

Electricity distribution / Anton Eberhard

## Power policy at a crossroads

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In the coming weeks, cabinet and parliament will make decisions with far-reaching consequences for the reliability and affordability of electricity services for all of us. These decisions will either lay a foundation for improved services or increase the risks of black-outs and rising prices as currently experienced in Johannesburg and many other municipalities around the country.

At the heart of these decisions is the role of municipalities in the distribution of electricity services. A cabinet memorandum is being prepared by the Department of Minerals and Energy that will report on progress with sorting out the festering problems in this sector and will make certain policy proposals. At the same time, Parliament will consider a new Electricity Regulation Bill. Both initiatives may take the wrong turn.

The solution to the country's electricity distribution problems has been debated for over a decade. During this time municipal electricity providers have grown less reliable due to insufficient investment in the maintenance of municipal infrastructure – notwithstanding the existence of large trading surpluses due to rising consumer tariffs. The slow progress with industry restructuring has failed to achieve economies of scale and has led to a steady loss of skills and capacity.

Residents in Johannesburg now take it for granted that some traffic lights and areas of the city will be without power on a daily basis. City Power spokespersons urge residents, institutions and businesses to invest in back-up power supplies. They continue to remind us that many components of the electricity network are more than 30 years old - but they do not explain why there has been insufficient investment in renewing these assets.

This problem has deep structural roots. Municipalities face contradictory incentives in managing and regulating electricity distribution services. On the one hand municipal councillors face pressure to lower electricity prices, sometimes even below the cost of provision. On the other hand they have an incentive to maximize revenue from their electricity assets. Unfortunately surpluses have been diverted and investment in extending electricity assets has suffered at the expense of other capital priorities. Sadly, the conflict between these governance roles is seldom understood and has yet to be resolved.

So what should be done? Over the past 12 years, the ANC government has engaged all stakeholders and won approval that the electricity distribution assets and staff of all municipalities and Eskom should be consolidated into six Regional Electricity Distribution companies (REDs) that cover the entire country. The intention was that the REDs would be publicly-owned and would be regulated by the National Electricity Regulator in order to achieve an appropriate balance between financial viability, efficient operation and affordable tariffs for customers.

However, a draft cabinet memo now appears to take a different position altogether. Through the intervention of National Treasury officials the version that may be taken to Cabinet says that the future should be more of the same: i.e. a few more municipal entities like City Power in Johannesburg (plus the takeover of some Eskom distribution assets) in each of the five largest metro areas. And the remaining small municipalities scattered around the country will somehow be combined into a sixth RED – a proposal that negates the rationale for creating viable, efficient distribution companies.

At the same time, National Treasury officials have rewritten chapters in the draft Electricity Regulation Bill that effectively remove the National Electricity Regulator's (NER) powers to regulate municipal electricity reticulation services, i.e. the majority of electricity consumers in South Africa! Are these proposals serious? Unfortunately, yes.

Perhaps there is insufficient understanding that electricity distribution is unlike other municipal services such as garbage removal or paving roads. Electricity investments are huge, often beyond the means of smaller municipalities. The industry demonstrates clear economies of scale – the key rationale behind the six RED model.

Elements of the electricity industry are natural monopolies and therefore need to be regulated to protect consumers. The NER has restrained Eskom's monopoly pricing in the generation and transmission sectors – but the draft Electricity Regulation Bill will effectively prevent the NER from regulating the final distribution stage in the value chain. Upstream gains may therefore never reach the end consumer. Clearly, this does not make sense.

Why do officials from National Treasury appear to be acting against the national interest and sabotaging a decade's worth of policy consensus? The answer appears to lie in their interpretation of the Constitutional provision that grants municipalities executive and administrative powers over electricity reticulation within their municipal areas. To the extent that municipalities represent local interests they have an important planning role in service delivery. They can set targets and monitor progress. But this does not mean that they have to actually operate electricity distribution businesses or that they have exclusive rights to set tariffs and expropriate surpluses.

National Treasury officials are taking a fundamentalist view of the Constitution; one that gives municipalities unfettered powers over all aspects of electricity reticulation. This is a peculiar and myopic view. It ignores the problems explained above. It ignores the fact that most counties around the world do not allocate electricity distribution to municipalities (just as they do not allocate other national infrastructure services such as telecommunications). It is not even clear that these officials represent the view of their minister who is surely committed to a solution that guarantees reliable and competitively priced electricity services to all businesses and households.

Let's hope that sense will prevail and that cabinet and Parliament will consolidate the progress being made by the Department of Minerals and Energy, the EDI Holdings

Company and the National Electricity Regulator, who are committed to the rationalisation and regulation of the entire distribution industry in order to secure reliable and affordable electricity services for all.

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