WERKSMANS
ATTORNEYS

INFRASTRUCTURE & ENERGY

Why Government should accelerate the establishment of an independent system and market operator?

15 March 2021 *6 min read*

By Nozipho Bhengu, Director and Tsebo Masia, Associate

- On 15 February 2021, the CEO of Eskom SOC Limited ("Eskom"), Mr Andre de Ruyter made a much welcome announcement that the independent system and market operator will be in place by 2022. This was a clear acknowledgement that, as part of the process of unbundling Eskom, Government needs to accelerate the establishment of an independent system and market operator as a state owned entity. Legislative reforms to create the independent system and market operator were first commenced in 2011 by the Department of Energy by publishing the Independent System and Market Operator Bill, 2011 ("ISMO Bill"). Since then, not much has happened to finalise and pass the ISMO Bill into law.
- The main objects of the ISMO Bill are to establish an independent system and market operator (ISMO) as a state owned entity which will, *inter alia*, be responsible for the planning of supply of electricity by generators of electricity through the national grid, the transmission and operation of the national grid, the buying of electricity from generators and the sale of electricity to distributors and large customers. In essence, the ISMO Bill contemplates that the functions of the planning of supply of electricity, the buying and the selling of electricity will be transferred from Eskom to an independent body, namely the ISMO, which shall be free and independent from any industry participants, particularly power generators.
- Currently Eskom operates as a "monopoly" in the sense that it controls the generation, transmission and a significant portion of the distribution of electricity in South Africa. This current structure is not only outdated and inefficient but it allows Eskom to have enormous power and control over the power generation, transmission and distribution facilities. Eskom currently generates over 90% of the country's electricity. This concentration of power has, in the past, sadly resulted in Eskom sometimes protecting its dominant market position at the expense of independent power producers. Furthermore it has undermined the implementation of the national energy policy. Evidence of this was Eskom's refusal to sign the power purchase agreements with the independent power producers a few years ago which had disastrous consequences for the Renewable Energy Independent Power Producers Programme in South Africa. It is now widely accepted that the establishment of the ISMO will resolve the inherent conflict of interest arising from Eskom's current position as a generator, transmitter and distributor of electricity and level the playing fields by ensuring equal treatment of all power generators including the independent power producers and Eskom. Furthermore, market sentiment indicates that having an "independent and unconflicted" grid operator and consequently equitable access by all power producers to the national grid will boost investor confidence in the South African power industry, including the renewable energy sector which, in turn, is likely to attract increased private sector investment in the South African power sector.
- In order to accelerate the establishment of the ISMO, the main starting point will be to prioritise the finalisation and passing into law of the ISMO Bill. As noted above, the ISMO Bill contemplates the establishment of a state owned entity to be known as the Independent System and Market Operator SOC Limited. Government will be the sole shareholder of the ISMO. The main functions of the ISMO will include, *inter alia*, the planning of supply of electricity by generators, system operation, market operation including the procurement and sale of electricity. The Bill provides that the ISMO will be managed by an independent board of directors, the majority of whom shall be non executive directors. In order to ensure that the process of appointing the non executive members of the board of directors of the ISMO is transparent and represents a sufficient spread of skills, knowledge, qualifications and experience to enable it to function efficiently and effectively, the ISMO Bill provides that the process of appointing the board of directors of the ISMO will be conducted by a nominations committee. The ISMO Bill also deals with, *inter alia*, –
    - the appointment of the ISMO staff, including the Chief Executive Officer and the Chief Financial Officer;

- the transfer of assets, rights, liabilities and obligations required by the ISMO to perform its functions and personnel of Eskom performing functions pertaining to the ISMO; and
- the funding of the ISMO. The ISMO Bill envisages that all of the ISMO's normal costs should be recovered from tariffs, fees and charges to ISMO Customers and further that the ISMO may, subject to compliance with its Memorandum of Incorporation, the Public Finance Management Act and the Companies Act, borrow money or arrange for facilities to meet its capital and operational requirements.

- It is worth noting that, as currently drafted, the ISMO Bill merely deals with the operation of the transmission system and does not deal with the ownership and maintenance of the transmission system. In this regard, the ISMO Bill should clarify therein whether the ownership and maintenance of the transmission assets will be transferred to the ISMO or remain with Eskom or a subsidiary of Eskom. It is submitted that the ISMO does not necessarily have to own and maintain the transmission assets but consideration should be given to transferring ownership and maintenance of the transmission assets to an independent entity as it would be an untenable position and possibly frustrate the objectives of the ISMO if Eskom as a generator of electricity continues to own and maintain the transmission assets in a competitive environment. If however Government's position is that ownership and maintenance of the transmission should remain with Eskom, strict regulation will need to be put in place in order to guarantee equal and fair access to the transmission system by all generators.
- In conclusion, we wish to highlight that it is unsustainable that Eskom should remain a player and a purchaser of electricity in a competitive environment. Accordingly, in order to resolve this, Government is urged to –
  - in the best interest of all industry players in the power market, accelerate the establishment of the ISMO;
  - clarify who will own the national transmission assets – will it be the ISMO, Eskom or another independent body; and
  - to the extent Government's intention is to have ownership and maintenance of the transmission assets remain with Eskom and not an independent party, introduce regulation as to how equal and fair access to the national grid by all generators will be guaranteed.



Nozipho Bhengu

Director

View Profile