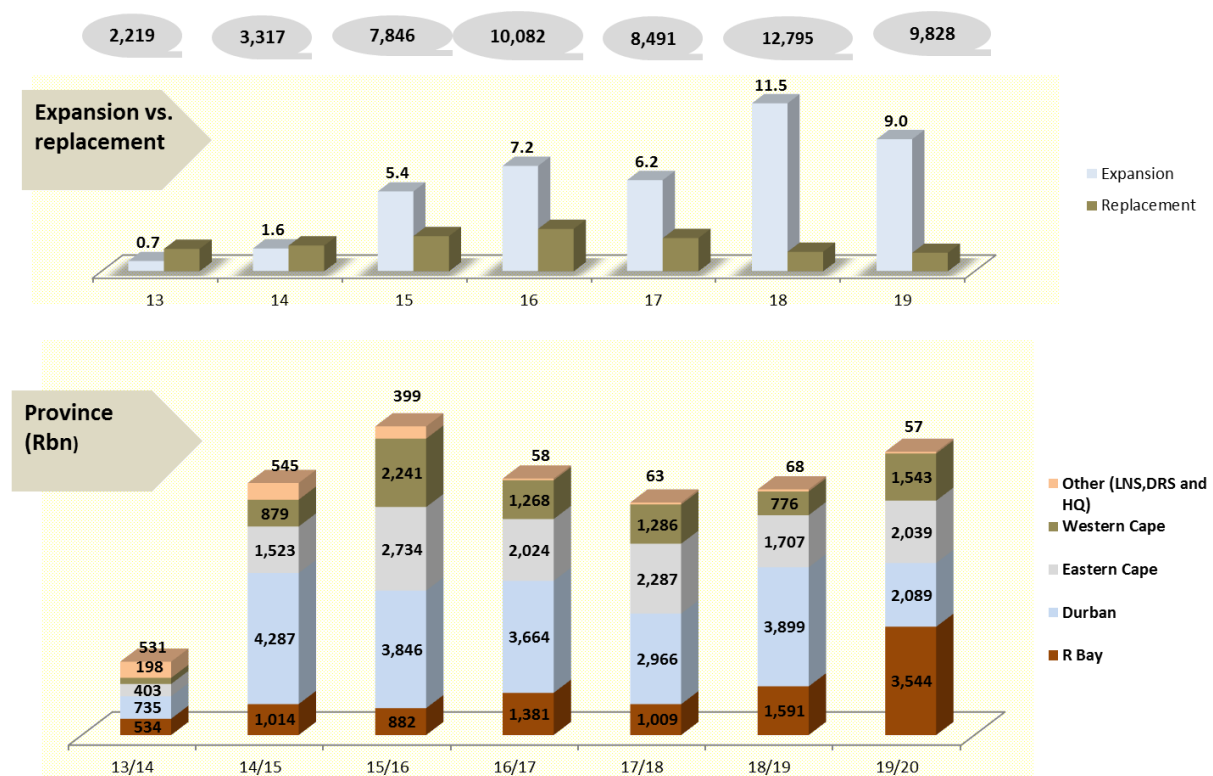
The majority of the MDS's investments will be in general freight and additional capacity across all other commodities. MDS is geared to improve rail connectivity ensuring that the port capacity will not be compromised by less than efficient railway operations.

The Authority is committed to its core strategy which is aligned to the MDS and Shareholder expectations. The Authority's planned investment programme contributes R57.6bn to the Transnet MDS Capex programme. The key pillars of the Authority's core strategy, which are aimed at lowering the cost of doing business and driving growth in the economy, are as follows:

- Create and manage infrastructure capacity ahead of demand;
- Improving port efficiency through increased productivity and operations oversight; and
- To facilitate an integrated logistics chain that will establish the port system as an integrated gateway for trade.

The MDS Capex programme is illustrated in the Diagram as follows:

**Diagram 2: MDS Capex Spend (Revised at September 2013)**



### 4.4 Tariffs in perspective

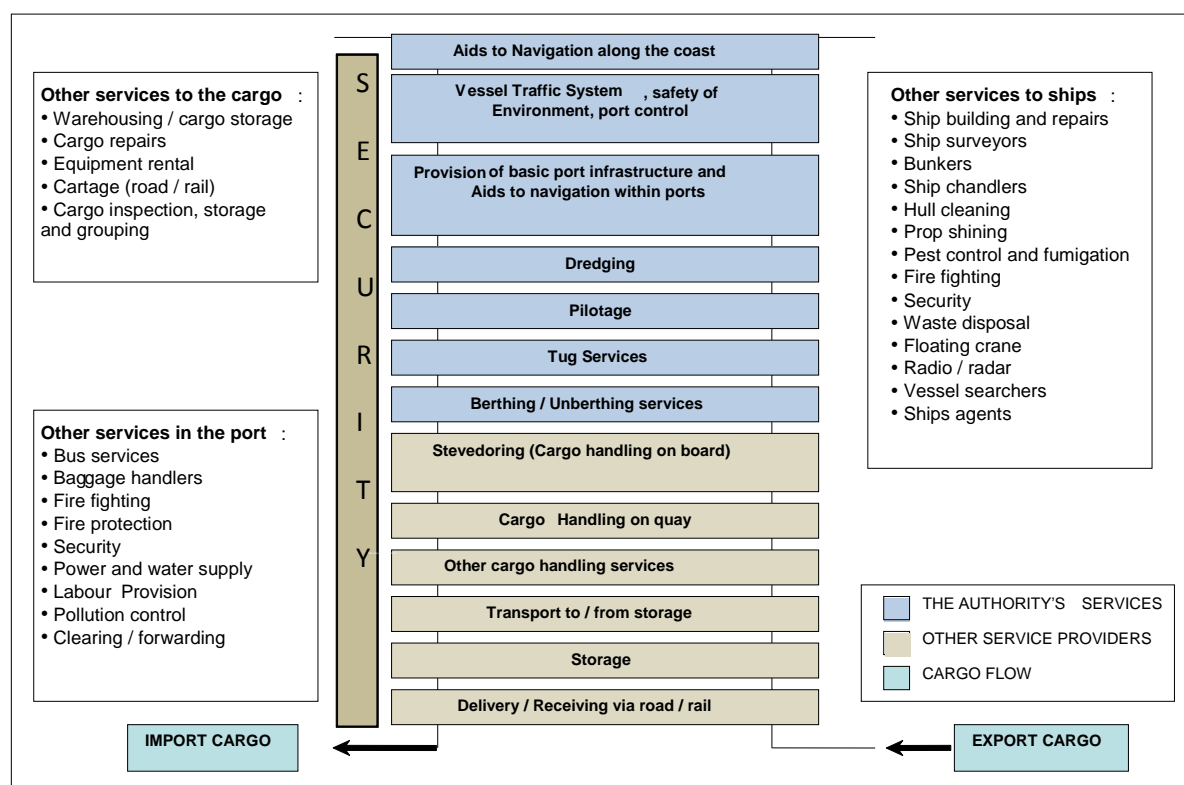
The Authority, like any other port authority, needs to generate revenue by charging tariffs for the services that it renders, and to achieve the aforementioned MDS targets. The Authority may charge fees, in accordance with tariffs approved by the Regulator in order to fulfil the functions it must perform in terms of the Act.

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As a landlord port authority, the Authority's core services, as specified in the Act, result in a number of revenue streams, which are utilised by the Authority to fulfil its responsibility for the safe, efficient and effective economic functioning of the national ports system.

There are various services provided within a port and **Diagram 3: Various Port Services** (adapted from the United Nations Conference on Trade and Development) illustrates the flow of cargo and ships through the port system:

**Diagram 3: Various port services**



The Authority's services at the ports can be divided into two basic groups:

- Basic port infrastructure; and
- Operational services to port users.

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The Authority's services and their respective revenue streams are set out in the table below:

**Table 6: The Authority's Services and Corresponding Revenue Streams**

Port Infrastructure		Revenue Stream
Port land and Terminals	Lease port land to terminal operators and other port service and port facility providers in the port(s).	Lease income (rentals)
Wet infrastructure	Lighthouse services infrastructure (lighthouses, buoys, beacons and electronic / radio navigation equipment) , port control and safety, entrance channels, breakwaters, turning basins, aids to navigation within port limits, vessel traffic services, maintenance dredging within ports.	Light dues, port dues, vessel traffic services fees
Dry infrastructure	Quay walls, roads, rail lines, buildings, fencing, port security, lighting (outside terminals), bulk services and in certain cases terminal infrastructure	Cargo dues, berth dues
Ship repair services	Provide and maintain ship repair facilities as well as the cranes utilised in such facilities.	Preparation fee, docking and undocking fees (vessels at repair facilities), Berth dues (vessels at repair quays)
Marine services	Pilotage, tug assistance, berthing, running of lines, floating cranes	Pilotage dues, tug assistance fees, berthing fees, running of line fees, floating crane hire fees

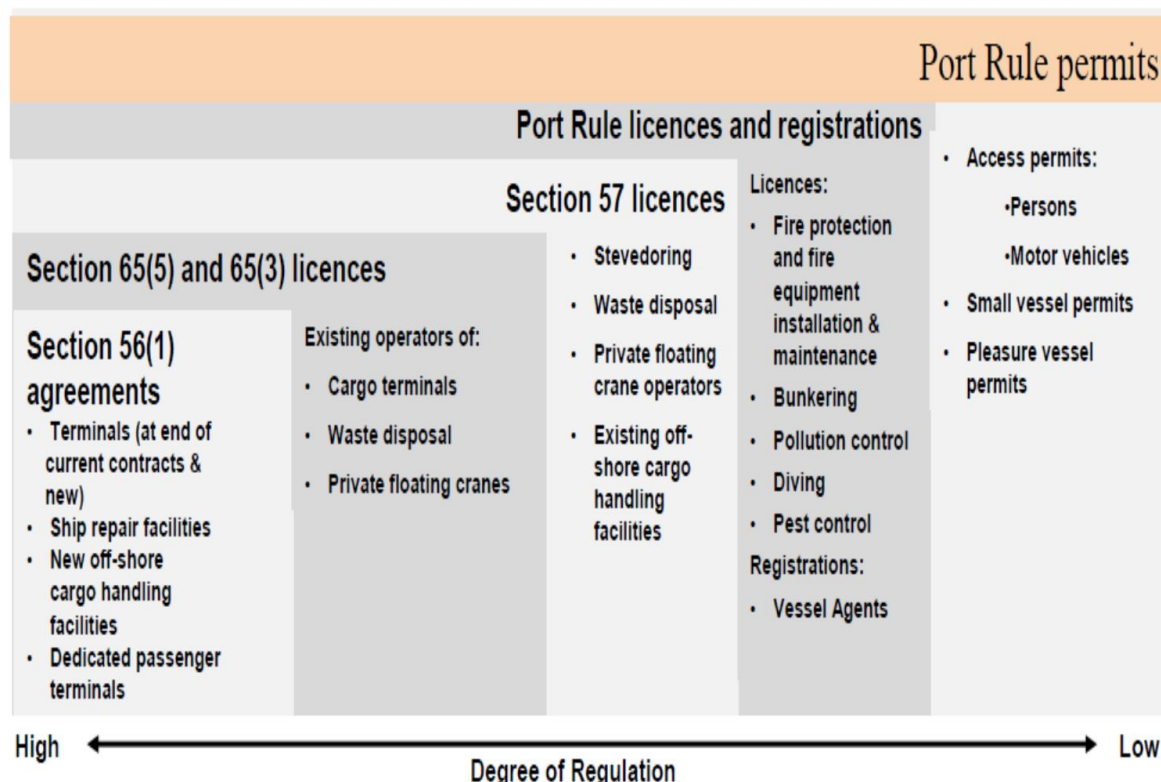
In the context of the South African ports system and the Act, the revenue generated from the Authority's services is utilised inter alia to:

- maintain basic port infrastructure;
- provide current and future port infrastructure;
- maintain and provide the current and future marine fleet; and
- maintain and provide current and future ship repair facilities

This makes the South African port system distinct from most ports internationally, where typically, some port capital costs are funded through State or Municipal budgets. The Authority's Tariff Book sets out the various tariffs that are charged by the Authority to maintain and develop the South African port system (Refer to **Annexure A**).

