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EDI RESTRUCTURING PROCESS UPDATE AND THE WAY FORWARD

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■ Introduction

The purpose of this paper is to provide a high level update on the Electricity Distribution Industry (EDI) restructuring process to date and the envisaged EDI reform journey ahead from an EDI Holdings perspective.

EDI Holdings was established by the Government to direct and oversee the restructuring of the EDI and started to operate in June 2003. EDI Holdings reports to the Department of Minerals and Energy (DME), the Ministry charged with the responsibility for the EDI restructuring programme.

■ EDI Restructuring Objectives

The EDI is highly fragmented leading to lost economies of scale; financial disparities between distributors; disparities in tariffs and uneven capacity to extend electricity services to poor households.

Since inception of the EDI restructuring process the Government has been consistent in the objectives of the restructuring and there has never been any doubt in terms of the expectations of the Government in this regard. The Energy White Paper of 1998 in no uncertain terms articulated amongst others, the seven restructuring objectives as indicated in the table below. Furthermore the EDI Restructuring Blue Print, of which the thrust was approved by Cabinet during 2001, was to serve as the guiding document for the EDI restructuring, it reconfirmed the objectives articulated in the Energy White Paper and also provided a level of clarity in terms of the expectation on how the Regional Electricity Distributors (REDs) will contribute to the achieving of the key objectives. A central feature of the Blueprint is the requirement that the EDI be consolidated into 6 financially viable REDs, in order to achieve the objectives of restructuring.

The Energy White Paper of 1998 and the EDI Restructuring Blue Print therefore remain important documents to serve as reference points and to assist in measuring the restructuring progress as well as the degree to which the EDI Restructuring objectives are met.

Energy White Paper Objectives (1998)	EDI Restructuring Blueprint Objectives (2001)
<ul style="list-style-type: none"> • Ensure electrification targets are met 	<ul style="list-style-type: none"> • Achievement of government's electrification programme • Universal access to electricity for all South Africans
<ul style="list-style-type: none"> • Provide low-cost electricity • Facilitate better price equality 	<ul style="list-style-type: none"> • Sustainable electricity supply to low-income consumers, regardless of location, at affordable prices
<ul style="list-style-type: none"> • Improve the financial health of the industry 	<ul style="list-style-type: none"> • Future REDs to operate on a sustained, financially viable basis as independent businesses
<ul style="list-style-type: none"> • Improve quality of service and supply • Foster proper co-ordination of operations and investment capital 	<ul style="list-style-type: none"> • Acceptable and sustainable levels of supply security and quality
<ul style="list-style-type: none"> • Attract and retain competent employees 	<ul style="list-style-type: none"> • Future REDs to provide secure employment to their employees, provide skills development and training consistent with a high technology, modern distribution business • Transition to be done within the context of a comprehensive human resources strategy and an agreed social plan
	<ul style="list-style-type: none"> • Planned and managed transition

■ EDI Restructuring Journey to Date

The EDI Restructuring Journey to date has not been an easy process and numerous factors have played a key role in the slow restructuring progress experienced to date. South Africa is one of the very few countries in the world that has initiated the restructuring of the electricity distribution industry in an environment where the participation is voluntary. Given the considerable debate which started way back in the early 1990's and which resulted in the 1997 ERIC report which supported the concept of REDs, it could be argued that the restructuring journey has been in progress for more than a decade.

The fact that the President, in the State of the Nation Address in 2004, indicated that the first RED would be established during 2005 provides an indication of the importance of the restructuring process from a Government perspective. It is widely acknowledge that the EDI plays a vital role in the economy of this country and is perhaps one of the most important vehicles to be used in the improvement of service delivery as well as providing basic electricity to the many people in the country who still not enjoy the benefits to be derived from electricity. The first RED, namely RED 1, anchored around the City of Cape Town, was established on the first of July 2005. On 14th September 2005 Cabinet considered the progress towards the establishment of REDs as well as some of the concerns raised by stakeholders. These concerns *inter alia* included the financial impact on the municipalities and Eskom, the cost of salary harmonisation etc. Cabinet then resolved to proceed with the establishment of six Metro REDs and requested that a feasibility study be conducted, through modelling, to evaluate amongst others, the feasibility of establishing a National RED; clusters; and neighbouring municipalities joining the Metro RED. EDI Holdings was charged with the responsibility to conduct the feasibility study. A process was

followed which allowed for transparency and maximum stakeholder participation. The results of the feasibility study were submitted during April 2006 to the Honourable Minister of Minerals and Energy.

