

Thursday, 30 July 2020

Re: Submission on the Economic Regulation of Transport Bill [B1 – 2020]
Att: Hon MJ Zwane, Chairperson of the Portfolio Committee on Transport
c/o: Ms Valerie Carelse

Dear Chairperson and Members of the Portfolio Committee on Transport,

Further to the call for comments on the Economic Regulation of Transport Bill.

We do not believe the Bill as it stands will best serve the public interest, either of transport users or the broader South African public. There are four main reasons for this:

1. The main issues in the transport sector do not have much to do with price regulation and therefore are unlikely to be resolved by it
2. Where price regulation is related to challenges in the sector, the state already has the power to resolve this and its failure to make the necessary decisions will not be remedied by introducing a regulator
3. The broad regulatory model that would be used has not worked in other sectors like electricity and has at times failed dramatically in transport sectors of other countries
4. The regulatory model requires scarce resources and skills which the country either does not have or at least could be much better utilised – especially in a post-Covid-19 economy
5. There are other, simpler models that could be adopted but ultimately the success of any model requires government to improve its management of the relevant transport sectors/modes.

Related concerns were already raised in the *National Development Plan (NDP)* in 2012. The NDP noted that South Africa had established regulatory agencies for a number of sectors, tasked with:

- “safeguarding reliable and competitively priced services for consumers,
- promoting affordable access for poor and remote households
- ensuring that utilities and operators, are efficient and financially viable”

However, it found that based on the performance of the sectors concerned, they have not achieved the positive outcomes initially envisaged. In particular, it cited poor quality and speed of telecommunications, and serious problems with the reliability and pricing of electricity supply. A notable example of the failure of the latter and, more broadly, of the regulatory model underlying the Bill is the National Energy Regulator (NERSA)'s failures to make appropriate tariff allocations to Eskom – as demonstrated by the late, rapid escalation in electricity tariffs and most recently the judgement by Judge Kollapen.

In response to the challenges, the NDP called for a reconsideration of the institutional arrangements and design of network regulators. Specifically, it drew attention to the broader requirements for effective regulation which is not just about the regulator. "The state itself must have adequate capacity and capability to formulate effective policies; support the design, establishment, review and improvement of regulators; and respond to issues identified by capable regulators."

We submit that these conditions are quite evidently not yet in place in the transport sector.

Attached to this short submission are two further documents in which we elaborate on these concerns in more detail:

- A working paper presented at the *5th Annual Competition and Economic Regulation Week* in July 2019
- A shorter article in *The Conversation* which summarises some of the concerns raised in the academic paper.

Both these documents address our broader concerns about the envisaged regulatory model of which the Single Transport Economic Regulator (STER) could be the most important, and problematic, consequence.

The socio-economic impact assessment (SEIA) accompanying the Bill provides a useful quantification of our concern regarding cost and capacity: it suggests that the STER will cost between R78million and R133million, requiring between 90 and 145 relatively highly-qualified staff. In our view, this would not have been a progressive allocation of resources in the pre-Covid-19 era. Critical posts are vacant or have been defunded across the public sector. As a country we are in dire need of more skilled and committed public servants in a wide range of areas from education to municipal infrastructure management. Yet for fiscal and other reasons,

there has been a paring back of posts even in areas where there are dire shortages. It is, we believe, not possible to justify the resource allocation proposed in that context. It is even less justifiable in the face of the dramatic worsening of our fiscal situation linked to the Covid-19 pandemic. But most importantly, it is not possible to justify this allocation of resources when the model proposed is at best likely to be ineffective and at worst could lead to a worsening of problems in the transport sector.

While the Portfolio Committee is necessarily concerned with the transport sector, higher level considerations relating to national resource allocation are surely relevant to its processing of this legislation. But we need not even rely on those arguments in order to encourage the committee to send this Bill back to the Executive. The reason is that we are of the view that the legislation will not even serve the transport sector itself. In saying this, we are fortunately able to draw on our shared knowledge of recent institutional history in the public service.

For example, one of us worked in the National Department of Transport 15 years ago when government was investigating possible sectoral restructuring in the rail sector (freight and passenger) as a solution to limited funds for investment and maintenance as well as relatively poor, and worsening, service delivery. All those problems have since become worse, whether because of mismanagement, corruption or underinvestment. But when the NDOT brought in external consultants from an ideologically conservative UK think tank, *even* those consultants cautioned against the notion that vertical or horizontal separation in rail – accompanied by the necessary regulatory institutions – would resolve the problems. This caution emanated from the fairly disastrous experience in the UK where privatisation under economic regulation led to massive state bailouts and deterioration of service quality in many cases. The UK context is of course different, but if anything the South African context is even less favourable to this kind of model.

Furthermore, pricing issues within the transport sector, many of which are mentioned in the SEIA, are *within the current scope of the government to resolve*. The problem is that the state/shareholder has not been willing to take difficult decisions and follow through. For example, the issue of excess port tariffs has been discussed for two decades. It was one of many important issues discussed in the NDOT's National Freight Logistics Task Team (completed in 2005). The challenge there is that ending high tariffs would mean also reducing Transnet's ability to

cross-subsidise loss-making operations or/and operate without greater efficiency or state support. Introducing the STER, as the SEIA notes, will not resolve this on its own because the STER is a public regulator that will require a public mandate and associated cooperation/support from the shareholder. In other words, whether such problems are resolved will still depend on the political will to do so; a regulator is neither necessary nor sufficient to resolve them.

Our experience in the water sector suggests, once again, that the challenges faced in the transport sector will not be addressed effectively by an independent regulator but require attention to the capacity of the whole sector. It is instructive that, until recently, the regional water utilities (water boards) had maintained a relatively smooth and reasonable price path and remained financially viable without the need for an economic regulator. To the extent that financial problems have emerged, this is largely due to poor municipal performance, which cannot be resolved by an economic regulator in the sector but falls within the purview of the Executive. Parliament itself has recently intervened to curb what appeared to be opportunistic proposed price increases which sought to take advantage of a break in continuity, due to changes in the political leadership and top management of the Department of Water and Sanitation.

The basic fact is that there is no avoiding the need to fix public management and governance in the transport sector. Adding the proposed STER and associated regulatory structure will add cost and complexity without solving any of the fundamental problems in the sector. It will further reduce the resources and capacity available for precisely the better public management that is required. Given that key operators in the transport sector are state entities, the state has the power to determine prices without creating a special, separate entity (the regulator) to do so. The recent court case in which Eskom successfully sued NERSA demonstrates the wastefulness, ineffectiveness and inefficiency of that approach.

We hold no ideological commitment to any particular ownership or regulatory structure in the sector, nor do we have any vested interests in these decisions. The sole purpose of this submission is therefore to raise concerns, based on our knowledge and expertise, with the consequences of the proposed legislation for the transport sector and the broader public interest. There may well be a time in future decades when a transport economic regulator and associated sector restructuring is appropriate, but that time is not now. We therefore respectfully

suggest that Parliament return this legislation to the Executive with a request that it propose more convincing, direct solutions to the problems that afflict the sector rather than proposing a costly outsourcing of responsibility for those problems which is what this Bill does.

If it would be useful for the Committee, one or both of us can avail ourselves to make virtual oral presentations to Members on these points.

Yours sincerely,

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