Apart from the services that the Authority itself renders, the Authority is also the controller of port services and facilities that are provided by others in the ports. The Authority exercises such control in accordance with the provisions of the Act, by means of agreements, licences and permits. The Act and Port Rules issued by the Authority in terms of section 80(2) of the Act and the Authority's Guidelines of Agreements, Licences and Permits (25 April 2008), specify the degree of regulation that is being exercised in this regard. The type of regulation is illustrated in the Diagram that follows:

Diagram 4: Types of Regulation



Section 73(1) (c) and (d) provides that the Authority may charge fees for the granting of concessions and licences and for any services provided by the Authority in the performance of its functions.

## 5. Port infrastructure development plan and capital expenditure required

### 5.1 Port investment planning

Section 11(1) of the Ports Act lists the main functions of the Authority, amongst others, the responsibilities with respect to the provision of port infrastructure:

#### “Functions of the Authority”

11. (1) *the main function of the Authority is to own, manage, control and administer ports to ensure their efficient and economic functioning, and in doing so the Authority must:*

- (a) *plan, provide, maintain and improve port infrastructure;*
- (b) *prepare and periodically update a port development framework plan for each port, which must reflect the Authority’s policy for port development and land use within such port;*
- (c) *control land use within ports, and has the power to lease land under such conditions as the Authority may determine;*
- (d) *provide or arrange for road and rail access within ports;*



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(e) *arrange for such services such as water, light, power and sewerage and telecommunications within ports;*

(f) *Maintain the sustainability of the ports and their surroundings;*

### 5.2 The Authority's capital investment program

The Authority's investment spending is primarily influenced by its detailed strategic initiatives which aim at providing adequate port infrastructure ahead of demand, improve vessel and cargo turnaround; and improve the productive use of assets. The following broad strategies of the Authority are aimed at supporting the MDS and volume growth:

- Improve management and delivery of capital projects :
- Ensure compliance to Project Lifecycle Process (PLP) model;
- Implement Enterprise Programme Management Office (EPMO) to track capital projects;
- Improve capital planning and budgeting processes;
- Improve procurement process to reduce turnaround time;
- Ensure disciplined execution of the capital and maintenance programmes.
- Implement integrated commercial management and integrated capacity planning processes with a total supply chain focus to improve customer service and achieve wider integration of the port system;
- Increase focus on business development;
- Improve land and other asset utilization;

The table below (Strategic Capital Objectives) illustrates the detailed projections for FY 2014/15 which has been included as part of RAB in the Revenue Requirement.

**Table 7: Strategic capital Objectives**

		2013/14	2014/15
		Rm	Rm
<b>Re-engineering, Integration, Productivity and Efficiency</b>	To maximise return on investments by obtaining additional volumes	492	1 267
	To maximise return on investments by improving operating efficiencies	351	683
	To preserve current revenue streams without obtaining additional volumes (ie. revenue protection)	1 037	895
<b>Safety, Risk and Effective Governance</b>	Ensure Safety Optimisation	202	383
	Optimise Business Enterprise Offerings	81	26
	Optimally Satisfy Social Investments (non economic value creating projects)	-	1
	Environmental	3	45
<b>Human Capital</b>	Optimise Human Resources	54	17
<b>Total (excl. borrowing cost)</b>		<b>2 219</b>	<b>3 317</b>

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The Capex for FY 2014/15 has been shared by the Authority and considered by the Port Consultative Committee (PCC). This is in line with the Regulator's decision that the capital programme of the Authority be shared with the PCC's.

Detailed information regarding the Capex programme is contained in **Annexure B**.

## 6. The Authority's Total Revenue

### 6.1 Real Estate Revenue

The Authority has positioned itself as a landlord port authority, managing all fixed assets under its control in a responsible and productive manner.

Real Estate Management is driven by key principles that seek to support the vision of creating a world-class port system in South Africa, that supports the developments goals of our country and the region as a conduit for import and export trade between South Africa and the world. The Authority leases out its limited land to achieve optimum productivity within the ports.

Third party tenants enter into long – term leases to enable them to invest and develop facilities for their operations. Lease premiums are negotiated on a case by case basis and are therefore not reflected in the Authority's tariff book.

A diverse mix of terminal, handling and warehousing facilities have been developed at ports, inter alia: container terminals; automotive terminals; multi-purpose terminals for a variety of commodities; liquid bulk storage and tank farms for storage of products ranging from petrochemicals, oils, chemicals, etc; dry bulk facilities for coal, iron ore, steel, manganese, etc.; cold storage facilities for fruit, fish and other perishables.

Some ports have other significant installations such as Island View's loading and storage facility in the Port of Durban, neighbouring the petroleum refinery and the coal terminal in Richards Bay. The infrastructure invested in such facilities by tenant's amounts to billions of rand, on massive footprints.

The salient details of the Authority's real estate portfolio are summarized in the table below to give a consolidated overview of the portfolio.

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Table 8: Real Estate Salient Features

Salient Features of Real Estate Business	Details
No of Ports	8
Gross Lettable Area	Approx. 27 million m <sup>2</sup>
No of Tenants	750
Total. No of Terminal Operators	89
Vacancy Factor	28%
Average term of Leases	5 - 25 Years
Total Revenue (at March 2013)	R1 771m
Estimated Revenue FY 13/14	R1 974 m
Estimated Revenue FY 14/15	R2 131m
Forecast Revenue Growth	R157m

Real estate business by nature of it being contract driven is not a subject of any tariff increase but is taken into consideration for the determination of the Authority's allowable revenue. This business is driven by a set of functions which are set out in the Act. In line with the Act the Authority must:

- control land use within ports and has the power to lease land under such condition as it may determine;
- ensure that adequate, affordable and efficient port service and facilities are provided;
- exercise licencing and controlling functions in respect of port services and port facilities to be able to perform efficiently
- ensure that any person required to render any port services and port facilities is able to perform efficiently;
- promote the achievement of equality by measures designed to advance persons or categories of persons historically disadvantaged by unfair discrimination in the operation of facilities in the ports environment.

### 6.2 Marine Business Revenue

The Authority generates revenue by providing services to port users, which include terminal operators, shipping lines, ship agents, cargo owners and the clearing and forwarding industry. The main source of revenue is the tariffs which are charged by the Authority for providing the aforementioned services after approval by the Regulator. The tariffs charged are influenced by the expected volume growth which is further influenced by demand and economic outlook.

### 6.3 The Authority's Volumes

The main volume drivers for the Authority are **Cargo** and **Marine services**.

The forecasted volumes are derived from various sources and translated into the Authority's future revenue expectation. The volumes are subjected to intense evaluation during the budget cycle, periodically reviewed and updated when necessary. The Authority gathers cargo volume and vessel forecasts primarily from terminal operators and shipping lines. The volume forecast patterns is

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

influenced by many factors including a volatile global environment. It is important that volume forecasts be reviewed on an on-going basis.

### 6.3.1 Cargo

Growth in cargo volume through the port system is driven largely by both local and global demand and supply. The Authority has various categories of cargo that traverse port infrastructure and therefore generate revenue in the form of cargo dues. Cargo types are categorised according to the manner in which they are handled.

These cargo types are further differentiated between imports, exports, coastwise and transshipments.

- imports are classified as cargo emanating from an international destination destined for South Africa.
- exports are cargo shipped from any South African port destined for an international destination.
- coastwise cargo is cargo emanating from within the borders of South Africa shipped from one South African port and destined to another South African port.
- transshipment cargo is cargo emanating from an international source destined for another international destination (except South Africa), which is handled at a South African port. This cargo could be termed “cargo in transit”.

Other areas having a bearing on cargo volume growth include factors such as modernisation of logistics infrastructure, capacity expansion and supply chain efficiencies which include port efficiencies. This is highlighted in the table below.

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Table 9: Authority's Volume Growth

	Actual	Budget	%	Forecast	%
	FY 2012/13	FY 2013/14	Dev	FY 2014/15	Dev
<b>Containers (TEUs)</b>					
Deepsea Full : Imports	1 420 679	1 416 130	-0.32%	1 469 318	3.76%
Deepsea Full : Exports	978 426	1 027 242	4.99%	1 068 067	3.97%
Transhipments	1 009 406	1 093 636	8.34%	1 131 723	3.48%
Other	994 847	1 073 997	7.96%	1 110 048	3.36%
Total	4 403 358	4 611 005	4.72%	4 779 156	3.65%
<b>Vehicles (Units)</b>					
Vehicles : Imports	385 858	368 436	-4.52%	387 857	5.27%
Vehicles : Exports	272 241	211 747	-22.22%	216 925	2.45%
Other	9 166	12 360	34.85%	12 730	2.99%
Total	667 265	592 543	-11.20%	617 512	4.21%
<b>Break Bulk(Metric tons)</b>					
Breakbulk : Imports	2 144 775	2 184 347	1.85%	1 703 019	-22.04%
Breakbulk : Exports	6 567 036	8 244 725	25.55%	8 889 842	7.82%
Breakbulk : Other	222 124	302 446	36.16%	104 934	-65.30%
Total	8 933 935	10 731 518	20.12%	10 697 795	-0.31%
<b>Dry Bulk (Metric Tons)</b>					
Coal Exports	73 307 314	81 820 000	11.61%	87 930 000	7.47%
Iron Ore Exports	53 597 302	58 965 000	10.01%	60 400 000	2.43%
Manganese Ore Exports	7 451 418	7 750 000	4.01%	7 800 000	0.65%
Other Dry Bulk	20 288 921	20 827 522	2.65%	26 041 882	25.04%
Total	154 644 955	169 362 522	9.52%	182 171 882	7.56%
<b>Liquid Bulk (KI)</b>					
Petroleum	32 115 315	32 007 765	-0.33%	32 619 504	1.91%
Chemicals	1 956 010	1 956 308	0.02%	1 984 753	1.45%
Other Liquid Bulk	7 801 327	8 238 908	5.61%	8 272 953	0.41%
Total	41 872 652	42 202 981	0.79%	42 877 210	1.60%

### 6.3.1.1 Containers

The volume projection for South African ports is estimated at 4 779m TEUs per annum for FY 2014/15. Container sector volumes are influenced by the economic relationship between GDP and trade volumes, exchange rate fluctuations, pricing and fuel prices.

Growth at the South African ports as a whole is threatened by the global headwinds that are posing challenges, namely the eurozone crisis and slowdown in China. However there are positive areas identified for growth as well. These areas are discussed as follows:

- growth in container volumes is forecasted in FY 2014/15 carrying over into FY 2015/16 due to improving household consumption.

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- in addition, strong South African consumer demand will support growth in containerised imports into South Africa which will be boosted by the import of components for a booming automobile production sector and related industries.
- containerised exports will continue to be driven by reefer shipping (significant fruit and agricultural industry) which is exported to Europe and Asia.
- containerised exports will also be driven by containerisation of dry bulk products including minerals and manufactured goods.
- increased infrastructure capacity of transshipments at the Port of Ngqura coupled with discounted rates from both the port authority and terminal perspective will attract transshipments to the SA port system.
- the following two new services which have been introduced by Mediterranean Shipping Company (MSC) will continue into FY 2014/15 which will result in increased transshipments:
  - ✓ Far East to West Africa Service (volumes which used to be transhipped at Valencia port in Europe)
  - ✓ South America to Far East which is a completely new service that MSC has introduced.

