



**CITY OF CAPE TOWN
ISIXEKO SASEKAPA
STAD KAAPSTAD**

Making progress possible. Together.

THE EXECUTIVE MAYOR

Mayor's Suite, 6th Floor, Podium Block
Cape Town Civic Centre, 12 Hertzog Boulevard
Cape Town
8001

T: 021 4001300 F: 021 400 1313
E: mayor.mayor@capetown.gov.za

Submitted via email to mypd@nersa.org.za

SUBMISSION BY GEORDIN HILL-LEWIS, MAYOR OF CAPE TOWN

RE: ESKOM'S FIVE-YEAR MULTI-YEAR PRICE DETERMINATION, 2023

14 January 2022

EXECUTIVE SUMMARY

The City of Cape Town submits that Nersa must reject Eskom's application to increase the price of electricity by 20,5% in the 2022/3 financial year. A more reasonable alternative would be to bring the increase in line with the Consumer Price Index (CPI) of 5,5%. The City further notes that further increases are planned in future, including an increase of 15.07% in 2023/4 and of 10% in 2024/5.

Capetonians simply cannot afford these increases. They are unfair, unaffordable and unjust. Like the majority of South Africans, many Capetonians are struggling to make ends meet. The pandemic and national lockdown led to the closure of hundreds of businesses in our City and the loss of thousands of jobs. Despite Cape Town having one of the lowest unemployment rates in the country, our residents are faltering under the burden of the rising costs of energy, fuel, food, and basic consumer goods.

The price of electricity has risen by 307% over the past 13 years, far exceeding inflation. On another method of calculation, over a 15-year period, the average price charged by Eskom for electricity has increased from 19.80c/kWh (in 2007) to 127.63c/kWh (in 2021). This is an increase of 544%.

Over this time, in which Capetonians have been bearing the costs of above-inflation increases in the price of electricity, they have also experienced an increasingly unreliable electricity supply. Rolling blackouts began in 2007, with 2020 and 2021 being two of the worst loadshedding years on record.

I have personally acknowledged Eskom CEO Mr André De Ruyter's ongoing effort to stabilise the utility's finances and have applauded his efforts in this regard. I have also acknowledged that Eskom clearly needs to take further urgent steps to reduce its debt and improve its financial sustainability.

However, passing the bill on to struggling consumers should not be the default solution, and Nersa should not allow this. We call on Nersa not to underestimate the harsh economic realities on the ground: our people are struggling to survive amidst increased costs of living, including electricity.

As we are not oblivious to Eskom's financial pressures, we have made proactive suggestions to Eskom in respect of alternative strategies to achieving financial sustainability.

These include:

- Urgently reducing Eskom's bloated payroll;
- Cancelling tenders with unscrupulous suppliers who provide Eskom with goods and services at massively inflated prices;
- Ending corruption and mismanagement (irregular, fruitless and wasteful expenditure cost the utility R14,6 billion in 2020 and R7,4 billion in 2019);
- Recovering money that has been looted during the period of state capture; and

- Adopting a greater focus on recovering debt from defaulters rather than targeting those who are paying their bills, who have in effect become 'soft targets'.

It is an extreme injustice that ordinary Capetonians — and, indeed, residents of every municipality in the country — will be forced to bear the cost of Eskom's inability to fix its own problems. Moreover, the planned increase will further limit struggling businesses' ability to operate profitably, and to sustain and create jobs. It will destroy hope of economic recovery in South Africa and add to our burden of poverty.

We would like to reiterate that the economic and social costs of Eskom's desired increase will be dire. The City of Cape Town requests and requires Nersa to say, "No".

DETAILED SUBMISSIONS

Municipal financing

The City of Cape Town has limited sources of income. Chiefly, the City's income derives from:

- Its equitable share from National Treasury;
- Rates on property;
- Licensing fees and fines; and
- Surcharges on the provision of services like electricity and water.

Abnormal price increases on electricity, such as that proposed in Eskom's latest 2023 MYPD application, reduce the demand on electricity. This, in turn, reduces the amount of electricity the City sells to consumers, limiting the ability to generate revenue. Customers that are able to defect from the grid do so in increasing numbers when electricity costs outweigh the cost of self-generation. Higher electricity costs also create further incentives for the theft of electricity. The result of each of these things is reduced income for the City.

