

**SALGA SUBMISSION TO THE POTFOLIO COMMITTEE ON
MINERALS AND ENERGY, ON THE VIABILITY OF THE
NATIONAL RED**

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The Electricity Distribution Industry is a highly Contested Environment, and the varying EDI desired End State and vision amongst key industry players creates a major challenge to the process. The uncertainty with regard to the number of REDs also create a challenge of its own as it leads to confusion and speculations with stakeholders engaged on an open ended discussions about 6 wall to wall versus the 6 Metro REDs, Cluster REDs, Local REDs plus the National RED debate.

The current debate and discussions on the National RED is beginning to point some fundamental contradiction with regard to the restructuring process, particularly on National interest versus individual interest, corporate interest and industrial interests. The debate also raises questions on the future role of Local Government in electricity distribution.

SALGA as the voice of local government would like to take the PPC back to 1992 when the current government was ready to govern, and produced a document titled **“Ready to govern”**. In this document it is envisaged that *“local government will play a key role in development and in the equitable redistribution and re-allocation of services. Local government will address as a priority the disparities in our cities, towns and villages which have resulted from the policies of apartheid”*.

When they wrote the Constitution of the Republic of South Africa, our law-makers, did not forget the “ready to govern” principles and they were also driven by the desire to create a structure of government which would be suited to the task of overcoming conditions of under-development.



Section 156(1)(a) and (b) of the Constitution states that municipalities have executive authority in respect of, and the right to administer, the local government matters listed in Part B of Schedule 4 and Part B of Schedule 5 and also any other matters as may be assigned to municipalities by national and provincial legislation. The EDI Blueprint acknowledges that Municipalities in South Africa have constitutional and other legislative rights to distribute electricity within their local boundaries. The current debate on the National RED creates questions on the status and relevance of the EDI Blue print, which SALGA considers to be the only government policy on EDI.

The South African **Developmental Local Government approach** to service delivery is well recognized. The World Bank entitled its 1999/2000 World Development Report **"Entering the 21st Century"** the Report took particular note of the work we had done to establish our system of local government. It said: *"South Africa and Uganda have adopted ambitious decentralization programmes and...are emerging as two important models for devolving centralized power"*. This approach is clear from the restructuring of the health sector, water, housing, etc, that have seen local government assuming more responsibilities. The creation of a National RED is in contradiction of this approach and will result in disempowered local government not able to exercise their executive authority.

The overall government approach to service delivery shows that **planning and authority on the delivery of basic services is devolving to the implementation level**, which is developmental local government. This major shift has necessitated alignment between Integrated National Electrification Programme (INEP) and the Integrated Development Plans (IDP), the later a statutory requirement for municipalities. Unfortunately to this date, we have not yet fully achieved the alignment because of the Eskom and Municipal areas of supply divisions in terms of operations and governance. In the absence of Service Delivery Agreements between municipalities and Eskom, municipalities are disempowered to play their executive authority role. This results in a situation where local people confront municipalities, particularly when there is black outs and poor quality of supply in Eskom areas, thereby creating bad relation between the municipality and the community it serves.



SALGA does not believe in the Eskom and Municipal areas of supply approach, and see the REDs as a solution to this sad state of affairs to enable municipalities to play their executive authority role in all areas within their jurisdiction.

Impact to Municipalities

Municipalities are variable in their capacity to discharge their constitutional mandate, and it must be noted that the level of governance, resources, capacity and systems differ from municipality to municipality. It should therefore be acknowledged that the impact of the National RED to municipalities will differ between category B and C municipalities. The organized local government concern is centred on the impact of the National RED on category B municipalities such as, Buffalo City, Umhlathuze, Mangaung, Southern Cape, etc, as they are currently operating viable and sustainable distribution services. Any proposal for REDs creation should thus allow viable category B municipalities to form REDs and together with the Metro REDs incorporate neighbouring municipalities into these REDs. The end state can be the six wall to wall REDs or the National RED, it is all possible we just need the enabling legislation and a well thought transactional approach to guide the process.

The Eskom Model

It is interesting to note that Eskom view itself as a credible vehicle to consolidate municipal electricity undertakings, hence they concluded that the National RED should be established Anchored by Eskom. This assertion by Eskom is well explained in slide number 6 of Eskom presentation on Wednesday.

Eskom motivation to Anchor the National RED is based on their experience with incorporating the TBVC and SGT. I will now shift attention to Mpumalanga to share our view with regard to Eskom experience with incorporating TBVC. The Lowveld Electricity Trust (TED) was formed as a joint venture (50/50%) with ESKOM and the Old Kangwane Electricity with ESKOM being the operating agent.



With the change in Government, legislation provided that all former homelands electricity systems be taken over by ESKOM. ESKOM took over Lowveld Electricity Trust (TED) on 1 Sept 1999 and the action was appealed, with the outcome that the Court restored TED on 1 January 2001.

Eskom never adhered to the order, but instead operated the network to generate an income and never shared this with the three municipalities, Albert Luthuli, Mbombela & Nkomazi Municipality. During this period no electrification was carried out leading to dissatisfaction from residents. The inability of Eskom to account for financial statements of the business, but be able to file for liquidation on account that the business is running at a loss was a serious concern to SALGA, DPLG, Provincial Department of Local Government and the municipalities concerned. . Despite our consistent appeal to Eskom that as government agents we should avoid taking each other to court and that whatever we do, we should ensure that people on the ground do not suffer as a result of our actions. Eskom proceeded with the liquidation process and won the bid, the three municipalities lost and to this day they are not happy with the way Eskom dealt with this incorporation which today Eskom is using to justify its role in the National RED. This is not an isolated case as some of you might be aware, Thulamela in Limpopo and Mafikeng in North West are amongst others who have suffered from the incorporation. The issue is about ownership of assets in preparation for the REDs and raises questions on how Eskom took control and ownership of municipal assets. This in our view does not reflect any good experience in incorporating municipal electricity distribution in its true sense, but reflect on Eskom experience with operational integration.