Furthermore, there are other factors that will impact on the volume of container imports and exports, including increased port infrastructural capacity, increased liner capacity and new business. A unit responsible for new business development has been set up in an attempt to develop markets that will ultimately lead to growth in transshipment volumes, in particular at the Port of Ngqura.

The projected rise in consumer spending will support growth mainly in container imports. The automobile production sector has also improved the imports of containers. Fruit exports to Asia from South Africa are also growing. Although the export of coal and iron ore is primarily undertaken through dry bulk activities, there is a global trend for more traditional dry bulk commodities to be transported in containers, thereby taking advantage of the intermodal links offered by containers.

In terms of the Authority's Marketing Strategy, the Port of Ngqura has been positioned as a preferred transshipment hub for the Sub Saharan Region. With the objective of attracting transshipment volumes to the Port of Ngqura, the Authority jointly with the terminal embarked on a "Go to the Market" strategy, culminating in visits to various customers internationally and locally. The MSC has responded on this strategy.

In December 2012, MSC shifted its service for cargo moving from Far East to West Africa, which had been transhipped at the Port of Valencia, to the Port of Ngqura. MSC is also committing to introduce an additional service from South America to the Far East via Ngqura which will bring additional transshipment volumes of +/-200,000 TEUs at the Port of Ngqura.

### 6.3.1.2 Automotive

The South African Automotive industry contributes around 6.8% to the GDP of the South African economy. It creates direct employment for 28 000 employees in the manufacturing sector while over 260 000 employees are in the components and retail side of the industry. However in terms of

global production, South Africa contributes less than 1% which is evident in the projections over the different periods. Growth has remained conservative, mainly due to South African exports being largely dependent on the state of global markets such as Europe and United States, facing slow and/or no growth after the economic recession. However, there exists optimism that the recently implemented Automotive Production Development Program (APDP which replaced the MIDP), will encourage and motivate local manufacturers to increase production resulting in increased export volumes.

#### **6.3.1.3 Coal**

Global demand for coal is increasing more than any other energy source. In years to come China and India's increase in coal imports will account for more than a third of the predicted increases in global energy demand hence the projected volumes will cater largely for these countries. Major mines are working on expansions of their facilities to be able to meet demand.

RBCT and Transnet Freight Rail are negotiating a 3Mtpa rail allocation for new entrants; RBCT is planning a further ramp-up of up to 110Mtpa depending on rail ramp-up. The Authority is working on the 3Mtpa short term capacity which is aimed at assisting junior miners. This would result in increased volumes for the Authority.

#### **6.3.1.4 Iron Ore**

South African Iron Ore contributes 4% to the global iron ore market. In order to retain and grow the industry, Transnet embarked on an iron ore expansion project to increase capacity on the supply chain to meet customer demand. In support of this, volume projections over the respective period are aligned to the contractual arrangements between Iron ore customers and Transnet. Until completion of Phase 2A, export capacity through the Bulk Terminal in Saldanha will be 58.5Mtpa, which excludes the 1.5Mtpa domestic volumes to the beneficiation plant in Saldanha, thereafter capacity will increase. As per the projections, the ramp up is expected to take the channel capacity to 65Mtpa and 82Mtpa respectively in FY 2018/19 and FY 2019/20 respectively.

#### **6.3.1.5 Manganese Ore**

Currently, the local industry is expanding with new role players being allocated capacity on rail and port infrastructure. The majority of volumes are being shipped through Port Elizabeth which is faced with certain constraints. All role players are making concerted efforts to achieve a throughput in excess of 5 million tons per annum, with current available capacity of 5.5Mtpa at the bulk terminal at the Port of Port Elizabeth. Additional capacity has also been created at the Port of Port Elizabeth through the skiptainer operation, with expected volumes of 0.5Mtpa.

In addition to Port Elizabeth, customers supplement volumes by exporting through Bulk Connections in the Port of Durban. Industry demand exceeds current port capacity, but with the relocation of the Manganese Terminal from Port Elizabeth to Ngqura, capacity will substantially increase to 8.0Mtpa and then 16Mtpa by FY 2017/18 and FY 2018/19 respectively.



### 6.3.2 Marine Services

Marine volumes comprise of the number of ships arriving at South African ports and their associated Gross Registered Tonnage (GRT). The size of the vessel and the number of days spent in the port dictates how much the shipping lines will pay for utilising basic port infrastructure and marine services operational charges, i.e. tugs, berthing and pilot assistance.

## 7. Tariff Application Approach

The Authority remains firmly of the view that the tariff methodology and approach to determine components thereof, as captured in its tariff methodology position paper described in **Section 3.3** above, is most appropriate for tariff determination purposes. The proposed methodology addresses the financial sustainability of the Authority especially during the critical years of the Transnet MDS which aims to address the needs of customers. Even though the Regulatory Manual is based on the revenue required methodology (called upon by the Authority in its position paper) the approach in determining the components differs in comparison to the Authority's proposal. The Authority retains its approaches as captured in its proposal. Therefore whilst the tariff application FY 2014/15 has been prepared on the basis of the guidelines contained in the interim Regulatory Manual, this is with the understanding that Authority's tariff methodology position paper is still under review by the Regulator.

### 7.1 Revenue Requirement Determination

The revenue requirement formula as per the manual provides a standard building block approach for setting of the required revenue. The formula as prescribed is as follows:

*Revenue Requirement*

*= Regulatory Asset Base (RAB)*

*X Weighted Average Cost of Capital (WACC) + Operating Costs*

*+ Depreciation + Taxation Expense – (+) Claw back*

*+ (-) Excessive Tariff Increase Margin Credit (ETIMC)*

The application of this formula is demonstrated in the following sections:

#### 7.1.1 Regulatory Asset Base (RAB)

The Authority is responsible for the management of the South African national ports system. The Authority owns, develops and maintains port land infrastructure.

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

Table 10: Regulatory Asset Base

	FY 2014/15
	Rm'
Opening Net Book Value (NBV)	63 120
NBV inflated	66 844
less Depreciation	-1 671
add Capex	3 317
Add inflation for half FY Capex	-
closing NBV	68 490
Average Opening and Closing	65 805
Less Working Capital	-1 111
RAB Final	64 694

### 7.1.1.1 Asset base

The RAB allowed by the Regulator to earn a return in the tariff methodology involves all assets of the Authority. The real difference between the Authority and the Regulator on the determination of RAB will be those assets that the Regulator has decided not to allow a return upon (e.g. Durban International Airport assets).

The Regulatory Asset Base of the Authority has been trended using the South African Reserve Bank (SARB) inflation indicator.

The steps taken to calculate the RAB is illustrated below.

- In order to determine the value of the RAB on which a return will be calculated in the allowed revenue formula, both the closing and opening values of the RAB including capital expenditure are averaged throughout the period. This is to recognise availability of and also incurrence of capital expenditure throughout the whole financial year rather than on the first day of the financial year.
- The formula for the determination of value to be allowed in RAB for the period under review,  $y$ , is as per **Diagram 1** on Page 13.

### 7.1.1.2 Depreciation

The depreciation of the assets in the RAB will be calculated as straight line, 40 year depreciation on the opening balance of the RAB ( $RAB_{O,y}$ ). The resultant depreciation is R1 671m.

### 7.1.1.3 Inflation trending

In the Revenue Requirement methodology, it is a requirement to inflate the Asset base as the Real WACC is being applied. SARB average inflation figure of 5.9% (i.e. reference to BER inflation forecast) has been used in the RAB calculation.

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### 7.1.1.4 Capital Work In Progress (CWIP) / Capital Expenditure (CAPEX)

CWIP refers to assets that are under construction. Such construction ties up scarce capital and port facilities which typically take between 24 and 36 months to construct. In order to arrive at the complete required return on assets, a return on CWIP must be included in the Revenue Requirement, as the construction of these assets must be financed. CWIP/CAPEX is informed by the Capex program which for FY 2014/15 is R3.3bn.

### 7.1.1.5 Working Capital

As per the Regulatory Manual, working capital is determined as follows:

**Table 11: Working Capital**

Indexation as per Regulatory Manual	AFS 2012/13	Indexation	FY 2013/14 Rm'	Indexation	FY 2014/15 Rm'
<b>Current Assets</b>	2 290		<b>2 290</b>		<b>2 432</b>
Trade Receivables (31 day 2010/11 Revenue)	2 247	2.50%	2 303	3.50%	2 384
Inventories at 2010/11 YE	43	5.40%	45	5.90%	48
<b>Current Liabilities</b>	3 037		<b>3 037</b>		<b>3 543</b>
Trade Payables	2 109	5.40%	2 223	5.90%	2 354
Vat Liability	928	5.40%	978	5.90%	1 036
Capex			-		153
Working Capital					-1 111
Trade Receivables indexed by Volume growth					
All other components indexed by inflation					
* Capex is difference from FY 2014/15 and 2013/14 (The difference divide by 12 months plus VAT at 14%)					

### 7.1.2 Weighted Average Cost of Capital (WACC)

A Vanilla WACC is used in this application (refer to **Annexure C** for a full explanation on the calculations of the WACC) with the key components contained in the table that follows:

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

Table 12: Weighted Average Cost of Capital (WACC)

	FY 2014/15
	Rm'
Risk-free rate (nominal)	8.32%
<i>Real risk free rate</i> <sup>1</sup>	2.29%
MRP <sup>2</sup>	7.10%
Asset beta	0.5
Equity beta (using Hamada)	0.86
Gearing	50.00%
WACD (nominal)	9.34%
Inflation <sup>3</sup>	5.90%
Tax rate	28.00%
Cost of equity (real)	8.40%
WACD (real, pre-tax)	3.25%
	<b>5.83%</b>

### 7.1.3 Taxation

The Revenue Requirement formula considers tax expense to be a pass-through cost. When the Vanilla WACC is applied to the average RAB for the period under review, the WACC will not include the cost of debt as it is a pre-tax determination. The calculation for tax is illustrated below:

<sup>1</sup> R186 SA Government Bond (10.5% Coupon Bond, Issued February 2002 and Expiring on 21/12/2025, 21/12/2026, 20/12/2027)

<sup>2</sup> Dimson, Marsh and Staunton (Credit Suisse Global Investment Returns Source Book 2013)

<sup>3</sup> Bureau of Economic Research (BER) forecast for 2014 (in June 2013)

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

Table 13: Tax Calculation

	FY 2014/15
	Rm'
<b>Gross income</b>	8 717
Pre Tax debt return	-
Equity Return on RAB	2 717
ETIMC	-
Opex	4 329
<b>Deductions</b>	
Depreciation	1 671
Opex	4 329
<b>Taxable income</b>	2 717
Gross up for tax	3 774
Tax at 28%	1 057

### 7.1.4 Operating Costs

The Authority's operating expenses are accounted for in terms of the organisations' best estimate of forecast expenditure and also taking into account delivery of MDS.

The Authority is a landlord port authority and therefore its operations are capital intensive. Consequently, most of the Authority's operating costs are of a fixed nature.

This section provides an analysis of the Authority's material operating expenditure items as shown in the table below with full details of Opex is provided in (**Annexure C**):

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

**Table 14: Operating Cost Including Group Overheads**

	Actual 2012/13 R Million	Budget 2013/14 R Million	Forecast 2014/15 R Million	Deviation R Million 2013/14 VS 2014/15	Deviation % 2013/14 VS 2014/15	% of Operating Cost 2014/15
Labour Costs	1 472	1 781	1 943	162	9.1%	52.0%
Rates & taxes	193	250	264	14	5.6%	7.1%
Maintenance	276	355	367	12	3.5%	9.8%
Contract Payments	57	65	68	3	4.5%	1.8%
Energy	353	445	485	40	9.1%	13.0%
Professional services	13	37	39	2	4.7%	1.0%
Material	75	97	94	(4)	-3.7%	2.5%
Computer & Info systems	64	81	86	4	5.5%	2.3%
Rental	52	60	68	8	13.5%	1.8%
Security costs	51	68	73	5	6.9%	2.0%
Research & development	32	82	72	(11)	-12.8%	1.9%
Sundry operating costs	104	215	179	(36)	-16.9%	4.8%
Total operating cost (excluding depreciation)	2 742	3 537	3 738	201	5.7%	100.0%
Group Costs	367	653	591	99	19.1%	100.0%
Total operating cost (Including Group Costs)	3 109	4 190	4 329	139	3.3%	100.0%

### 7.1.5 Revenue Claw back

Realised revenues in any given year could deviate from revenues allowed by the Regulator for that same year if realisation of volumes, expenses, etc. does not match the forecasts. Such deviations would represent either an over-recovery or under-recovery of required revenues. Either scenario would call for some form of ex post adjustment to the Authority's allowed revenues.