In the past, the City has absorbed some of the costs of Eskom's increases, in the interests of safeguarding our residents' household income and the City's economy. In the 2020/1 financial year, the City only passed on a 13.48% increase in electricity prices to its customers, as opposed to the 17% increase in prices from Eskom, which was approved by Nersa. These cost absorptions are a significant financial burden for the City.

When Eskom increases the price of electricity, this erodes the ability of the City to cross-subsidise the provision of other, less (or non-) financially viable services, including free electricity for the indigent, infrastructure maintenance, housing, and services for the homeless. To ensure it can continue delivering these critical social goods, the City is forced to lean more on the ratepayer base which, justifiably, often results in mistrust and discontent on the part of ratepayers.

South African municipalities, like Cape Town, who loyally pay what they owe to Eskom for the electricity they sell on to residents, are approaching a tipping point in respect of their ability to financially survive these exorbitant increases.

General economic costs and Eskom's debt burden

Rising living costs force more households into poverty, increasing their reliance on the struggling fiscus for social support. Further, the demand side of the South African economy faces pressure every time consumers are forced to spend more on basic living costs, reducing their purchasing power for other consumer goods. The economic ramifications of Eskom's price increases are thus far-reaching and significant.

Eskom is incapacitated by a debt burden that exceeds R450-billion. The misappropriation of funds, a bloated organisational structure as well as glaring inefficiencies its operations have contributed to the utility's burgeoning debt. If it were a private company competing in the free market, Eskom would have failed many years ago. Instead, because of its monopoly and the support of the state, it

has been kept alive by bailouts from South African taxpayers and the exorbitant prices paid by electricity consumers.

Several alternative mechanisms of achieving financial sustainability have been suggested to Eskom by economists; mechanisms which would not further burden struggling Cape Town households. It is not acceptable that Capetonians are tasked with salvaging Eskom and rescuing it from its debt spiral, especially when alternatives exist.

It is therefore imperative that municipalities, which make up 42% of Eskom's customer base, express their opposition to any poorly motivated or conceived increase to the price of electricity. Questions regarding the methodology employed in arriving at the proposed tariff increases have been posed by SALGA members. The City of Cape Town will not repeat these, other than to question whether in fact Eskom has truly employed efficiency in its estimations of costs to be incurred.

Quantum of the increase

The City is vehemently opposed to the quantum of the increase, which is roughly four times the recently stated CPI of 5,5%. This will have negative economic and social impacts, with electricity becoming unaffordable for both commercial and residential customers. It will also have the effect of denying a growing segment of the citizenry the right to access basic municipal services, and electricity in particular. Thus, it has a significant negative impact from a constitutional and service delivery perspective.

The City reserves its right to challenge the proposed increase in an appropriate legal forum. The ability of the City to provide a lifeline tariff to its indigent customers is threatened, which will plunge this segment of the market even deeper into energy poverty.

Impact of arrear debt

The City of Cape Town diligently pays over all the money it owes to Eskom in respect of its purchase of electricity and has never been in arrear debt. Sadly, this is not the case in respect of dozens of other South African municipalities, which owe Eskom significant amounts of money, in some cases running into the billions of Rand.

Eskom's calculations in respect of the increase requested incorporate the arrear debt owed to Eskom by errant municipalities. Incorporating this arrear debt into the calculations effectively spreads the burden amongst all municipalities including those who are not in arrears. Thus, a cross-subsidy situation is created which is constitutionally and administratively unfair and irregular, in that it penalises compliant municipalities and their residents.

The City reserves the right to challenge the incorporation of arrear debt into the calculations. Compliant metros, such as the City of Cape Town and its customers, become a "soft target" for the national utility. This is a perverse practice, which must be eradicated before it erodes the financial viability of the compliant municipalities.

Eskom's rising fuel costs and declining plant efficiency

Eskom has built its rising fuel costs (mainly that of coal) into the calculation matrix. The City believes that Eskom should radically review the pricing of its coal supply contracts with a view to reducing its fuel costs or offer a plausible reason why this cannot be done.

The City reserves the right to require full disclosure of information regarding coal supply contracts in terms of the Promotion of Access to Information Act.