The National RED Model

The original Six REDs model should be kept on the table, given the developments and communication that went into it and the low number of REDs. It must be noted that cabinet has not yet pronounced on the result of the Modelling exercise and currently, there is no decision made on the nature and structure of the National RED. SALGA welcome and appreciate the opportunity created by the PPC to engage all key stakeholders in the process and recommend that the model that is sustainable and in line with the Blue print objectives be chosen, it is very clear from the above that it can not be a National RED Anchored by Eskom.



Cabinet decision to accelerate the restructuring process is welcome because the process has been moving very slow. **The organised Local Government has responded positively to the cabinet decision and municipalities across the country are at different levels with the preparations for the transition to the REDs,** however the absence of the transactional framework and enabling legislation that is in line with the constitution remain major obstacles, in addition to the following;

- National RED/s governance
- Compensation model
- Asset transfer
- The EDIR Bill
- Section 76 of the Electricity Regulation Bill

The Six REDs can materialise at the end and the modelling has shown that this is the most economically viable with only RED 3 experiencing losses, and this can be mitigated. SALGA support the Six REDs model and should it be that Cabinet decide on the **Six plus One** Model, it is recommended that Eskom model of the National RED should not be considered and preference should be given to a complete new Public Entity owned by government. The National RED will operate at a major loss compared to RED 3 in the Six REDs Model, and a multi approach loss mitigation strategy comprising of the following amongst others, will be required to succeed as explained by the EDIH report;

- Tariff increase
- National transfer
- Cross REDs subsidy
- National Bulk price subsidy
- Tax exemptions, etc

Chairperson, this brings me to raise a question on the differences that exist between the results of the Eskom Modelling on the National RED that shows that the National RED is financially viable, and the EDIH Modelling that shows that the National RED is not financial viable as explained above.



As SALGA we did not do our own model on this, but opted to encourage municipalities to make information available to EDIH for modelling purposes. However, it is worrying that Eskom opted to do its own Model that point to a National RED anchored by Eskom. EDIH was established to facilitate the process, and key stakeholders, particularly municipalities and Eskom are expected to cooperate in the process in the spirit of the cooperative agreement that was signed between SALGA, EDIH, DME, Eskom and NER. SALGA wants an explanation on how the Eskom modelling was conducted as we were fully part of the EDIH modelling process, both at the board level and the operational level. It is our firm conclusion that Eskom's modelling results should not be regarded as credible because we don't believe it was done in the interest of the industry or the country, but corporate interests.

The Electricity Supply Industry

The recent power failures in the Western Cape have exposed problems we are having as a country in the generation of electricity. Eskom as a strategic resource in the Electricity Supply Industry should be phased out of distribution to focus on generation and transmission.

This proposal makes sense in light of the current realities as it free Eskom from Distribution problems to focus on the generation problems that are also very complex and demanding. It must be noted that there can be no distribution without generation. This necessitates the need for ongoing monitoring of the generation and transmission whilst restructuring the distribution. It will be problematic to have a well restructured electricity distribution industry without sufficient electricity to distribute. SALGA welcomes the huge investment made on increasing our generation capacity and sees Eskom as a very critical player in generating enough electricity to meet our target of 6% economic growth and beyond.

Conclusion:

- 1) SALGA notes the biasness towards Six Metro REDs and One National RED scenario by some stakeholders despite the absence of Cabinet pronouncement on the matter and calls on all stakeholders to respect the process and wait for the Cabinet pronouncement to avoid confusion in the industry



- 2) SALGA recognises the immense responsibilities that are progressively devolving to local government and call for attention to the task of building local government capacity in line with project consolidate, as opposed to disempowering municipalities in electricity distribution.
- 3) SALGA notes the claim by Eskom that it has successfully incorporated TBVC and calls on Eskom to explain the success story in light of the concern from affected municipalities
- 4) SALGA is of the view that the incorporation of the TBVC to Eskom is incomplete and can not be used to justify Eskom's role in the National RED
- 5) No municipality has shown interest to be incorporated into Eskom, and should this happen, it will be unconstitutional.
- 6) SALGA request the Department of Minerals and Energy to fast track the enabling legislations that are in line with the constitution to guide the process as a matter of urgency
- 7) SALGA notes the Eskom Model on the National RED and request that the PPC be cautious given Eskom interest in the matter
- 8) SALGA recommend that Eskom distribution assets to be transferred to the REDs should include key customers as per the original six wall to wall REDs model and EDIR blue print
- 9) SALGA recommend that the end state of the restructured electricity distribution industry should establish the REDs as the only distributor to all customers, domestic, industrial, key customers, etc.
- 10) SALGA supports the transactional approach to REDs creation in the interest of the country and discourage quick fix National RED, that will lead to problems in the long term
- 11) SALGA support the Six REDs Model as the End State to supply Electricity to all customers in the country
- 12) SALGA furthermore recommend that we Uphold, respect and recognize the following key principles that were agreed upon to guide the Electricity Industry Restructuring process;
 - a. Restructuring must be conducted in accordance with the Constitution, taking into account that the responsibility of electricity reticulation is a municipal function;
 - b. The Financial state of municipalities currently performing the electricity function must not be adversely affected;
 - c. Any RED end-state model must meet the restructuring objectives set out in the EDI Blueprint that was approved by Cabinet earlier.

END