The key purpose of applying claw back is to ensure that the Authority does not gain or lose out from discrepancies between forecasts made at the time of the tariff application and actual figures on the realisation of capital expenditure, operating expenditure, depreciation, taxation and volume. With these considerations in mind, the value of any claw back for over-recovery or under-recovery of revenues as presented for year y may be calculated as:

$$C_y = \Delta AR_{y-2} - IC(1 + WACC_{y-1})(1 + WACC_{y-2}) \quad \text{Where,}$$

- $C_y$  = the value of the claw back to correct for the effect of outturn revenues over a period of two tariff determinations.
- $\Delta AR_{y-2}$  = is the difference between actual revenues observed in year y-2 and the revenues that the Regulator ought to have set in that period, had it enjoyed perfect foresight over volumes, expenses, tax obligations and depreciation (i.e. the elements of allowed revenues for which it is possible to observe ex post values after the fact);
- IC = the Interim Claw back (50%) as determined by Ports Regulator
- $WACC_{y-1}$  and  $WACC_{y-2}$  are the rates of profit allowed to the Authority over review periods y-1 and y-2, respectively. Differences between forecasts and actuals for y-2 are compounded forward two periods within the claw back to account for the approximate time value of money over these years.

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The claw back relating to financial year FY 2012/13 has been calculated with the benefit of hindsight to determine the true over-recovery of revenue using the proposed methodology.

Given that FY2012/13 has ended and the revenue earned by the Authority is known, the final calculation of claw back for the financial year equates to R525m. With R447m having been taken as part of tariff determination 2013/14 the residual clawback to be returned to customers is R78m.

The approach used in the calculation was to re-determine the revenue requirement given the full information on actual Capex spending, operating expenditure and depreciation. The FY 2012/13 Revenue of R9 058m reflects the actual revenue earned (i.e. R 8 329m) in the FY 2012/13 annual financial statements but reversing the claw back provision of R729m previously created. The calculation of claw back is as follows:

- Revenue of R 9 073m is the composition of the return on RAB as allowed by the Regulator in FY 2012/13 (R57bn), vanilla WACC of 6.13% and depreciation of R1.4bn. Operating expenditure is confirmed from the Annual Financial Statements (R3.1bn) and Tax is recomputed as a pass-through cost on vanilla WACC (R950m). This gives the recalculated revenue requirement for FY 2012/13 of R9 073m illustrated as follows:

**Table 15: Re-calculation of revenue requirement for clawback purpose**

	FY 2012/13	FY 2012/13
	Rm'	Rm'
RAB	57 779	
WACC	6.13%	
Return		3 542
Opex (AFS 2012/13)		3 109
Depreciation		1 472
		8 123
Plus Tax		950
		9 073

The recalculated revenue requirement of R9 073m less the claw-back of R1 440m already taken in the previous year is added to the ETIMC of R900m resulting in recomputed allowed revenue of R8 533m. This allowed revenue compared to the actual revenue of R9 058m gives rise to a recalculated claw back of R525m which, less the provisional claw back taken in FY 2013/14 of R447m, leaves a remainder of R78m. This remainder of the claw back will earn a return equivalent to the WACC approved.

The recalculated revenue requirement for FY 2012/13 is calculated as follows:



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**Table 16: Claw back calculation FY2012/13**

<b>Actual Clawback FY 2012/13</b>	<b>Rm'</b>
Revenue Requirement (FY 2012/13)	9 073
Clawback taken	-1 440
<i>Act Mar'11 Clawback calculated</i>	874
<i>Clawback Estimated Mar'12</i>	566
ETIMC	900
	8 533
2012/13 AFS Revenue	9 058
	<b>-525</b>
Add balance of Act Mar'12 PER ROD	
Final Clawback Mar '13	-525
Provisional taken in ROD 13/14	447
Residual Clawback March 13	<b>-78</b>

The claw back provision for FY 2013/14 is based on the latest estimate of revenue to be earned up to the end of the financial year as compared to what the Regulator has allowed in the FY 2013/14 ROD. The latest estimate of the Revenue to be earned in FY 2013/14 is R 9.4bn compared to R9.8bn allowed in the ROD for FY 2013/14. This gives a clawback of R400m, half of which should be taken in FY 2014/15 as per the Interim Regulatory manual.

**Table 17: Claw back estimation FY2013/14**

<b>Estimate Clawback FY 2013/14</b>	<b>R'm</b>
Allowed Revenue per ROD 13/14	9 838
Latest Estimate 13/14	9 437
Estimated Clawback 13/14	401
@ 50%	201
Total clawback to be recovered March 2015	
Residual Clawback o/s Mar'13	-83
Guestimate Mar'14	201
Net Clawback	<b>118</b>

### 7.2 Revenue Requirement

The application of the methodology using the respective components described above is illustrated in the table below:

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**Table 18: Revenue requirement**

	<b>FY 2014/15</b>
	<b>Rm'</b>
<b>RAB</b>	64 694
Real Post WACC	5.83%
Return on Capital	3 772
Plus: Depreciation	1 671
Plus: Operating Expense	4 329
Plus: Taxation Expense	1 057
Plus: Clawback	118
Revenue Requirement	10 947
Less: Real Estate	-2 113
Marine Revenue	8 834

Application of the formula results in a revenue requirement of R10 947m comprising of Real Estate business revenue of R2 113m and Marine business revenue of R8 834m. In order to determine Marine Business revenue to be derived from tariff adjustments, the required revenue of R8 834m is compared with the expected revenue of R7 462m for FY 2013/14 increased for the expected growth in volumes of 3.5% for FY 2014/15.

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Table 19: Authority's Average Volume Growth

	Volumes: Budget 13/14	Revenue : Tariff Book Budget 13/14 R million	Volumes : Increase Projection 14/15	Revenue : Volume increase before Tariff Increase Projection 14/15 R million	Volumes: Total Projection 14/15	Revenue : Before Tariff Increase Projection 14/15 R million
<b>Containers TEU's</b>						
Deepsea Full : Imports	1 416 130	2 643	53 189	99	1 469 318	2 742
Deepsea Full : Exports	1 027 242	631	40 825	25	1 068 067	656
Transshipments	1 093 636	83	38 088	3	1 131 724	86
Other	1 073 997	49	36 050	2	1 110 046	50
<b>Total Container (TEUs)</b>	<b>4 611 005</b>	<b>3 406</b>	<b>168 151</b>	<b>129</b>	<b>4 779 156</b>	<b>3 535</b>
<b>Vehicles (Units)</b>						
<b>Import summary:</b>						
Vehicles : Imports	368 436	464	19 421	26	387 857	490
Vehicles : Exports	211 747	81	5 178	2	216 925	83
Other	12 360	0	370	0	12 730	0
<b>Total Ro-Ro ( Units)</b>	<b>592 543</b>	<b>546</b>	<b>24 969</b>	<b>28</b>	<b>617 511</b>	<b>574</b>
<b>Breakbulk (Metric Tons)</b>						
<b>Import summary:</b>						
Break Bulk: Imports	2 184 347	89	(481 328)	(16)	1 703 019	73
Break Bulk : Exports	8 244 725	198	645 117	13	8 889 842	211
Other	302 446	3	(197 512)	(3)	104 934	1
<b>Total Breakbulk (Tons)</b>	<b>10 731 518</b>	<b>291</b>	<b>(33 723)</b>	<b>(6)</b>	<b>10 697 795</b>	<b>285</b>
<b>Dry Bulk (Metric Tons)</b>						
<b>Import summary:</b>						
Dry Bulk: Imports	8 202 579	143	1 302 873	24	9 505 452	167
Dry Bulk : Exports	161 159 943	705	11 506 487	51	172 666 430	756
Other	-	-	-	-	-	-
<b>Total Dry Bulk (Tons)</b>	<b>169 362 522</b>	<b>848</b>	<b>12 809 360</b>	<b>75</b>	<b>182 171 882</b>	<b>924</b>
<b>Liquid Bulk (Kl)</b>						
<b>Import summary:</b>						
Liquid Bulk: Imports	31 613 816	376	489 463	7	32 103 279	383
Liquid Bulk : Exports	3 824 774	93	196 383	3	4 021 157	96
Other	6 764 390	91	(11 616)	(0)	6 752 774	91
<b>Total Liquid Bulk (Kilo litres)</b>	<b>42 202 981</b>	<b>560</b>	<b>674 229</b>	<b>9</b>	<b>42 877 210</b>	<b>569</b>
<b>Cargo Dues Revenue</b>		<b>5 650</b>		<b>236</b>		<b>5 886</b>

Table 20: Revenues related to volume growth

	Revenue Budget ( Nil % tariff increase) 2013/14 R million	2014/15 Weighted Average Revenue Volume Increase %	2014/15 Revenue: Volume Increase R million	2014/15 Revenue: Before Tariff Increase R million
<b>REVENUE</b>				
Containers	3 406	3.8%	129	3 535
Break Bulk	291	-2.1%	(6)	285
Dry Bulk	848	8.9%	75	924
Liquid Bulk	560	1.7%	9	569
Automotive	546	5.1%	28	574
<b>TOTAL CARGO DEUS AFTER REBATE</b>	<b>5 650</b>	<b>4.2%</b>	<b>236</b>	<b>5 886</b>
Marine & other revenue	1 812	1.2%	22	1 834
<b>TOTAL TARIFF BOOK REVENUE</b>	<b>7 462</b>	<b>3.5%</b>	<b>258</b>	<b>7 720</b>
Real estate revenue	1 975	7.8%	154	2 128
<b>TOTAL REVENUE</b>	<b>9 437</b>	<b>4.4%</b>	<b>412</b>	<b>9 848</b>

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This translates into an average tariff adjustment of 14.39% for FY 2014/15.

**Table 21: Marine Revenue**

Marine Revenue	Rm'
Latest Estimated Revenue for FY 2013/14	7 462
Estimated Volume Growth for FY 2014/15	3.50%
	7 723
FY 2014/15 Required Revenue	8 834
Tariff Increase	14.39%

The roll-out of the Authority's CAPEX programme in terms of the MDS will result in spikes and troughs for future tariff adjustments when applying the Revenue Requirement formula. The Authority's projection of future tariff adjustments (beyond FY 2014/15) using similar parameters for FY 2014/15 will range between 7.0% and 12.89% per annum. In the last tariff application for FY 2013/14, the Authority commenced with discussions on a multi-year tariff application approach which would assist with smoothing the tariff trajectory. This approach would result in a smoothed tariff increase of 9.70% from FY 2015/16 to FY 2018/19. However, the Regulator is yet to make a decision on this approach.

Whilst the Authority understands its role in facilitating economic growth by providing infrastructure as part of the market demand strategy it is also mindful that our customers are battling through a depressed global economy. The Authority, together with Transnet, has undertaken various financial sustainability assessments with the objective of containing the cost of doing business in South Africa. The Authority has therefore considered a route to ensure a sustainable tariff increase which is in the interest of the economy. As the Authority is still in the establishment phase of the Transnet MDS execution plan, its cash flow requirements could be sustained with a marine business cash revenue base of R8 380m for FY 2014/15.