It must further be noted that the net efficiency of Eskom's thermal plants continues to decline, requiring incrementally more coal to maintain efficiency levels. With fuel pricing that is not transparent, Eskom's customers can anticipate even more increases to the tariff to cater for the decline in efficiency in plant performance. What is required and expected, however, is that the cost of primary fuel should

decrease over time, as aged plants are decommissioned, and the energy availability factor remains historically low (61% in 2021). This does not appear to be the case in the compilation of this tariff application.

In the absence of a bona fide review into the rising costs of its coal contracts, the declining quality of coal sold to Eskom, and declining plant efficiency, it is unacceptable to pass the financial implications of these on to Capetonian households.

Costs of maintenance

The surcharges levied by the City on the sale of electricity fund the maintenance of municipal reticulation infrastructure. With decreased revenue from electricity sales by the mechanisms described above, the recovery of the basic costs for maintenance will also be significantly eroded, leading to decreased maintenance, and increased network outages. This is an unacceptable situation in light of the City's constitutional obligation to deliver basic services to all our residents.

As highlighted above, the City, in the interests of safeguarding its residents and the economy, tries to absorb part of Eskom's cost increases. This is partly enabled by improving efficiency in its operations, but also by cutting back on the filling of vacancies in essential positions. In addition, the City has had to restrict the recovery of the fixed service charge on its Home User Tariff to the bare minimum, with the eventual outcome being insufficient recovery to meet future network growth and refurbishment demands.

Put simply, this price increase will put our reticulation infrastructure — and therefore our electricity supply — at risk.

Loadshedding and electricity supply reliability

Importantly, this above-inflation increase offers no guarantee of alleviating loadshedding in the near future. Despite calls for service delivery agreements to be

put in place between Eskom and distributors such as the City of Cape Town, these have not been forthcoming.

The current legal matter before the High Court, in which SALGA is challenging Eskom on matters that include service delivery agreements, will have an impact on electricity pricing if SALGA succeeds. Eskom will be required to maintain acceptable standards in terms of quality of supply and this will likely result in even higher increases being sought. Eskom needs to urgently address quality of supply concerns, including the imposition of loadshedding on its customers. Measures that limit loadshedding need to be identified, tested and communicated effectively, without placing further strain on municipalities' finances.

Cost breakdown of increase

Eskom claims that about 13% of the 20.5% increase is to help cover the costs of power procurement from Independent Power Producers. This means that about 7% of the increase is attributed to generation, transmission and distribution cost recovery. It raises concerns that there is not adequate planning in place for growth and refurbishment of transmission and distribution assets. This will have a material impact on the security of supply of distributors — like the City of Cape Town — who rely on the integrity of the high- and medium-Voltage network of Eskom as feeders into distributor networks.

CONCLUDING REMARKS

The push by Eskom to cost reflectivity in its pricing does not factor in the historical legacy of inefficiency, which is then entrenched as part of a baseline. Eskom needs to revisit its baseline costs to determine where efficiency improvements are possible. A further cause for concern is ensuring environmentally non-compliant plants are brought in line with emission permit requirements. Aged plants, in particular, will require significant investment to ensure emissions are in line with permitted levels.

The City of Cape Town notes that a portion of the proposed increase (1.09% of 20.5%) is meant to help Eskom meet its obligations to pay National Treasury's carbon tax. While we recognise the urgent need for government to adopt measures to combat climate change, we urge reconsideration of this tax, the effects of which are deeply regressive.

There has been a perceived lack of transparency with respect to the compilation of Eskom's latest tariff application. Important information, such as that relating to plant efficiency degradation, coal contracts, restructuring plans (amongst others) has not been made available. Since these influence price increases significantly, it is imperative that this information is shared with key stakeholders before a determination is made.

Price certainty, entailing long-term pricing signals to industry, is required to ensure we our economy retains critical industries and related jobs.

Finally, and most importantly, Eskom seems oblivious to the plight of the indigent and municipalities who rely on electricity revenues to provide other critical services to their residents. The proposed increases by Eskom over the MYPD timeframe serve only to further entrench energy poverty and limit economic growth indefinitely, preventing economic upliftment.

A radical change in mindset is needed to address Eskom's financial woes without compromising the ability of municipalities to provide services in line with their constitutional mandate.

I reiterate the stance of the City of Cape Town, which is an unequivocal rejection of any price increases in electricity above inflation. The City remains committed to working with all stakeholders to find a more acceptable solution to the challenges facing Eskom and the electricity industry.

ENDS.