**3. REPORT OF THE STANDING COMMITTEE ON APPROPRIATIONS ON ITS OVERSIGHT VISIT TO ESKOM HOLDINGS SOC LIMITED FROM 14 TO 16 OCTOBER 2019, DATED 27 NOVEMBER 2019**

The Standing Committee on Appropriations, having undertaken an oversight visit to the Eskom Holdings SOC Limited from 14 to 16 October 2019, reports as follows:

**1. Introduction**

The Standing Committee on Appropriations (the Committee) is established in terms of section 4(3) of the Money Bills Amendment Procedure and Related Matters Act, No.9 of 2009. The Act requires the Committee to consider and report on:

* Spending issues;
* Amendments to the Division of Revenue Bill, the Appropriation Bill, Supplementary Appropriation Bill and the Adjusted Appropriation Bill;
* Recommendations of the Financial and Fiscal Commission (FFC), including those referred to in the Intergovernmental Fiscal Relations Act, 1997 (Act No. 97 of 1997);
* Reports on actual expenditure published by the National Treasury (section 32 reports); and
* Any other related matters.

Within the current difficult fiscal context and limited resources, the Committee is of the view that all programmes, projects and activities appropriated should be rolled out in an effective and efficient manner, and in compliance with the relevant laws and regulations. This means that all state organs must take active steps to improve operational efficiencies, accelerate the effectiveness of service delivery, and attain value for money.

The Committee undertook an oversight visit to the Gauteng Province in order to visit Eskom Holdings SOC Limited to engage with the leadership as well as organised labour with a view to addressing institutional instability, weak governance, non-compliance with procurement prescripts, liquidity constraints, and cost escalations due to delays and design defects in capital projects (Medupi and Kusile Power Stations, in particular).

**2. Delegation**

The delegation was as follows: Mr S Buthelezi (Chairperson), Mr XS Qayiso (ANC), Ms D Peters (ANC), Ms C Dikgale (ANC), Mr Z Mlenzana (ANC), Mr OM Mathafa (ANC), Mr D Joseph (DA), Ms RN Komane (EFF), and Mr NLS Kwankwa (UDM). The delegation was accompanied by the following parliamentary officials: Mr D Arends (Committee Secretary), Mr S Magagula (Content Advisor), Mr M Zamisa (Committee Researcher), Ms N Chaso (Committee Assistant), and Ms F Lombard (Parliamentary Communication Specialist).

The Committee met with the following stakeholders at the various sites and stakeholder meetings during the oversight visit:

**Department of Public Enterprises:** Ms M Makololo (Acting Deputy Director-General: Energy), Mr L Tekane

**National Treasury:** Ms T Moahloli (Acting Deputy Director-General: Asset and Liability Management), Mr R Rajlal (Chief Director: Sectoral Oversight); Mr JZ Quvane (Director), and Ms MBN Mathekga (Director)

**Sizwe Ntsaluba Gobodo: Grant Thornton:** Mr S Vilakazi (Director); Ms N Ngobese (Director)

**Auditor General South Africa**: Mr SJ Sybrand Struwig (Senior Manager)

**Eskom Holdings SOC Limited:** Mr J Mabuza (Acting Chief Executive Officer and Interim Executive Chairperson), Prof T Mongalo (Board Member), Mr J Oberholzer (Chief Operating Officer), Mr C Cassim (Chief Financial Officer), Mr B Nxumalo (Group Executive Generation), Mr S Scheppers (Group Executive Transmission), Mr M Bala (Group Executive Distribution), Mr M Buys (General Manager: Finance), Ms H Tlhotlhalemaje (General Manager: Regulation), Ms R Waja (Acting General Manager: Corporate Affairs), Mr A Etzinger (General Manager: Sustainability and Risk), Ms S Pule (Group Executive: Human Resources), Mr J Mthembu (Acting Group Executive: Legal), Mr I Bhowani (Acting General Manager: Assurance and Forensic), Mr S Tshitangano (General Manager: Procurement), Mr D Mashego (Acting General Manager: Primary Energy), Mr I Bhowani (Acting General Manager: Assurance and Forensics), Mr B Hewu (Acting Group Executive: Governance [Legal]), Mr K Bowan (Middle Manager: Wholesale), Ms N Sigwebela (Senior Manager: Energy Planning), Mr P le Roux (General Manager: Procurement Strategy and Excellence), Mr A Laher (Senior Manager: Compliance),

