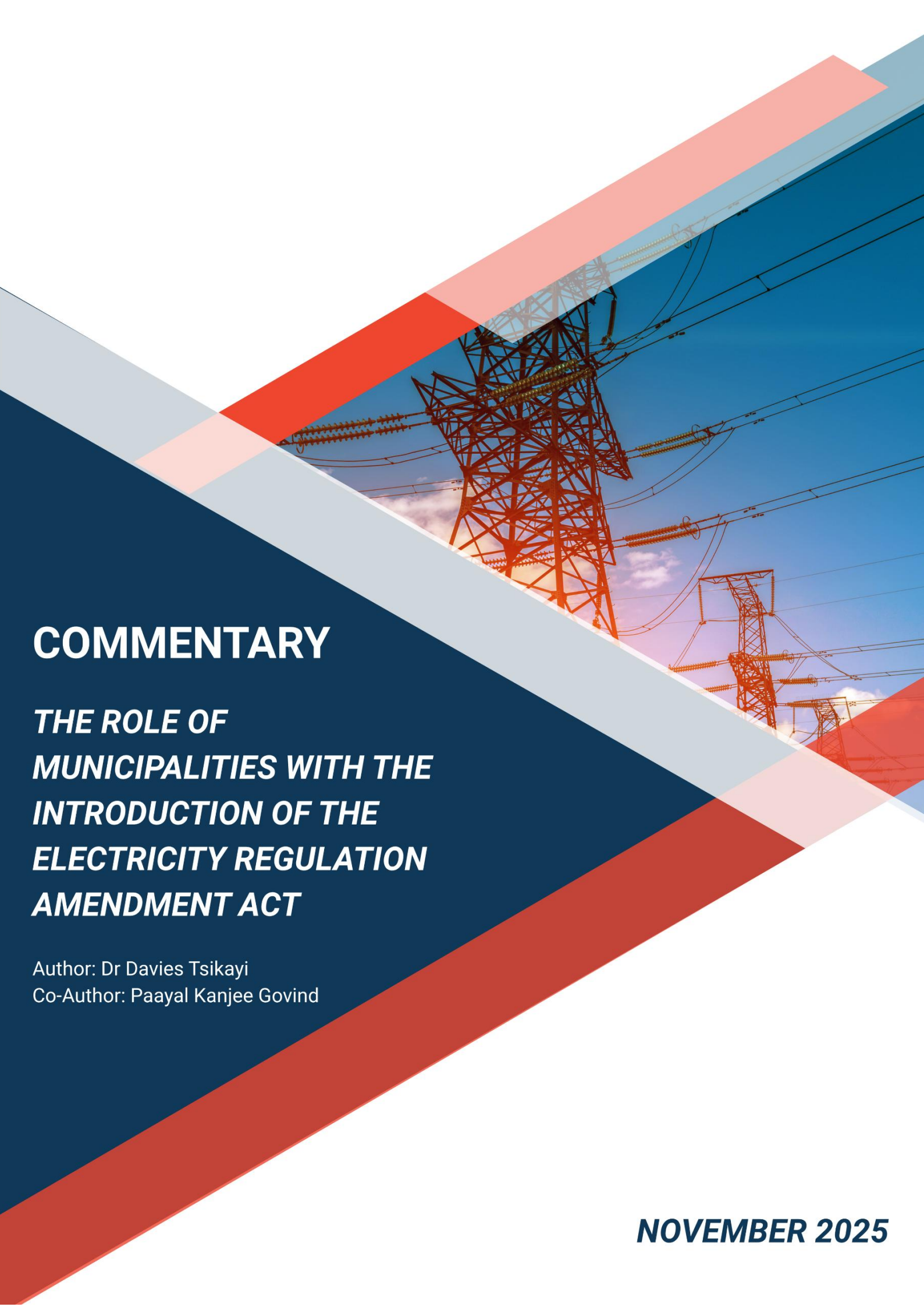




COMMENTARY

THE ROLE OF MUNICIPALITIES WITH THE INTRODUCTION OF THE ELECTRICITY REGULATION AMENDMENT ACT

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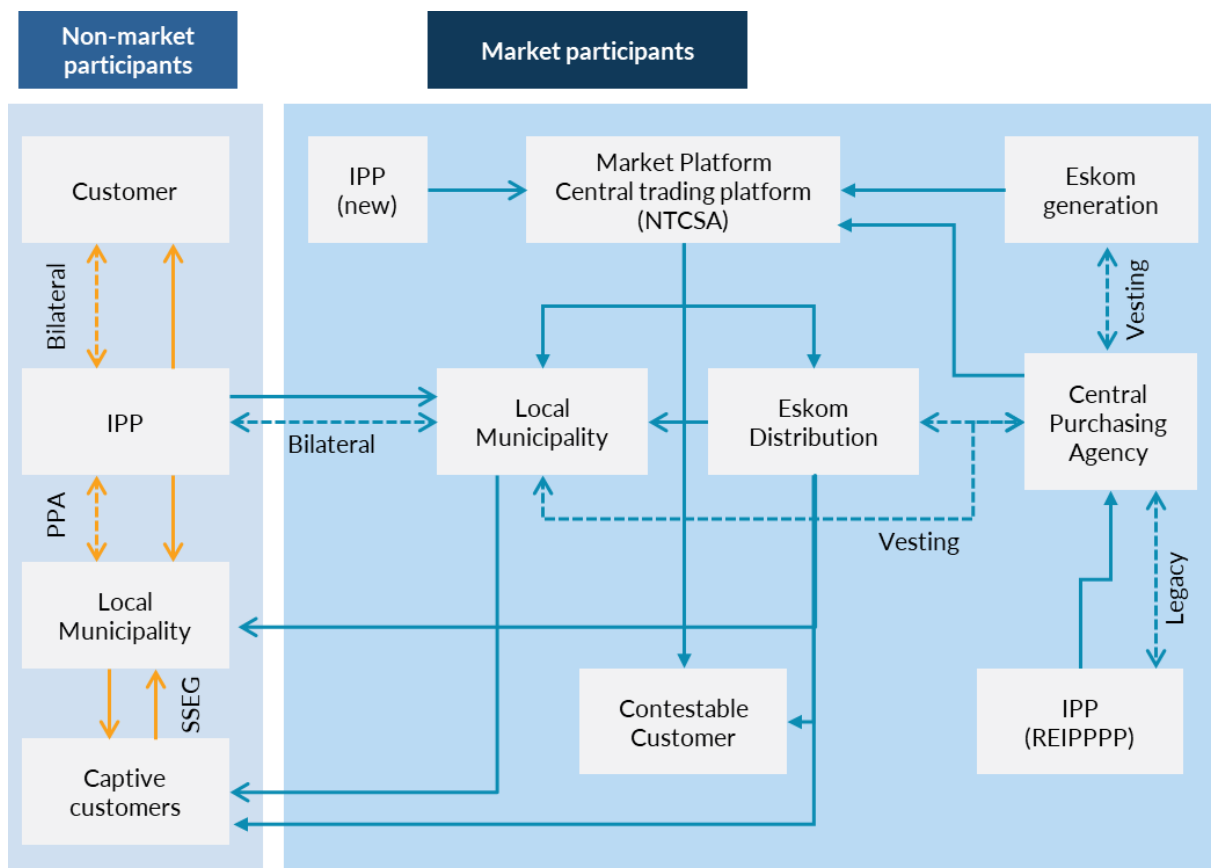
NOVEMBER 2025

Overview of the ERAA

The Electricity Regulation Amendment Act (ERAA) or referred herein as *the Act* marks a transformative shift in South Africa's energy landscape, aiming to foster a more competitive and decentralised electricity market. It builds on interim reforms introduced since 2021, which initially allowed private generation projects of up to 100 MW without requiring a license from the National Energy Regulator of South Africa (NERSA). These changes unlocked a significant pipeline of private generation and enabled energy wheeling to multiple customers. In late 2022, the licensing threshold was removed entirely, allowing generation of any size, provided the project is registered and grid compliant. Further amendments on 17th of January 2023 to Schedule 2 exempted all generation facilities, regardless of capacity, from licensing if they supply electricity to one or more customers via wheeling, as long as a proper grid connection agreement is in place. This streamlined registration-and-connection regime has opened the door for large-scale, privately financed renewable energy projects, significantly accelerating private investment in new generation capacity.