### 7.3 Excessive Tariff Increase Margin Credit

The Regulator regulates in the long term interest of the industry. This requires that the Regulator not only confine itself to the immediate tariff decision, but also consider ways to ease any future shocks to the system that are capable of being managed sustainably within the space that is available for such intervention. As such, the Regulator considered it prudent based on past tariff determinations to retain an Excessive Tariff Increase Margin Credit (ETIMC) inside of the Authority to offset against future large, but justified, tariff increases resulting from the capital expenditure spikes envisaged, but not as yet articulated to a level of detail and phasing that allows accurate prediction. In the FY 2012/13 decision, the Regulator retained R900 million of the claw back in the ETIMC. The ETIMC retained for the FY 2013/14 is R378m.

Whilst the application of the Regulatory Manual results in a Marine Business revenue requirement of R8 834m for FY 2014/15, the Authority could sustain a Marine Business cash revenue of R8 380m. Therefore the Authority applies to the Regulator to release R454m of the ETIMC provision held within the entity.

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ETIMC is a component of the revenue requirement formula of which the decision on the revenue allowed is decided on by the Regulator. ETIMC represents the revenue that is allowed to the Authority in anticipation of the capital expenditure to be incurred in the future; as a result the ETIMC attracts a cost equivalent to the WACC approved by the Regulator which the Authority is expected to payback in the future.

The revenue allowed in the revenue requirement formula (i.e. including the ETIMC portion of the approved revenue) attracts tax at 28%. Although taxation expense is treated on a pass-through approach basis, the “notional portion” of tax expense on the ETIMC payable and due to the receiver of revenue is not allowed to the Authority by the Regulator. The Authority will not request for the notional tax expense on the ETIMC to be allowed in the required revenue as it will inflate the bill for the port users. Therefore the Authority furthermore proposes that it be exempted from incurring a finance cost equivalent to the vanilla WACC on that portion of the ETIMC that is equivalent to the notional tax on the ETIMC.

### 7.4 Tariff Application

Application of the tariff methodology guided by the Regulatory Manual and with the proposed release of R454m from past ETIMC provisions translates to a tariff adjustment of 8.5% as follows:

**Table 22: Required revenue post ETIMC**

Marine Revenue	Rm'
Marine Revenue Required	8 834
Less ETIMC	454
Marine Revenue for FY 2014/15	8 380

For the FY 2014/15 , the Authority therefore applies to the Regulator for a revenue of R10 493m comprising marine business revenue of R8 380m and real estate business revenue of R 2 113m. This translates to an average overall tariff adjustment of 8.5%.

**Table 23: Marine Revenue based on 8.5% increase**

Marine Revenue	Rm'
Latest Estimated Revenue for FY 2013/14	7 462
Estimated Volume Growth for FY 2013/14	3.50%
	7 723
FY 2014/15 Required Revenue	8 380
Tariff Increase	8.5%

Translation of this marine revenue of R8 380m into individual tariffs (tariff book) will be informed by the Regulator guideline which will be issued post the tariff determination process.

## 8. Tariff Book

The Authority has previously acknowledged concerns with the current tariffing regime and embarked on developing a pricing strategy that is principle based and regulatory compliant whilst integrating common practices. Through the development of this strategy the following key issues related to the current tariff structure have been confirmed:

- Lack of a clear set of principles and rules to be applied in determining the individual tariffs for the various services and facilities;
- Lack of clarity and transparency regarding all operating costs, expenses and revenues incurred or generated from a specific service or facility, as well as the value of the capital related to such services or facilities;
- Lack of explanation for differential tariffs for different commodities using the same handling classification;
- Lack of information and detail with respect to services' or facilities' pricing and cost relationships, making it impossible to determine where and in which direction subsidisation takes place or if it does not;
- Lack of information on how the tariff structure promotes access to ports and efficient and effective management and operation of ports.

Furthermore, the Real Estate business of the Authority has until recently been excluded from the tariff structure, which therefore led to the tariff structure not encompassing the entire business of the Authority. As a result of this, the current tariff structure presents several imbalances in the determination of the various tariffs, including:

- High tariff levels for cargo dues resulting from the migration from the old wharfage charge, which was calculated on an ad-valorem basis (depending on the value of the cargo);
- High differentials in the levels of cargo dues for different cargo types and commodities with no clear motivation for the differences;
- Low tariff levels for maritime services, which are based on an activity-based costing exercise conducted during the tariff reform of 2002 that has since not been updated, resulting in the subsidisation of some services;
- Lower levels of revenue from the Real Estate business as compared to other landlord port authorities across the world.

The new proposed tariff structure, premised on the Revenue Requirement methodology, aims at addressing these imbalances by providing a set of clear principles and rules, to determine the optimal levels for the various tariffs. Moreover, the new structure also represents a step forward towards the promotion of efficient and effective management and operation of ports thereby supporting the country's economic growth objectives.

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Under the current tariff structure, cargo owners are bearing the burden of port charges. The current split of the Required Revenue by port user group cannot be soundly defended, as it is not based on a clear allocation of assets.

The proposed tariff structure means that terminal operators will pay higher rentals that are more in line with international norms; cargo owners will pay lower cargo dues, also more in line with international norms; and shipping lines will pay slightly higher tariffs. Based on the application of the design principles, the proposed tariff structure presents the most balanced and defensible distribution of Required Revenue across port user group. The success of achieving the higher Real Estate revenue is critical for the successful implementation of the pricing strategy.

The Authority has shared its pricing strategy with the Regulator in September 2012. The Ports Regulator held a consultation process with stakeholders during April 2013 and solicited written comments up until end of May 2013. The Authority has been informed through the regulatory manual that for the 2014/15 tariff application the Regulator will provide the Authority with the guidelines for the amendment of the 2014/15 tariff book. This guideline is planned to be issued after the overall tariff has been determined in response to this application. It will provide general rules on the allocation of costs and tariff adjustments to be included in the overall tariff book amendments.

## 9. Port Efficiency

The National Ports Act No 12 of 2005 (the Act) mandates the Authority to improve port efficiency, productivity and overall performance as well to exercise the necessary oversight associated with such improvement. The Authority recognises the need for port efficiency and productivity to precede capital expansion and new capital development. In light of the aforementioned, the Authority has been repositioned through a comprehensive operations strategy which is defined by three broad spheres, namely:

1. port performance monitoring,
2. implementing the Authority's mandate at port level and
3. Optimisation of existing port capacity.

The Authority has adopted a holistic port supply chain approach to addressing the improvement of port efficiency, productivity and performance. This approach emphasises the flow of cargo and vessels in accordance with operations schedules based upon predetermined levels of productivity.

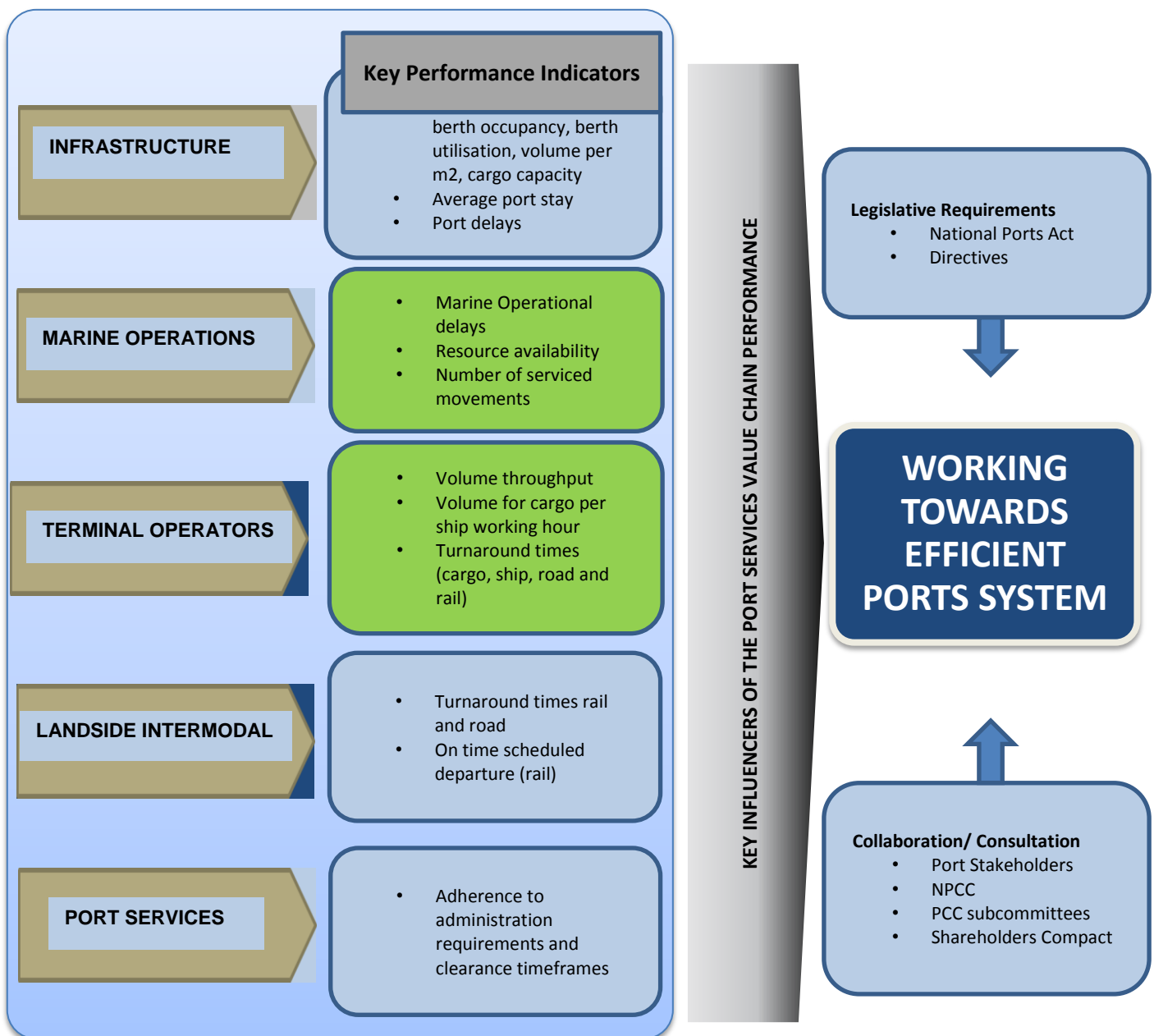
Within this approach, the Authority will concentrate on improving port efficiency, productivity and performance within the specific areas shown in **Diagram 5**. The Authority has prioritised the improvement of terminal operator performance through the issue of Terminal Operator Performance Standards (TOPS) for all 90 licenced terminal operators at South African ports. TOPS is heralded as an inaugural and comprehensive instrument that establishes the expected levels of productivity and performance at port terminals in consultation with terminal operators, port users and stakeholders. TOPS is informed by factors such as terminal capacities, demand and commercial arrangements, amongst others. The Authority will assess performance against TOPS at quarterly intervals with a view towards achieving and maintaining expected performance.

The Authority is currently in the process of establishing performance norms for the remaining areas to ensure performance coverage of the port supply chain. In order to achieve the above objectives, the Authority has improved its institutional capability by appointing Senior Operations Managers at all ports and per port precinct in Durban. The creation of Port Operations Centres to track and monitor elements of port performance is on track and continues to demonstrate the Authority's commitment towards the improvement of port efficiency, productivity and performance.



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Diagram 5: Focal Area for port efficiency, productivity, and performance improvement



**Diagram 5** provides the focal areas for efficiency, productivity, and performance improvement, which are discussed below.

## **9.1 Marine Operations Management Oversight**

The Authority is committed to ensuring a seamless service is provided to vessels entering or exiting South African ports.