**Eskom Board:** Mr J Mabuza (Chairperson), Dr R Crompton, Dr BCE Makhubela, Ms B Mavuso, Dr P Molokwane, Ms S Mabaso-Koyana, Mr M Mvunelwa, and Mr M Tyalimpi (Board Company Secretary)

**Financial and Fiscal Commission:** Prof D Plaatjies (Chairperson)

**National Union of Metalworkers of South Africa:** Mr I Jim, Mr N Kgoete, Mr B Kola, Ms W Pram, Ms N Letlape, Mr Z Gqina, Ms P Hlubi-Majola,

**Solidarity:** Mr T Weddespon, Mr J Fernandez, Mr T Jacobs, Mr D Jennings

**National Union of Mineworkers:** Ms K Pholoba, Mr P Mashego, Mr K Baloyi

**3. Background**

Eskom Holdings SOC Limited, herein after referred to Eskom, plays a vital role in the South African economy and contributes massively to infrastructure spending. The power utility is set to spend R134.3 billion on infrastructure over the 2019 Medium Term Expenditure Framework (MTEF). Therefore, it is critical to the achievement of the National Development Plan (NDP) Outcomes, economic growth, skills development and job creation. Whereas Eskom accounts for 70 per cent of South Africa’s debt, it faces significant challenges related to leadership instability, weak governance, liquidity constraints, and cost escalations due to delays and defects in construction of capital projects. The Committee has appropriated significant financial resources to Eskom over the past financial years, therefore it is critical to conduct an oversight visit to the power utility in order to come up with sustainable interventions.

The Committee is expected to and has appropriated significant financial resources to support Eskom in the recent past. For instance:

* On 10 September 2019 Eskom appeared before the SCOA for a briefing on the proposed special appropriations amounting to R59 billion for the 2019/20 and 2020/21 financial years.
* Similarly, in 2015 the Committee passed a Special Appropriation Bill through which it allocated a total of R23 billion[[1]](#footnote-1); and
* The Committee also passed the Eskom Subordinated Loan Special Appropriation Amendment Act (2008/09-2010/11 Financial Years) in 2015. The objective of the Bill, which was later enacted into law, was to convert the subordinated loan to Eskom Holdings SOC Limited in the amount of R60 billion over the said financial years into shares for the State[[2]](#footnote-2).

In the light of the above, it was critical for the Committee to conduct an oversight visit to Eskom in order to gain a deeper understanding of challenges facing the power utility and to come up with sustainable interventions. The following section outlines key objectives of the oversight visit.

* 1. **Key Objectives of the Visit to Eskom**

The Committee visited Eskom to meet with leadership and Executives as well as other key stakeholders for extensive discussions and comprehensive reports on the following areas:

* Efficient, effective and economic use of financial support that Eskom has received through the appropriation process of Parliament;
* Plans for efficient, effective and economic use of the proposed special appropriation of R59 billion for 2019/20 and 2020/21;
* Expenditure and construction of capital projects including power plants such as Medupi and Kusile;
* Key challenges such as leadership instability, weak governance, weak internal controls, non-compliance with the PFMA and supply chain management (SCM) prescripts, deteriorating financial etcetera;
* Comprehensive and sustainable maintenance plan for power stations in order to avoid potential loss of power in the short term and a total system collapse in the long term;
* Plans regarding improvements in achieving performance targets outlined in the shareholder compact, especially those that relate to skills development and transformation;
* Effectiveness of internal controls and risk management systems and strategies;
* Eskom’s business model with its suppliers and Independent Power Producers (IPPs);
* Management of contractors involved in the construction of major power plants such as Medupi and Kusile, which have been subject to high project delays, structural defects, huge cost-overruns, and unwarranted costs for maintenance of structural defects;
* Status of compliance with the Public Finance Management Act (PFMA) and related supply chain management prescripts;
* Compliance with prescripts relating to promotion of local content and local suppliers; and
* Plan for effective change management in preparation for the planned restructuring process.

Based on the above objectives, the Committee also held a preparatory meeting with the representatives from the Office of the Auditor general South Africa (AGSA) and National Treasury 14 October 2019 to discuss the key financial matters of Eskom over the past five financial years. The Committee also held a series of meetings with Eskom’s Group Executives and the labour representatives at the Megawatt Park in Sunninghill, Johannesburg on 15 and 16 October 2019. The Committee also had a follow-up meeting with the Eskom’s Board in Parliament on 29 October 2019.