Historically, the country's electricity supply industry has been dominated by Eskom, which held a monopoly over generation, transmission, and distribution. This concentration of control effectively stifled competition and innovation within the sector. It can be argued that the ERAA was introduced primarily to address the systemic failures of Eskom during the height of loadshedding and spur investment in South Africa's renewable energy sector through the introduction of a competitive market. Eskom's long-standing monopoly over electricity generation, transmission, and distribution contributed to inefficiencies, financial instability, and persistent load shedding experienced between 2021 and beginning of 2024. The Act seeks to dismantle this monopoly by unbundling Eskom's operations and establishing a Transmission System Operator (TSO) a neutral, state-owned entity responsible for managing the national grid and facilitating open access for Independent Power Producers (IPPs). This structural reform is designed to create a competitive electricity market, enabling multiple generators to sell power through transparent platforms and bilateral agreements. By promoting non-discriminatory grid access and market liberalisation, the ERAA aims to attract private sector investment, accelerate the deployment of renewable energy projects, and support South Africa's transition to a low-carbon energy future. These changes are critical to meeting the country's growing energy demand, reducing reliance on coal, and achieving the goals outlined in the National Development Plan and Just Energy Transition framework.

Parallel to the licensing exemptions, the Electricity Regulation Amendment Act of 2023 (now Act 38 of 2024) introduces deeper structural reforms that reshape South Africa's electricity market. Key provisions include non-discriminatory open access to transmission and distribution networks for third-party generators, the establishment of an independent TSO and market operator, and a clear framework for electricity trading and wheeling by IPPs, traders, large consumers, and municipalities. Crucially, IPPs are no longer restricted to selling electricity solely to Eskom, they can now enter into bilateral contracts with private off-takers or trade on emerging market platforms. The Act mandates that transmission and distribution licensees must offer network access to third parties on equal terms, with access only denied in cases of genuine capacity constraints, which must be justified in writing. Additionally, generators and customers are entitled to request information on available grid capacity and the costs of any necessary upgrades. These reforms lay the legal foundation for widespread wheeling of privately generated electricity across both Eskom and municipal grids, while also clarifying the roles and licensing requirements for new market participants such as electricity traders and aggregators.



Municipalities under EERA

While the EERA introduces sweeping changes at the national level, it is equally important to recognise its profound implications for municipalities. Local governments will need to adapt to a more decentralised and competitive electricity market, which may require restructuring their procurement processes, updating grid infrastructure, and developing new capabilities to engage with IPPs. The shift from a centralised Eskom-dominated model to a more open and dynamic energy landscape means municipalities must now navigate complex regulatory frameworks, manage wheeling agreements, and ensure compliance with grid connection standards. These changes present both challenges and opportunities: while municipalities may face initial capacity constraints, they also stand to benefit from improved energy security, diversified supply sources, and potential cost savings through competitive energy procurement.

Municipalities Shrinking Control of Distribution

Schedule 4B of the South African Constitution grants municipalities executive authority over electricity reticulation, traditionally allowing them to manage networks operating at voltages *up to 132 kV*. Under Eskom's vertically integrated model, municipalities primarily functioned as electricity resellers, purchasing bulk power and distributing it to end-users. However, the EERA significantly redefines this role.

Instead of merely reselling electricity, municipalities are now expected to take on a more strategic and operational role, coordinating service delivery, overseeing grid access, managing a diverse supplier base, and ensuring accurate metering and demand forecasting. Importantly, the Act narrows the definition of "reticulation" to systems operating at or below 11 kV. This shift limits municipal control over infrastructure above 11 kV, which is now open to participation by IPPs. This redefinition introduces

uncertainty around municipal jurisdiction over higher-voltage network elements and may require legal and operational adjustments. At the same time, it presents an opportunity for municipalities to modernise their energy systems, engage directly with IPPs, and benefit from more competitive and diversified electricity supply options.