This will include a process of stringent monitoring and measurement of the causative factors, which could result in ships being delayed due to Pilotage, Tugs or Berthing Services (which are under the direct control of the Authority). Approved targets have been set for each of the aforementioned categories and are monitored at various managerial platforms.

### **9.1.1 Pilotage**

Pilotage delays are caused due to pilot license restrictions or the pilot being occupied with other shipping at the required service time.

In order to reduce the abovementioned type of delay the following initiatives are currently being implemented:

- On-going focus of ensuring that pilots are qualified to higher license levels (up to open license) thereby ensuring an appropriate spread of experience across all shifts; and
- On-going proficiency training which will include simulator training as well as in class training sessions.

The Authority currently offers pilotage via helicopters at the ports of Durban and Richards Bay. An external service provider has been operating the Authority's helicopter service since 1995. For the past 18 years, no capacity building was undertaken in this area of expertise and the Authority has no pilots and engineers to man this operation. The Authority has taken a decision to develop capacity in this area and the helicopter service is expected to be insourced within the next 36 months. The fully integrated service will further strengthen Authority's internal controls and create opportunities for growth and development of previously disadvantaged individuals.

The first phase of this project commenced in the second half of 2012/13 and aims to develop human capacity in this area through a skills development programme. A total of twenty-four (24) aviation cadets are currently in training as part of the insourcing project execution.

### **9.1.2 Towage**

Tug delays are caused by tugs not being available at the required service time due to mechanical breakdowns, the tugs being busy with other shipping, or due to a shortage of tug capacity (which will include manning levels).

In order to reduce the abovementioned type of delay, the following initiatives are currently being implemented:

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- The on-going upgrade of the existing marine fleet which includes the delivery of new tugs which are now operational in the various ports.
- On-going focus on the Tug Maintenance regime to ensure maximum availability.
- Due to the significant skills scarcity of Chief Marine Engineers to man the tugs, the Authority had to substantially invest in programmes to ensure future availability of this skills base through:
  - The establishment of a structured Chief Marine Engineering Officer (“CMEO”) training programme which will ensure standardized assessment criteria and training across all ports;
  - Finalisation of a fixed term training contract to ensure the CMEO qualification is obtained within a prescribed period; and
  - Continuous engagement with the South African Maritime Safety Authority to address changes to the CMEO training requirements.

### 9.1.3 Berthing Services

Berthing delays are caused due to the berthing gangs not being at the allocated berth or not being available at the required service time.

In order to reduce the abovementioned type of delays, a quad shift system at the ports of Cape Town, Durban, Saldanha and Richards Bay have been implemented which will ensure that the berthing services shift patterns are aligned with the pilotage and tug operations.

Operational centres will review all marine operational processes, and includes marine operational planning, resourcing, technology infrastructure, as well as its functional structure is continuously being monitored to improve efficiency levels. It is expected that this project will also ensure that the current number of shipping delays are reduced, thereby further enhancing the overall efficiency of the ports system.

## 9.2 Terminal Operations Oversight

The Terminal Operator Licence is a key instrument to level the playing field and introduce the same regulatory/oversight framework for similar existing types of cargo handling terminals.

The Terminal Operating Licence establishes the conditions that the Authority prescribes for terminal operators within its port premises. Some of the key components of the Licence include the Safety, Health and Environmental Management compliance, Maintenance regime for its assets, as well as the operational performance requirements.

Section 65 of the National Ports Act provides for a special regime (transitional mechanism) for existing terminal operators. Following the Ministerial Notice (25 November 2011) and the Authority’s Government Gazette invitation (02 December 2011), existing Terminal Operators were invited to submit applications to the Authority for deemed licence conversion/s. All deemed existing

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Terminal Operators through engagement with the various ports have submitted their licence applications.

Eighty nine (89) Terminal Operator Licences were issued in terms of section 57 read with section 65 of the Act. In the process the Authority issued in the port of Durban fifty four (54), Richards Bay six (6), East London seven (7), Port Elizabeth nine (9), Cape Town ten (10) and Saldanha Bay three (3) Terminal Operator licences.

Following the issuing of the Terminal Operator Licences, amongst others, the terminal performance measures has been finalised for relevant terminal operators. Ngqura Container Terminal Licence is dealt outside the deemed licence process as part of the section 79 directive process.

To ensure the conditions in the Licence agreements are conformed to by the Licensees, the Authority has established an internal oversight function that will monitor and ensure compliance to the requirements of the operating Licence. This function will therefore significantly contribute to the overall operational efficiency of the port system as the terminal oversight responsibility will be executed in a proper and regulated manner.

### 10. Conclusion

South Africa, as a key member of the BRICS (Brazil, Russia, India, China and South Africa) family of nations, seeks to leverage emerging developments in the global environment by continuing to reorganize itself structurally to induce greater economic growth. In support of this national agenda, it is vital for ports, given their centrality in the transport and logistics chain, to be integral in ensuring the sustained competitive advantage of the South African economy and the region as a whole. To this end, the Authority in execution of the Transnet MDS is committed to its strategic path of:

- providing optimal port infrastructure in an integrated manner;
- improving port efficiency through increased productivity and operations oversight; and
- facilitating an integrated logistics chain that will establish the port system as a gateway for trade.

The benefits of optimal level of port infrastructure are real and can be quantified as they accrue to exporters, cargo owners, shippers and macroeconomic trade in general. Much wider benefits accrue to the following stakeholders:

- **Government** – at the macroeconomic level improvement of external trade competitiveness, port efficiency, and better coordination of sea and land transport
- **Transport Sectors** – cost effective port operations and services allow for efficient and better use of transport assets, better competitive position for transport operators and business growth
- **Shippers, Exporters and Importers** – enhanced competitive position through lower port costs, lower maritime freight rates resulting in lower import and export costs

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- **End Consumer** – Lower prices for consumer goods and increased access to wider range of products

In terms of the Port Directives, when considering the proposed tariffs for the Authority, the Regulator must ensure that such tariffs allow the Authority to:

- a) recover its investment in owning, managing, controlling and administering Ports and its investment in port services and facilities;
- b) recover its costs in maintaining, operating, managing, controlling and administering Ports and its costs in providing port services and facilities; and
- c) Earn a return commensurate with the risk of owning, managing, controlling and administering ports and of providing port services and facilities.

The Authority's proposed tariff methodology remains under review by the Regulator. The tariff application for FY 2014/15 has been prepared in accordance with the interim Regulatory Manual issued by the Regulator using the revenue requirement methodology.

Application of the Revenue Requirement formula results in a revenue requirement of R10 947m comprising of Real Estate business revenue of R2 113m and Marine business revenue of R8 834m translating to an overall average tariff adjustment of 14.39% for FY 2014/15.

The Authority is mindful of Transnet's commitment to reducing the cost of doing business in South Africa and has considered an approach to ensure a sustainable tariff increase which is in the interest of the economy. This would entail releasing R454m of the ETIMC provision previously created.

For the FY 2014/15, the Authority therefore applies to the Regulator for a revenue of R10 493m comprising marine business revenue of R8 380m and real estate business revenue of R 2 113m. This translates to an average overall tariff adjustment of 8.5%.

Translation of this marine revenue of R8 380m into individual tariffs (tariff book) will be informed by the Regulator guideline which will be issued post the tariff determination process.

**End.**

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### ANNEXURE A

#### The Authority's Tariff book

**Table 24: The Authority's Tariff Definitions**

Tariffs	Service Rendered	Application
Light dues	The provision of navigation aids to vessels along the South African coast	Raised per vessel (per gross ton) at the first port of call  (Tariff Book Section 1)
Vessel Traffic Services	The provision of vessel traffic services, safety of the port environment and port control	Raised per vessel (per gross ton) at all ports  (Tariff Book Section 2)
Port dues	The provision and maintenance of entrance channels, breakwaters, turning basins, navigational aids (beacons and buoys inside port limits) and maintenance dredging inside the port	Raised per vessel (per gross ton), linked to the time that the vessel remains in port  (Tariff Book Section 4)
Berth dues	The provision and maintenance of repair quays and other non-cargo quay (berth) infrastructure	Raised per vessel (per gross ton), per 24-hour period  (Tariff Book Section 4)
Cargo dues	To recover the cargo contribution towards the provision and maintenance of basic port infrastructure	Raised per unit of cargo, differentiated between different commodities  (Tariff Book Section 7)
Rentals	Lease of port land to terminal operators, port service and port facility providers	Rental arrangements including escalations are negotiated on a case-by-case basis and are not reflected in the tariff book.
Pilotage	Pilotage assistance to vessels entering/leaving the port	Raised as a basic fee per service, plus per vessel (per gross ton)  (Tariff Book Section 3)
Tug Assistance	Tug assistance to vessels entering/leaving the port	Raised per service, based on the size of the vessel (per gross ton)  (Tariff Book Section 3)
Miscellaneous	Tanker fire watch, fire fighting and standby	Raised per service, per hour

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Tug/Vessel services	services	(Tariff Book Section 3)
Berthing Services	Berthing services to tie/untie vessels at the berth	Raised per service (Tariff Book Section 3)
Running of Vessel Lines	Running of lines for vessels entering, leaving or shifting	Raised per service (Tariff Book Section 3)
Floating Crane Services	Floating crane services rendered to the vessels	Raised per service, per hour (Tariff Book Section 3)
Ship Repair Facilities <sup>4</sup>	Preparation, Docking and Undocking of vessels at repair facilities	Raised per service (Tariff Book Section 6)
Dry-dock, floating dock, synchrolift and slipways	Dry-dock, floating dock and synchrolift fees	Raised per service for the use of a facility, based on the size of the vessel (per gross ton) (Tariff Book Section 6)

Authority has created a separate section in the Tariff Book, Section 5, where the licence, registration and permit fees are specified. This is summarized in the following table:

**Table 25: Authority's License Fees**

Fees	Service rendered	Application
Port Service Licence, Port Rule Licence, Port Rule Registrations and Port Rule Permit Fees	Fees payable for licences, registrations and permits in accordance with section 57 of the Act and with Port Rules issued in terms of section 80(2) of the Act.	Raised as a fee for the respective licences, registrations and permits issued (Tariff Book Section 5)

<sup>4</sup> The Authority has re-evaluated its involvement in ship repair facilities and the operation thereof. The decision has been taken that the Authority will continue to operate its ship repair facilities until the approval of the ship repair strategy.

## Transnet National Ports Authority Tariff Application for Financial Year 2014/15

### ANNEXURE B

#### Detailed NPA Capital Investment Program for the MDS period

The Authority's investment spending is primarily influenced by the strategic initiatives which are aimed at providing adequate port infrastructure ahead of demand. The broader scale of these initiatives includes infrastructure that will improve vessel, cargo turnaround and overall efficiency use of port assets.