1. **Engagements with invited stakeholders**

The Committee had a preparatory meeting with the Auditor General South Africa, Sizwe Ntsaluba Gobodo: Grant Thornton, National Treasury and the Department of Public Enterprises on 14 October 2019 focusing on the key financial aspects and audit outcomes of Eskom. The said invited stakeholders were requested to make presentations followed by questions of clarification by the Committee. The main observations and findings stemming from the aforementioned discussions will form part of section 7 of the report.

1. **Engagements with the Eskom Board**

The Committee initially planned to engage with the Eskom Board during the oversight visit; however, the Committee decided that it would meet at a later stage due to the limited number of available Board Members. The meeting was rescheduled to 29 October 2019 in Parliament. The Committee engaged on the follow matters with the Board:

* Eskom’s financial performance for the past five financial years;
* Financial management and supply chain management matters at Eskom;
* Operational and financial risks/challenges facing the power utility;
* Human Resources and Labour Relations matters at Eskom; and
* Non-compliance with applicable legislation and regulations and mitigating measures.
1. **Engagements with Eskom Group Executives and Senior Managers**

The Committee met with the Group Executives for Capital, Generation, Transmission, Distribution, Human Resources, Legal, as well as the General Managers for Finance, Regulation, Corporate Affairs, Sustainability and Risk, and Assurance and Forensics.

Presentations were made by the afore-mentioned stakeholders followed by in-depth discussions between the Committee and invited stakeholders. The main observations and findings emanating from these discussions will form part of section 8 of the report. The following areas covered during the engagements with the Executive and Senior Management:

* Eskom’s financial performance for the past five financial years;
* Overview of municipal debt;
* Operational and financial risks/challenges;
* HR related challenges within Eskom;
* Eskom employees doing business with Eskom;
* The impact of dismissals, and termination of contracts on Eskom’s operations;
* Non-compliance with applicable legislation and mitigating measures;
* State of affairs/business at Eskom regarding procurement;
* Potential risks to procurement and SMC processes and mitigating factors;
* Cost of IPPs vs contribution to the electricity grid; and
* Challenges and costs associated with evergreen/long term contracts.
1. **Engagements with organised labour**

The Committee engaged with the National Union and Metalworkers South Africa (NUMSA), National Union of Mineworkers (NUM) and Solidarity around the labour related challenges facing Eskom’s staff and the likely impact of the restructuring on employees. The common areas for concern raised by the three unions included:

* The costs and ownership of IPPs within South Africa and its effect on Eskom’s revenue generation capacity. The three unions agreed that the costs for the IPPs exceeded the selling price of electricity and that was not sustainable. Furthermore, the unions were of the view that Eskom should also be allowed to participate in renewable energy.
* The three unions stated that they were not in favour of the unbundling of Eskom and was of the view that this would lead to privatisation. From the Union’s perspective, this was because cost and benefits of the three units are already available and therefore the reasons for the unbundling are substantiated enough to warrant that activity.
* The unions called on a forensic audit into the reported estimated R450 billion debt of Eskom.
* Concerns were expressed by the unions around the cost overruns at the Medupi and Kusile power stations and suggested that a forensic investigation be conducted in that regard.
* Organised labour also expressed serious concerns at the mooted closure of power stations which have negative socio-economic results for the affected areas. Organised labour feels that the life cycle of the power plants can be extended with available technology and it is therefore a deliberate move to privatise Eskom that results in the closure of Eskom in order to put the institution in crisis.
* The overall challenges facing Eskom put forward by the unions included the cost of IPPs, inadequate training and development of staff, exorbitant cost and poor quality of coal being utilised at power stations, bloated managerial structure as a result of settling the business programme often resulting in duplication of work, and the debt owed to Eskom by municipalities and Soweto.
1. **Overall Committee Observations and Findings**

The observations and findings which were highlighted by the Committee during the deliberations with the various stakeholders and subsequent site visits are outlined below as per the three different themes for the oversight:

* 1. **Eskom’s Audit Opinion**
		1. The Committee noted with concerns that the auditors (Sizwe Ntsaluba Gobodo: Grant Thornton (SNG) on behalf of the Auditor General South Africa)were unable to determine the full extent of the irregular expenditure disclosed by Eskom. Furthermore, the auditors were unable to find sufficient appropriate audit evidence to confirm the fruitless and wasteful expenditure. Eskom received qualifications on fruitless and wasteful expenditure for the past three financial years (2016/17 to 2018/19).
		2. There are significant internal control deficiencies that resulted in the above-mentioned qualified opinions such as inadequate oversight by the accounting authority related to compliance with legislation and lack of proper procurement and contract management. Furthermore, there was improper record keeping to ensure complete, relevant and accurate information to support financial and performance reporting.
		3. The Committee also noted with concern the report from SNG that Eskom’s Internal Audit Unit is not effective enough and that its head has been suspended in the previous financial year. Furthermore, the Chief Financial Officer also resigned and this shows the level of instability within the power utility.
	2. **Eskom’s Finances**
		1. During the 2018/19 financial year, Eskom incurred a loss of R20.729 million and its current liabilities exceed its current assets by R44.057 million. Furthermore, the power utility’s sales volumes have been in decline whilst the operational and capital expenditure have been increasing.
		2. The Committee notes with serious concern that the Medupi power station was initially budgeted at R79 billion however it is expected to cost approximately R146 billion after completion due to delays and other defects. Furthermore, the maintenance costs to address the defects have been estimated at R7 billion.
		3. The construction of the Kusile power station was initially budgeted at R81 billion however due to delays and design defects, it is expected to be completed at approximately R161 billion. The maintenance costs to address the defects are estimated at R285 million.
		4. The Committee welcomes the report that Eskom has set itself an operational and capital expenditure cost savings target of R77 billion by 2023. This forms part of its strategy towards financial sustainability which also includes the proposal that government take over some debt to alleviate debt servicing costs and the migration of the electricity price to prudent and efficient cost reflectivity.
		5. Notwithstanding, the above strategy towards financial sustainability, the Committee remains concerned about the major cost drivers in Eskom which include the exorbitant cost of coal and diesel, the cost of IPPs, and debt service costs. Cost overruns on contracts, especially the Medupi and Kusile power stations, and employee costs.
		6. The Committee notes that the cost of IPPs grew from R9.5 billion in 2015/16 to R25 billion in 2019 thus representing an increase of 27.5 per cent over five years. This represents the highest increase over the period under review when compared to other sources of primary energy.
		7. Eskom’s debt service costs increased by 23.3 per cent from R30 billion in 2015/16 to R69 billion in 2019/20.
		8. In terms of government guarantees, Eskom reported that the total government guarantees amounted to R350 billion, from which R291 billion has been utilised as at the end of September 2019 and R43 billion has been committed and would be drawn down in future.
		9. The Committee notes with concerns that Eskom is selling electricity at lower than the cost of production which is further compounding the ailing financial position of the power utility.
	3. **Debt owed to Eskom**
		1. The total debt owed to Eskom was R66.6 billion as at the end of August 2019 from which R41.189 billion or 62 per cent was overdue. The breakdown of the debt to Eskom is: Municipalities (R38.279 billion), Soweto (R15.912), Top customers (R6.769 billion), Other LPU (R2.773 billion), and Other SPU (R2.891 billion).
		2. Municipalities (R23.538 billion) and Soweto (R15.663 billion) contributed to R39.201 billion or 95 per cent of the total overdue debt owed to Eskom. The total amount of overdue municipal debt between March 2014 and August 2019 grew from R2.593 billion to R23.538 billion.
		3. The Committee noted with serious concerns that the overdue municipal debt owed to Eskom increases by over R1 billion per month. The afore-mentioned amount increased from R22.101 billion in July 2019 to R23.538 billion in August 2019 with the anticipated total by the end of the financial year being R25.900 billion.
		4. The Committee noted and welcome the work done by the Inter-Ministerial Task (IMTT) on municipal debt in order to address the issue as set out on 7.6 above. However, the IMTT needs to expedite the process of addressing the issues given the significant increase in overdue debt.
		5. The Committee also noted Eskom’s proposed changes to its revenue collection strategy to reduce or eliminate the R23 billion in overdue debt. The proposed changes include:
* Incentivised payment arrangements (with conditions);
* Engagements with National Treasury on the possible direct payment of debt owed through the equitable share allocations;
* Prioritisation of paying customers for fault repairs;
* Review of existing supply agreements (restrict, interrupts and terminate supply of electricity and consideration of the takeover of networks and customers); and
* Attachment and sale of movable and immovable assets.
	1. **Labour Relations Matters**
		1. The Committee notes with concern the strained relations and trust deficit between the Executive, the Board and organised labour. The Committee is of view that effective industrial relations are important to the success of the entity.
		2. All three unions representing Eskom employees, i.e. NUMSA, NUM and Solidarity, indicated that they are not in support of the unbundling of the power utility. The said unions view the unbundling as another form of privatisation and that it does not fundamental challenges facing Eskom. The said challenges include increase in interest payments, excessively high borrowing levels, and high operating costs in particular for IPPs and coal, and declining electricity sale volumes.
		3. The Committee noted the submissions from the organised labour that poor quality coal is being utilised by Eskom thus resulting in maintenance challenges whilst the good quality is being exported. The Committee further notes the submission that coal should be made a strategic asset within South Africa.
	2. **Procurement and Supply Chain Management Matters**
		1. The Committee notes with concern the report that five contractors have been overpaid in the amount of about R5 billion during the construction of the Kusile power station. Efforts are underway with the Special Investigations Unit (SIU) to recoup the money.
		2. The Committee notes the submission that the key challenges confronting Eskom include leadership instability, weak governance, weak internal controls, non-compliance with the PFMA and SCM prescripts, and lack of consequence management. The areas of non-compliance as per the 2018/19 audit opinion include the:
* abuse of single/sole source procurement;
* tender processes not being adhered to and incorrect tenders processes being applied;
* incorrect classification as emergency procurement;
* tender processes not followed ad insufficient delegation of authority;
* modifications to contracts exceeding allowed amounts;
* tax clearance certificates from suppliers;
* contracts awarded without following the Construction Industry Development Board (CIDB) requirements;
* contracts not in accordance with National Treasury guidelines;
* Internal processes not being adhered to; and
* Breach of commercial requirements.
	+ 1. The Committee notes with concern that one contractor with an open value of R2 billion had 456 months left on five contracts with Eskom. The Committee is of the view that Eskom needs to commence a process of renegotiating some contracts, especially related to coal supply given its current fiscal constraints.
		2. The Committee views the role of the Executive Board, as the accounting authority, as important to the turnaround of Eskom and therefore it should comprise of individuals with requisite skills and experience.
		3. The Committee welcomes the submission from the Department of Public Enterprises that it is looking at hiring additional capacity to assist with the monitoring of Eskom’s finances and operations.
	1. **Human Resources Matters**
		1. Eskom’s staff compliment stood at 45 708 as at the end of July 2019.
		2. The Committee notes with concern that the number of engineers at Eskom have reduced by 823 from 2882 in March 2013 to 2059 in July 2019. The accountants reduced from 71 to 17 during the same period whist the auditors decreased from 83 to 19.
		3. The senior managerial positions within Eskom have increased significantly (from 80 to 506) since the introduction of the settling of the business programme that was introduced in 2008. However, this number has reduced by 118 to 388 during the period March 2013 and July 2019. The Committee is of the view high number of senior managers also contributes to the financial difficulties being experienced by the power utility.
		4. Eskom reported that there were 117 dismissals per task grade at group level for the period March 2018 to April 2019.
		5. In terms of employee relations, the Human Resources Executive reported that there were 19 national disputes at the time of the oversight visit in progress between Eskom and organised labour.
1. **Recommendations**