Municipalities As Either Market or Non-Market Participants

The Act places greater responsibility on municipalities as South Africa transitions to a more decentralised and competitive electricity market. Under the new framework, municipalities must rethink how they procure electricity and manage their distribution networks. This includes adapting to new market dynamics, engaging with IPPs, and ensuring compliance with updated grid connection standards. The shift away from Eskom's centralised model means municipalities will need to build new technical and regulatory capabilities to operate effectively in a liberalised environment. While this transition presents challenges such as capacity constraints and regulatory complexity, it also offers opportunities for improved energy security, cost savings, and access to diversified power sources. The roles of national entities like the National Transmission Company of South Africa (NTCSA), the CPA, and the Market Operator will be key in supporting municipalities through this transformation.

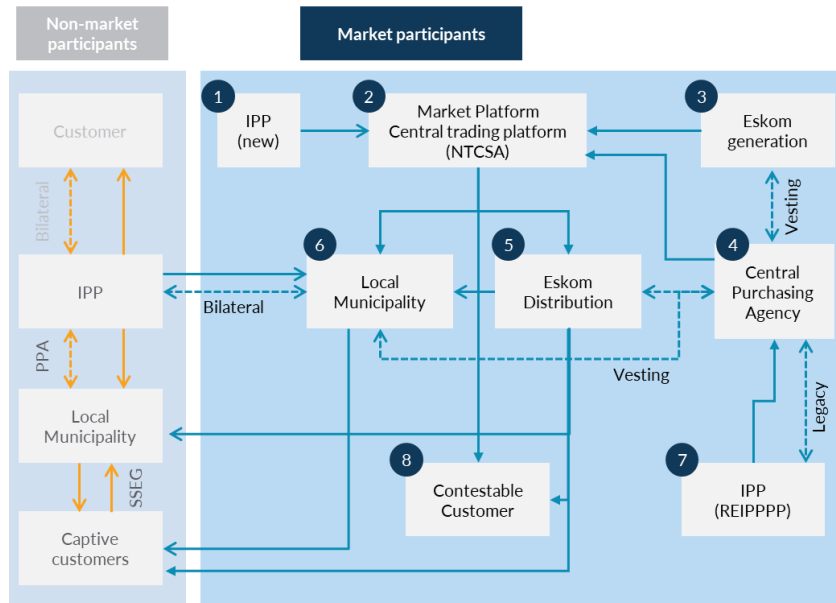
There are options available to Municipalities, under the new market structure, a local municipality must choose whether to remain a regulated buyer outside the competitive market or to become a wholesale market participant. This choice determines their purchasing obligations, risk exposure, and relationship with the central market institutions as tabulated.

The two strategic pathways are outlined in Table 1 below.