Notwithstanding all the challenges, amongst others the ambivalent stakeholder support, significant progress has been made to date with reference to the RED creation process. The following achievements, *inter alia*, were realised:

- * Metro RED creation governance structures established and operating
 - Sponsors Committees
 - Technical Steering Committees
 - Work Groups
- * Metro RED DAY ONE Roadmaps and work plans developed
- * Various municipalities engaged in ringfencing in preparation for the RED creation:
 - 6 Metros have generally made good progress
 - 11 Municipalities are at various levels of progress
- * Eskom restructured its distribution business from 7 Regions to 6 Regions in line with the EDI Blueprint six wall to wall boundary recommendation
- * Significant contributions were made in terms of assistance towards the resolving of the outstanding legislative requirements
- * Transitional Labour Relations Structure (TLRS) established and functioning very effectively
- * Extensive industry modelling completed
- * Industry modelling report submitted to the Department of Minerals and Energy
- * Significant industry restructuring and best practices experience and knowledge developed
- * Enterprise wide programme management capability established

■ Experience & Lessons to Date

The experience gained through the establishment of the first RED serves as a very important reference point on the way forward. Without the transfer of the legacy electricity businesses to the relevant RED it is hardly possible to create viable operating entities. Furthermore, misaligned interests and ambivalent support from some key stakeholders is not assisting the restructuring process.

The following points provide some indication of the obstacles experienced to date in the establishment of RED 1 and the work done to date in establishing the Metro REDs. These matters need urgent attention to ensure progress in the establishment of the REDs. These points are:

- Voluntary mode of reform
- Absence of an enabling legislative framework
- Incompleteness and misalignment of existing legislative regime
 - Asset transfer from the City of Cape Town to RED 1 is delayed due to lack of prescribed asset transfer framework in terms of the MFMA
 - Asset transfer from Eskom to RED 1 is delayed due to suspensive conditions imposed by Eskom
 - EDI Restructuring Bill is an imperative to set clear policy guidelines for EDI restructuring implementation
 - The municipal entity governance regime is cumbersome and constraining

- Separating out of customers, networks and systems to create a Metro RED is extremely complex and does not contribute towards accelerated RED creation or leveraging existing investments in the Industry
- To create a Metro RED significant investments are required upfront which will not contribute to improved business performance but merely to meet the boundary reconfiguration requirements
- The negotiated nature of restructuring makes it impossible to deliver on the anticipated objectives and outcomes within the stipulated timeframes
- The current performance of the EDI is deteriorating

In addition to the above challenges there are a number of outstanding policy and legislative matters which call for urgent attention as they directly contribute to the delay in the RED creation process:

Unresolved Policy Matters

- End State pronouncement
- Local Government Surcharge Principles
- Compensation for asset contribution
- Shareholding
- Tax issues
- Ownership and Governance of the REDs
- Asset transfer framework

Lack of enabling Legislation

- EDI Restructuring Bill
- Exemptions from compliance to onerous legislative provisions contained in, for example, MFMA and Systems Act

■ **RED Creation Journey Ahead**

EDI Holdings have every confidence in Government and there is no doubt that the Government is committed to the EDI reform process and will pursue a model which will serve the best interest of South Africa and its people. Based on extensive research, lessons learnt and experience to date, EDI Holdings is convinced that the 6 wall to wall RED model, as approved by Cabinet in May 2001, remains the most appropriate option for the EDI in South Africa.

Furthermore based on legal analysis, lessons learnt and experience to date:

- REDs should be established as public entities
- The EDI Restructuring should take place on a mandatory basis, supported by the necessary enabling legislation

With reference to the RED creation journey ahead, the current negotiation and EDI reform governance arrangements will be leveraged in aligning the current RED creation activities with the final Cabinet Decision. The work done and lessons learnt through the establishment of RED 1 and in preparation of the METRO REDs will, amongst others, be used to inform the RED creation journey ahead. South Africa is in the fortunate position to exploit opportunities to learn from the international experience in electricity distribution reform.

The importance of all stakeholders is acknowledged and therefore the stakeholder engagement will be intensified to enhance engagement on the way forward and to address potential uncertainties. It is envisaged that the Multi Stakeholder Forum (MSF) will be revived to facilitate *inter alia* the resolving of the outstanding policy matters

■ Conclusion

The EDI restructuring journey to date has had many obstacles and taking this into account, good progress in terms of the EDI restructuring has been made to date. The Government has allowed for a very transparent and participative process in terms of the restructuring and EDI Holdings has utilised these opportunities in the National interest.

A decision by Government on the EDI model and way forward is imminent. Based on the level of readiness, understanding of the EDI and stakeholder relationship, EDI Holdings is committed to deliver the EDI model in line with the final Cabinet Decision in this regard. EDI Holdings wish to thank all the stakeholders who have made a positive contribution towards the restructuring process. Without the support of all the stakeholders, this journey has the potential of being a very difficult one. In conclusion, EDI Holdings appeals to all the stakeholders and in particular the industry leadership, to commit to the restructuring process and to proactively participate in this journey in the best interests of South Africa and its people.