The Capital Expenditure provided for FY 2014/15 as well as comparatives for FY 2013/14 is broken into various categories in order to demonstrate the impact thereof. The figures presented in the Authority's capital program do not include Durban International Airport. The categories are illustrated as follows:

**Table 26: Strategic capital Objectives**

		2013/14	2014/15
		Rm	Rm
<b>Re-engineering, Integration, Productivity and Efficiency</b>	To maximise return on investments by obtaining additional volumes	492	1 267
	To maximise return on investments by improving operating efficiencies	351	683
	To preserve current revenue streams without obtaining additional volumes (ie. revenue protection)	1 037	895
<b>Safety, Risk and Effective Governance</b>	Ensure Safety Optimisation	202	383
	Optimise Business Enterprise Offerings	81	26
	Optimally Satisfy Social Investments (non economic value creating projects)	-	1
	Environmental	3	45
<b>Human Capital</b>	Optimise Human Resources	54	17
<b>Total (excl. borrowing cost)</b>		<b>2 219</b>	<b>3 317</b>



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**Table 27: List of Major Projects for the Authority**

Project	Corridor	Commodity
Acquisition of 9 tugs (Rcb, Dbn, PE & Sld)	RCB/DBN/PE/SLD	All
Bayvue rail yard expansion - Outcome from ECICS feasibility	RCB	Other
Provision of additional berthing capacity for MPT - berths 709 to 711 (700m quaywall)	RCB	Break Bulk
Provision of additional DBT Export berthing capacity - Berth 802 / 3	RCB	Dry Bulk
Reconstruction of Sheet-Pile Quay Walls at Maydon Wharf	DBN	Break Bulk
Edwin Swales Link Road FEL 4	DBN	Other
Execution: DCT berth deepening 203 to 205	DBN	Containers (Maritime)
Acquisition of 6 tugs for Dbn (4 Replacement & 2 additional)	DBN	Other
Execution: Pier 1 Phase 2 Infill (Salisbury Island)	DBN	Containers (Maritime)
Extend main breakwater and deepen entrance	EL	Other
Operationalise Port for Containers (Prelim & Execution)	NGQ	Containers (Maritime)
Tank farm Berth A100, roads, port entrance and services	NGQ	Liquid Bulk
General Cargo Berth B101 and associated services	NGQ	Break Bulk
Manganese project	NGQ	Manganese
Expansion of Container Terminal : CPT	CPT	Containers (Maritime)
Port Infrastructure for Moss gas Quay Extension & Associated Dredging Works & Dry Dock Facilities - change to Provision of Ship repair (Floating dock and rig repair)	SLD	Break Bulk
Ore Expansion Phase 2 Berth Construction	SLD	Export Iron Ore
Provision of second new TSHD	DRS	Other

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**Table 28: Expansion business vs. maintenance of current business for FY 2014/5 and FY 2013/14**

### Major Commodity per Port for FY 2014/15 and FY 2013/14

#### FY 14/15

	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft
	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Expand Business : - Growth initiatives	1 562	296	211	26	458	1	3	-	65	-	489	14
Maintain current Business : - Replacement Efficiency/ Service Quality	1 755	358	529	229	7	276	5	124	98	21	89	18
<b>Total (excl. borrowing cost)</b>	<b>3 317</b>	<b>654</b>	<b>740</b>	<b>255</b>	<b>465</b>	<b>277</b>	<b>8</b>	<b>124</b>	<b>163</b>	<b>21</b>	<b>578</b>	<b>33</b>

#### FY 13/14

	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Expand Business : - Growth initiatives	693	87	215	4	165	0	6	37	39	-	124	16
Maintain current Business : - Replacement Efficiency/ Service Quality	1 525	230	365	58	14	172	5	84	286	72	95	144
<b>Total (excl. borrowing cost)</b>	<b>2 219</b>	<b>318</b>	<b>581</b>	<b>62</b>	<b>179</b>	<b>172</b>	<b>11</b>	<b>121</b>	<b>324</b>	<b>72</b>	<b>219</b>	<b>159</b>

**Table 29: Ports Related Spending by Asset Type**

#### FY 2014/15

	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft	Draft
	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15
Asset Types	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Buildings and structures	729	342	60	173	-	20	6	101	22	-	-	5
Aircraft	-	-	-	-	-	-	-	-	-	-	-	-
Land	17	-	5	-	-	-	-	-	13	-	-	-
Machinery, equipment and furniture	137	19	42	2	2	3	1	10	3	21	7	28
Permanent way and works	122	120	1	-	-	-	-	-	-	-	-	-
Vehicles, Rolling stock & containers	3	-	-	3	-	-	-	-	-	-	-	-
Port Facilities	2 310	173	632	77	463	254	1	13	125	-	572	-
Other	-	-	-	-	-	-	-	-	-	-	-	-
Pipelines networks (etc)	-	-	-	-	-	-	-	-	-	-	-	-
<b>Total (excl. borrowing cost)</b>	<b>3 317</b>	<b>654</b>	<b>740</b>	<b>255</b>	<b>465</b>	<b>277</b>	<b>8</b>	<b>124</b>	<b>163</b>	<b>21</b>	<b>578</b>	<b>33</b>

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### FY 2013/14

Asset Types	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate	Estimate
	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Buildings and structures	653	209	195	57	1	20	4	59	18	43	-	46
Aircraft	-	-	-	-	-	-	-	-	-	-	-	-
Land	1	-	1	-	-	-	-	-	-	-	-	-
Machinery, equipment and furniture	204	8	34	2	2	3	3	5	3	30	2	113
Permanent way and works	28	2	18	-	-	-	-	8	-	-	-	-
Vehicles, Rolling stock & containers	-	-	-	-	-	-	-	-	-	-	-	-
Port Facilities	1 334	99	333	4	176	149	4	48	303	-	217	-
Other	-	-	-	-	-	-	-	-	-	-	-	-
Pipelines networks (etc)	-	-	-	-	-	-	-	-	-	-	-	-
<b>Total (excl. borrowing cost)</b>	<b>2 219</b>	<b>318</b>	<b>581</b>	<b>62</b>	<b>179</b>	<b>172</b>	<b>11</b>	<b>121</b>	<b>324</b>	<b>72</b>	<b>219</b>	<b>159</b>

Table 30: Port Related Spending per Commodity

### FY 2014/15

Commodity	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast	F/Cast
	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15	2014/15
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Containers	248	-	12	-	236	-	-	-	-	-	-	-
Liquid Bulk	405	3	37	119	177	-	-	70	-	-	-	-
Iron Ore	27	-	-	-	-	-	-	-	27	-	-	-
Coal	108	98	-	10	-	-	-	-	-	-	-	-
Manganese	-	-	-	-	-	-	-	-	-	-	-	-
Break Bulk	407	8	322	-	45	-	-	2	30	-	-	-
Automotive	1	-	-	-	-	1	-	-	-	-	-	-
Fleet - craft	433	-	206	-	-	158	-	-	68	-	-	-
Dredging Services	578	-	-	-	-	-	-	-	-	-	578	-
Other (incl LHS)	1 109	545	162	126	7	118	8	52	38	21	-	33
<b>Total (excl. borrowing cost)</b>	<b>3 317</b>	<b>654</b>	<b>740</b>	<b>255</b>	<b>465</b>	<b>277</b>	<b>8</b>	<b>124</b>	<b>163</b>	<b>21</b>	<b>578</b>	<b>33</b>

### FY 2013/14

Commodity	TNPA	RCB	DBN	EL	NGQ	PE	MSB	CPT	SLD	LHS	DRS	HO
	Budget	Budget	Budget	Budget	Budget	Budget	Budget	Budget	Budget	Budget	Budget	Budget
	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14	2013/14
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Containers	183	-	80	-	67	-	-	36	-	-	-	-
Liquid Bulk	260	-	152	1	89	-	-	17	-	-	-	-
Iron Ore	40	-	-	-	-	-	-	-	40	-	-	-
Coal	12	8	-	4	-	-	-	-	-	-	-	-
Manganese	0	-	-	-	-	0	-	-	-	-	-	-
Break Bulk	113	-	96	-	9	-	-	-	8	-	-	-
Automotive	-	-	-	-	-	-	-	-	-	-	-	-
Fleet - craft	552	78	81	-	-	127	-	4	262	-	-	-
Dredging Services	219	-	-	-	-	-	-	-	-	-	219	-
Other (incl LHS)	840	231	172	57	14	45	11	63	14	72	-	159
<b>Total (excl. borrowing cost)</b>	<b>2 219</b>	<b>318</b>	<b>581</b>	<b>62</b>	<b>179</b>	<b>172</b>	<b>11</b>	<b>121</b>	<b>324</b>	<b>72</b>	<b>219</b>	<b>159</b>

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Table 31: Multi-year Strategic objectives

Strategy	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	Total 7yr
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Re-engineering, Integration, Productivity and Efficiency	492	1 267	4 978	6 734	6 137	11 077	7 944	38 629
	351	683	866	777	110	83	128	2 998
	1 037	895	1 343	1 954	1 984	1 422	1 466	10 101
	202	383	424	302	158	35	114	1 618
Safety, Risk and Effective Governance	81	26	37	119	71	38	-	372
	-	1	87	89	10	140	177	503
	3	45	32	23	13	-	-	115
	54	17	80	85	7	-	-	242
Human Capital	54	17	80	85	7	-	-	242
Total (excl. borrowing cost)	2 219	3 317	7 846	10 082	8 491	12 795	9 828	54 578

Table 32: Multi-Year Capex Spending Per Port Service

Capex spend per Port Service / Facility	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	Total 7yr
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Infrastructure	1 377	2 284	6 901	9 206	8 046	12 203	9 254	49 271
Marine services	552	433	648	852	395	550	520	3 950
Lighthouse services	71	21	25	23	48	40	52	280
Dredging services	219	578	272	2	2	2	2	1 077
Total (excl. borrowing cost)	2 219	3 317	7 846	10 082	8 491	12 795	9 828	54 578

Table 33: Multi-Year Ports related spending by asset type

Asset Type	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	Total 7yr
	Rm	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Buildings and structures	653	729	798	1 319	1 194	719	1 012	6 423
Aircraft	-	-	-	-	20	86	-	106
Land	1	17	50	152	30	110	92	451
Machinery, equipment and furniture	204	137	226	334	228	124	156	1 408
Permanent way and works	28	122	296	124	268	303	513	1 655
Vehicles, Rolling stock & containers	-	3	-	-	-	-	-	3
Port Facilities	1 334	2 310	6 468	8 146	6 743	11 453	8 055	44 507
Other	-	-	-	-	-	-	-	-
Pipelines networks (etc)	-	-	-	-	-	-	-	-
Total (excl. borrowing cost)	2 219	3 317	7 838	10 074	8 483	12 795	9 828	54 554

Table 34: Multi –year Port Related Spending per Commodity

	Estimate	Draft	Projection	Projection	Projection	Projection	Projection
	2013/14	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
	Rm	Rm	Rm	Rm	Rm	Rm	Rm
Containers	183	248	2 103	2 425	2 056	4 021	1 711
Liquid Bulk	260	405	1 491	1 650	2 105	2 235	2 445
Iron Ore	40	27	356	1 867	782	42	281
Coal	12	108	29	93	82	78	180
Manganese	0	-	80	86	-	-	-
Break Bulk	113	407	979	638	546	3 757	2 746
Automotive	-	1	10	35	-	10	85
Fleet - craft	552	433	648	852	395	550	520
Other (incl DRS&LHS)	1 059	1 687	2 151	2 435	2 525	2 102	1 860
Total	2 219	3 317	7 846	10 082	8 491	12 795	9 828

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### Ports Consultative Committees (PCC)

Following on from the ROD for FY 2012/13 and discussions with the office of the Regulator the ports have been requested, at their respective PCC meetings, to share their capital programme for the next financial year, as well as their 5 year and 10 year Capital Expenditure Programmes (CAPEX). The table below shows the dates at which the CAPEX programmes for FY 2014/15 and the following 5 years were presented at the respective PCC's.

**Table 35: Port Consultative Committee Capex Presentation Dates**

Port Name	PCC Date	Presentation
Mossel Bay		8 <sup>th</sup> May 2013
Saldanha Bay		9 <sup>th</sup> May 2013
Cape Town		10 <sup>th</sup> May 2013
Richards Bay		16 <sup>th</sup> May 2013
Durban		17 <sup>th</sup> May 2013
Port Elizabeth		27 <sup>th</sup> May 2013
Ngqura		28 <sup>th</sup> May 2013
East London		3 <sup>rd</sup> June 2013

There were no objections to the Capex presented to PCC's in consultation sessions shown above.