Table 1: Municipalities options

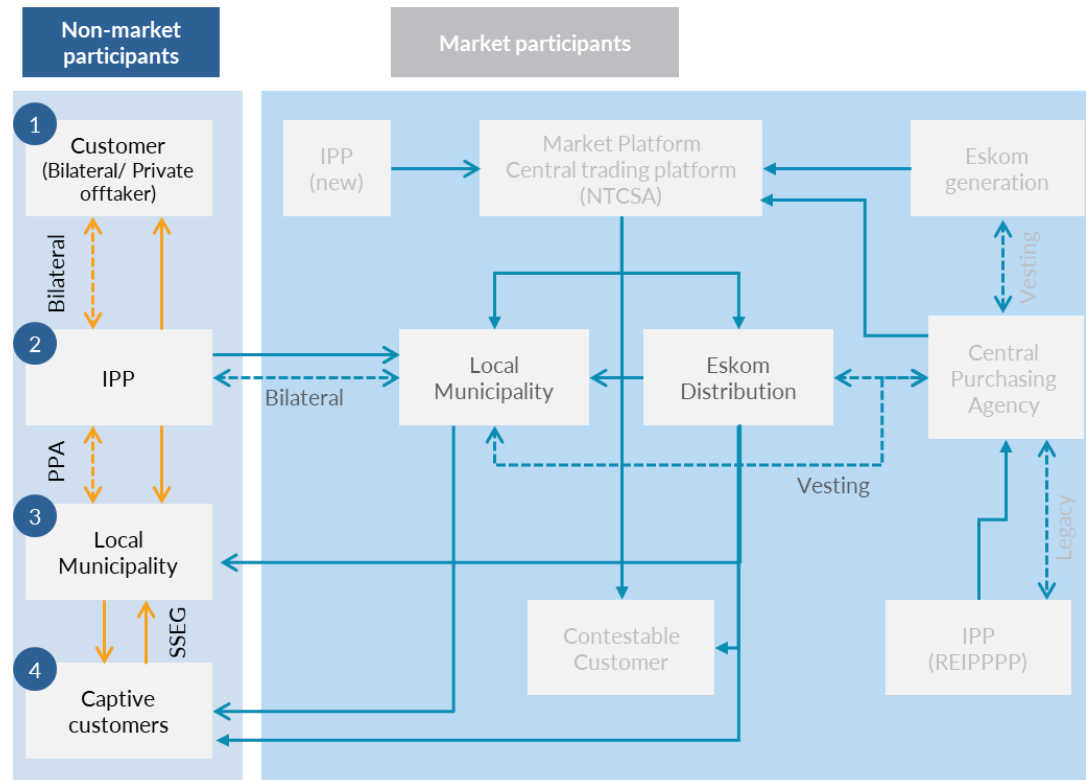
	Option 1	Option 2
Purchasing Obligations	– Continue purchasing bulk electricity from Eskom Distribution at regulated tariffs – Prices are linked to a wholesale energy rate approved by NERSA – No need to participate in market bidding	– Procure electricity directly from the NTCSA-operated wholesale market – Submit demand forecasts and purchase bids in day-ahead or real-time markets – Responsible for balancing scheduled vs actual consumption – May enter bilateral PPAs validated through the market system
Risk Exposure	– Low financial and operational risk – Insulated from market price volatility – CPA absorbs payment default risk, shielding Eskom – No need for forecasting, hedging, or balancing	– Exposed to market price volatility and imbalance charges – Must provide credit cover or financial guarantees to participate – CPA offers a 5-year vesting contract to stabilise costs via a strike price mechanism – Requires active load management and trading expertise
Relationship with Central Market Institutions	– CPA acts as intermediary, contracting with Eskom on behalf of municipalities – Market Operator runs the wholesale market, but municipalities do not engage directly – Municipalities may still pursue bilateral PPAs or own generation, coordinated with the System Operator	– Direct interaction with NTCSA's Market Operator for scheduling and trading – Coordination with NTCSA's System Operator for real-time balancing – Must comply with Market Code rules and settlement procedures – CPA provides transitional support but does not shield municipalities from financial risk

Market Participants (Wholesale Market)



1. IPP (new)
 - Generators licensed to trade on the market
 - Participate directly in the NTCSA platform, subject to balancing and settlement rules
2. Market Platform (operated by NTCSA)
 - NTCSA: Newly established transmission entity responsible for owning & operating the transmission grid and for system balancing. Houses the Market Operator (running the central trading platform) and the CPA. Ensures open and non-discriminatory grid access
 - Central wholesale trading platform
 - Generators (Eskom and IPPs) bid supply offers; distributors, municipalities, traders, and contestable customers bid demand. Prices are set through a clearing process (similar to marginal pricing)
3. Eskom Generation
 - Market-participating generator bidding onto the central platform
 - Receives availability & energy payments through CPA vesting contracts to prevent price manipulation and ensure system adequacy
4. CPA
 - Special-purpose vehicle managing transition risk and legacy contracts
 - Takes over REIPPPP PPAs and on-sells to the market
 - Holds vesting contracts with Eskom generation and distribution to stabilise prices
 - Recovers legacy costs via energy or capacity charges to all customers
5. Eskom Distribution
 - Market participant and distributor serving municipalities and retail customers
 - Maintains regulated pricing for non-contestable customers; purchases from CPA at an agreed strike price to shield against non-payment by municipalities
6. Local Municipality
 - Optionally participates directly in wholesale market via CPA vesting contract
 - Ability to procure power from multiple sources and to sell through its distribution network
7. IPP (REIPPPP)
 - Existing contracted IPPs under legacy PPAs
 - Their power is sold into the market by CPA on their behalf until contracts expire (legacy flow)
8. Contestable Customer
 - Large industrial or commercial users defined in the Market Code
 - May buy directly from the market or retain current retail supplier arrangement