The Committee having engaged with Eskom Holdings SOC and the relevant stakeholders, recommends as follows:

* 1. That the Minister of Public Enterprises should ensure the following:
		1. That Eskom ensures that there is adequate socio-economic benefits derived from the contracts entered into with Independent Power Producers.
		2. That Eskom, as a matter of urgency, find a balance between the requests for higher tariffs and revenue generation.
		3. That Eskom engage in a process of renegotiating contracts especially related to the supply of primary energy such as coal.
		4. That the Eskom Board and Senior Executive comply with the declaration of financial interests regulations and declare their financial interest.
		5. That the filling of all critical vacancies be expedited within a reasonable time at Eskom.
		6. That the oversight capacity over Eskom be strengthened within the Department of Public Enterprises.
	2. That comprehensive investigations be conducted by the Auditor General South Africa into the reasons for the substantial cost overruns during the construction of the Kusile and Medupi power stations. The report on the investigations should be submitted to Parliament within three months of the adoption of this report by the National assembly.
	3. That the Minister of Finance should ensure that that stringent conditions be attached to the special appropriation of R59 billion that will ensure the sustainability and financial viability of Eskom.

**10 Conclusion**

The responses to the recommendations as set out in section 9 above by the relevant Executive Authorities and the Auditor General South Africa must be sent to Parliament as well as the Committee within 90 days of the adoption of this report by the National Assembly.

Report to be considered.

1. Parliament (2015) [↑](#footnote-ref-1)
2. Parliament (2015) [↑](#footnote-ref-2)