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### ANNEXURE C

#### The Authority's Total Costs

The Total cost analysis of the Authority's operating expenditure including Group cost is shown in the table below:

**Table 36: Authority's Operating Cost Including Group Overheads**

	Actual 2012/13 R Million	Budget 2013/14 R Million	Forecast 2014/15 R Million	Deviation R Million 2013/14 VS 2014/15	Deviation % 2013/14 VS 2014/15	% of Operating Cost 2014/15
Labour Costs	1 472	1 781	1 943	162	9.1%	52.0%
Rates & taxes	193	250	264	14	5.6%	7.1%
Maintenance	276	355	367	12	3.5%	9.8%
Contract Payments	57	65	68	3	4.5%	1.8%
Energy	353	445	485	40	9.1%	13.0%
Professional services	13	37	39	2	4.7%	1.0%
Material	75	97	94	(4)	-3.7%	2.5%
Computer & Info systems	64	81	86	4	5.5%	2.3%
Rental	52	60	68	8	13.5%	1.8%
Security costs	51	68	73	5	6.9%	2.0%
Research & development	32	82	72	(11)	-12.8%	1.9%
Sundry operating costs	104	215	179	(36)	-16.9%	4.8%
Total operating cost (excluding depreciation)	2 742	3 537	3 738	201	5.7%	100.0%
Group Costs	367	653	591	99	19.1%	100.0%
Total operating cost (Including Group Costs)	3 109	4 190	4 329	139	3.3%	100.0%

The Authority's total cost amounts to R4 329m including Group overhead. The split of costs into different operations of the Authority's business such as marine costs and lighthouse costs has not been provided. This will be informed by the pricing strategy project. The Regulator has included in the guidelines a request that the Authority submits information regarding Group overhead costs and the audit thereof as part of analysing internal transfer pricing.

#### Labour Cost

Labour costs contribute 51.8% to the total operating costs for FY 2014/15. Labour costs are direct to supporting the on-going business of the Authority. As a result, Labour costs are expected to grow by 12.3% in FY 2014/15. The number of permanent employees at the Authority is planned as follows:

**Table 37: Head Count in Accordance with MDS**

Cost Category	Actual 2012/13	Budget 2013/14	Forecast 2014/15	Deviation 2013/14 vs 2014/15	Deviation % 2013/14 vs 2014/15
Total Number of Employees	3 584	4 409	4 598	189	4.30%

The cost of labour includes various training initiatives which the Authority has started in the last FY 2012/13 continuing into the future. These initiatives are highlighted as follows:

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- cadet Training
- helicopter Pilot Training
- MSC shipping in transport-Rotterdam
- aircraft Maintenance & Aircraft Avionics
- practical Ship Handling Training

In addition there is a set of skills that are required by the Authority in order to meet objectives of the MDS Strategy and to support delivery in key focus areas, these critical skills identified are as follows:

- port engineering and Project management resources to be in line with the upgrading of existing infrastructure as well as new infrastructure requirements;
- marine services as a result of the quad-shift system in order to improve efficiencies;
- aviation services which are currently out-sourced, however a Cadet training programme has been established with the aim of providing aviation in-house in the future;
- risk management competencies (including environmental management);
- contracts and vendor management;
- operations and oversight management and
- security services which are shifting toward in-sourcing.

### Rates and Taxes

Rates and taxes relate to municipal rates and are based on the methodology employed by the municipalities in accordance with the Municipal Rates and Taxes Act. Rates and taxes are increasing in line with inflation for the FY 2014/15.

### Maintenance

Repairs and maintenance remains one of the Authority's key focus areas, as a result Maintenance will be increased slightly from FY 2013/14 to FY 2014/15 in order to ensure the efficient continuity of operations in line with required standards.

### Contract Payments

Contract payments will be closely monitored and are expected to grow below inflation.

### Energy

The main driver for increased energy cost is electricity and is linked to electricity tariff increases implemented by municipalities and Eskom. The trend of higher fuel and electricity costs are expected to continue into the immediate future as global markets experience higher oil prices and the local economy gears up for increased capital expenditure by Eskom, resulting in higher tariffs. Electricity costs also include a margin charged by municipalities which are the source of supply to the ports.

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### **Professional Services**

The majority of professional fees relate to internal and external audit fees (financial and operational/environmental) and legal fees whilst the remainder relates to other professional services expected.

### **Material**

These costs are influenced by material price increases and exchange rate fluctuations on maintenance material used for the marine fleet and civil maintenance.

### **Computer and Information Systems**

Computer and information systems cost includes network costs, software licenses, information system support, development cost, computer consumables and on-going maintenance thereof.

### **Rental**

The increase in rental for the FY2014/15 is higher than inflation. This is attributable to increases in hire of internal and external land and buildings; machinery, equipment and furniture, non-revenue earning vehicles; and telecommunications equipment. The 13.5% increase is predominantly driven by increased rentals for new computer and office space for head office personnel given the Authority's focus on its oversight role

### **Security**

The Authority is using private security firms in the ports. The cost increases relates to contract obligations and additional security arising from ISPS obligations, which require stringent compliance to international standards. As a result, security costs are expected to increase by 6.9% for FY 2014/15.

### **Research and Development**

These costs relate to studies for future capital investments in a pre-feasibility phase to determine the merits or viability of a project and different options available. The feasibility phase is funded from the capital programme for final detailed design. Costs will vary from year to year depending on the future capital programme. Research and Developments costs for FY 2014/15 is attributed to, amongst other projects, ship repair facility at the Port of Saldanha, deepening and widening of the entrance channel at the Port of East London and Port services and logistics master plan.



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### **Sundry Operating Cost**

Sundry Costs includes expenses relating to insurance, stationery and printing, transport, promotions and advertising, cleaning services, environmental and other miscellaneous operating expenditure. Majority these costs are increasing in line with inflation.

Miscellaneous revenue captured under sundry operating costs relates to income received from penalties and levies raised by the Authority from time to time.

The Authority's business warrants the use of subject specialists from time to time, which in some cases, may have to be sourced abroad at higher than normal consulting rates. For FY 2014/15 professional services will be required for various Section 56 processes including the Port of Ngqura container terminal, Port of Ngqura manganese terminal and the Cruise Liner terminals. These expenses are grouped under Other 1 costs.

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**Table 38: Authority's Sundry Operating Costs**

Sundry Operating Costs	Actual 2012/13 R Million	Budget 2013/14 R Million	Forecast 2014/15 R Million	Deviation R Million 2013/14 VS 2014/15	Deviation % 2013/14 VS 2014/15	% of Operating Cost 2013/14
External property ancillary costs revenue	(184)	(196)	(209)	(13)	6.5%	-5.6%
Intra NPA recoveries (Positive)	(304)	(297)	(318)	(20)	6.8%	-8.5%
Intra cc recoveries (Positive)	214	209	224	16	7.5%	6.0%
Intra cc charges (Negative)	42	42	44	2	5.8%	1.2%
Miscellaneous revenue (Positive (Rev) / Negative (loss)	(40)	(26)	(41)	(15)	59.7%	-1.1%
Group Auditors	1	14	15	1	9.0%	0.4%
Bad Debts Written Off - Tax Deductible	7	7	3	(4)	-54.8%	0.1%
Entertainment	16	14	15	1	5.5%	0.4%
Environmental management	32	18	19	1	3.4%	0.5%
Fines and Penalties	0	-	-	-	0.0%	0.0%
Health and Sanitation	29	39	41	2	4.7%	1.1%
Insurance Operations	30	34	37	2	7.1%	1.0%
Legal Costs - Tax Deductible	15	28	25	(3)	-9.1%	0.7%
Internal Audit	33	29	31	2	5.5%	0.8%
Membership Fees	4	5	5	(0)	-7.5%	0.1%
Bank Charges	0	0	0	0	5.5%	0.0%
Catering Costs	1	2	2	0	5.5%	0.1%
Claims Paid	1	-	-	-	0.0%	0.0%
Commission Paid	0	0	0	0	5.5%	0.0%
Discount Allowed	-	-	-	-	0.0%	0.0%
Gifts	1	0	0	0	5.4%	0.0%
License Fees	1	1	1	0	5.4%	0.0%
Magazines, Books and Periodicals	0	1	1	0	5.5%	0.0%
Newspapers	-	-	-	-	0.0%	0.0%
Nursery / Flower Expenditure	6	12	12	1	5.5%	0.3%
Water	59	53	56	3	6.0%	1.5%
Other 1	30	76	62	(14)	-18.3%	1.7%
Navigation, Landing and Parking	18	23	25	1	5.5%	0.7%
Postage	0	0	0	0	5.4%	0.0%
Printing and Stationery	7	12	12	(0)	-2.6%	0.3%
Promotions and Advertising	16	25	27	2	6.1%	0.7%
RDP Costs / Social Investment	-	-	-	-	0.0%	0.0%
Regional Services Levies	-	0	0	0	5.5%	0.0%
Telecommunication Services : External	16	19	20	1	5.5%	0.5%
Travel Benefits / Concessions	-	-	-	-	0.0%	0.0%
Transport Cost : External	3	2	2	0	5.5%	0.1%
Travel - Local	29	40	38	(2)	-4.7%	1.0%
Travel - Overseas : Deductible	3	7	8	0	4.2%	0.2%
Accommodation and refreshments	17	21	20	(1)	-3.7%	0.5%
Total sundry operating expenses	104	215	178	(37)	-16.9%	4.8%

### Group Overhead Cost

Transnet Corporate Centre (i.e. Transnet Group Head Office/TCC) incurs significant expenditure centrally to support the various operating divisions ("OD's"). In addition, provision is made for certain divisional specific costs at TCC. Furthermore losses/profits in respect of Transnet Capital Projects and Transnet Foundation (social responsibility costs) are required to be recovered from the OD's. Previously TCP did not recover full costs of its services from the OD's and therefore had losses. These losses had to be recovered from the OD's as overhead costs. During this budget cycle TCP will break even.

These costs that have been incurred / budgeted need to be recovered from the relevant OD's on a fair basis. In order to recover these costs, various cost-drivers are utilised to allocate these costs

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(e.g. revenue, capital expenditure plans, personnel headcount, estimated utilisation etc.). An analysis of the TCC costs expenditure items is shown in the Table below:

**Table 39: Group Overhead Costs**

Cost Category	Actual 2012/13 R Million	Budget 2013/14 R Million	Budget 2014/15 R Million	Deviation R Million FY13/14 vs. 14/15	Deviation % FY13/14 vs. 14/15	% Of Operating Cost 2014/15
Labour costs	83	228	250	22.5	9.9%	42.4%
Professional Fees	90	187	183	-3.4	-1.8%	31.0%
Electronic Data Costs	22	11	11	-0.1	-0.9%	1.8%
Other Operating Costs	172	228	146	-81.5	-35.8%	24.8%
<b>Grand Total</b>	<b>367</b>	<b>653</b>	<b>591</b>	<b>-62.5</b>	<b>-9.6%</b>	<b>100.0%</b>

### Labour Costs

The MDS strategy aims to increase Transnet's employee headcount to 74 978 by FY 2018/19. Group overheads-labour costs increase results from migration of different schools of excellence from ODs to Transnet Group with effect from FY 2013/14. These include Maritime School of Excellence, School of Security, School of Procurement and Transnet Talent Management which all fall under Transnet Academy. Associated with Transnet Academy are increased training costs for programmes to support increased future activity that will result from MDS rollout.

### Professional Fees

The implementation of the MDS will necessitate the use of various professionals and subject specialists across Transnet. These include the consultation fees for capital planning and execution teams, capital scrubbing and procurement specialists that are assisting with eight high value mega capital projects totalling in excess of R200 billion.

### Other Operating Costs

One of the key objectives of MDS includes the delivering of lasting economic, social and environmental value to society. This will therefore warrant an increase in Corporate Social Investment (CSI) spending; Transnet Foundation costs have increased significantly mainly as a result of the second health train that came into operation in the FY 2013/14 financial year. Other operating costs include costs that are taken over by Transnet Group for the first time e.g. administration fees for pensioners managed by Momentum. Also included in other operating costs is depreciation costs and turn over based supplier development costs that are carried by Transnet Group.

**End.**