Non-Market Participants



1. Bilateral / Private Off-takers
 - Large corporates or campuses buying directly from IPPs
 - Transactions take place through wheeling arrangements across Eskom or municipal grids, paying a "use-of-system" fee
2. IPP (non-market)
 - Generates electricity and sells directly via PPAs or bilateral contracts to private off-takers (customers, traders, or municipalities)
 - Operates outside the central market; energy and payment flows are privately contracted but must still report schedules to the system operator.
3. Local Municipality
 - Licensed electricity distributor
 - Constitutionally responsible for electricity reticulation
 - Can act as a buyer from IPPs or Eskom Distribution; may generate its own power (SSEG or large IPP)
 - During transition, may remain a non-market buyer at a regulated price or opt into market participation
4. Captive Customers / SSEG owners
 - Embedded generators such as rooftop PV prosumers
 - Supply excess power to the local grid through municipal SSEG tariffs
 - Remain under regulated frameworks, not market settlement

Comparing The Two Buyer Roles

In summary, the regulated buyer model offers municipalities simplicity and financial stability. Under this arrangement, the municipality purchases electricity at a predictable, NERSA-approved tariff linked to Eskom's costs. The Central Purchasing Agency (CPA) and Eskom handle generation procurement and imbalance management, allowing the municipality to avoid direct exposure to market volatility. However, this model limits autonomy as municipalities remain dependent on Eskom and the CPA, potentially missing out on cost savings and flexibility offered by competitive sourcing.

In contrast, the wholesale market participant model provides greater independence and the potential for more cost-effective and diversified energy procurement. Municipalities choosing this path must actively manage their electricity purchases, forecast demand accurately, submit bids, and balance their consumption against scheduled supply. They also assume financial responsibilities, including credit requirements and exposure to market price fluctuations. While this model aligns with the long-term vision of a competitive, multi-buyer electricity market, it demands significant technical and financial capacity.

Both options are supported by transitional mechanisms. The CPA's vesting contracts help mitigate risk during the initial phase of market reform. Importantly, the choice is not permanent: municipalities may begin as regulated buyers and transition into market participants as their capabilities grow. Throughout this process, NTCSA's central institutions play a vital role. The Market Operator facilitates trading and settlements for market participants, while the CPA ensures municipalities, regardless of their chosen model can access electricity on reasonable terms without compromising Eskom's financial stability.

Conclusion

The ERAA introduces a foundational shift in South Africa's electricity sector, redefining the role of municipalities within a liberalised and decentralised market framework. The narrowing of municipal jurisdiction to networks operating at or below 11 kV necessitates a strategic reassessment of their operational and procurement models. Municipalities are now positioned to either maintain their status as regulated buyers, characterised by low risk and limited autonomy, or transition into wholesale market participants, which offers enhanced flexibility and potential cost efficiencies, albeit with increased technical and financial responsibilities.

The Act enables municipalities to engage directly with IPPs, participate in market-based procurement, and manage wheeling arrangements across both Eskom and municipal grids. Transitional instruments, such as vesting contracts facilitated by the CPA, provide interim stability as municipalities build the requisite capabilities to operate within the new market structure.

Success in this evolving landscape will depend on each municipality's ability to align with national institutions such as the NTCSA and CPA, develop internal capacity, and navigate the regulatory and operational complexities introduced by the ERAA. As South Africa advances toward a multi-buyer electricity market, municipalities will play a critical role in ensuring local energy resilience, affordability, and sustainability.