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Eskom

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Eskom

Abstract

This case study analyzes the way in which the South African energy giant Eskom has integrated principles of human rights into its core business strategy in a rapidly evolving and demanding post-Apartheid environment. In particular, this study addresses the origins and evolution of the company's preferential procurement policy from its nascent beginnings to the present day. Eskom's emphasis on developing Black¹ owned and managed businesses, or Black Empowerment Enterprises (BEE), has arguably served as a key model to a South African government and private sector focused on continued economic growth. While Eskom's status as a State-Owned Enterprise has affected its responsiveness to social issues in South Africa, internal leadership around black empowerment has characterized the company's actions and policies. The company's focus on developing a diversified base of suppliers not only represents a business opportunity for Eskom, but also a chance to demonstrate an explicit commitment to Global Compact Principle 6, which holds that companies should endeavor to eliminate discrimination in employment and occupation. Eskom's policy to develop Black Empowerment Enterprises that permit all South Africans to actively participate in a growing economic environment also touch on Principle 1, which requires businesses to support the protection of human rights norms.

Company Profile

Eskom is a vertically integrated organization employing approximately 30,000 individuals and was founded in 1923. Eskom generates, transmits, and distributes electricity to South African consumers and businesses, and purchases and sells electricity from and to other southern African countries. Today Eskom ranks among the seven largest electricity providers in the world in terms of production and ninth in terms of sales. Eskom is also a South African State-Owned Enterprise (SOE), whose interests are represented by the Ministry of Public Enterprises. The Ministry selects the Chief Executive and all members of the Board of Directors, while the Executive Board is vested with the responsibility of business implementation. The company is completely self-financing and thus receives no financial support from the South African government; indeed, it pays yearly dividends to the government.

Human Rights and the South African Context

¹ Pursuant to Eskom's [published] policy, "Black" is defined as an individual who is of African, Asian, or mixed-raced descent.

[ESKOM, *Eskom Global Compact Case Study - Flexible Hot Water Load Management Control Sys*, South Africa: Eskom, 2008]

To understand Eskom's status and position at the time of its formal commitment to a preferential procurement program, it is important to recount recent South African history and the end of Apartheid. In March 1992, the country held its last white-only referendum in which white South Africans gave the government permission to work with black leaders and promulgate a new constitution free of the codified racial discrimination endemic to South African society. In 1994 the country held its first-ever general election in which black citizens could vote.

The election brought Nelson Mandela to power and the resulting unity government soon produced a comprehensive plan that enabled greater economic and social development among South Africa's overwhelmingly poor Black population. Blacks in South Africa previously had extremely limited access to capital and lived largely in underdeveloped rural areas, often without basic provisions like electricity and running water. The 1994 Reconstruction and Development Programme (RDP) instituted by the new South African government outlines the government's development priorities while emphasizing the importance of high economic growth to the creation of a more politically and economically equitable state. More specifically, the government committed to focus on capital investments in order to both uphold new constitutional tenets, but also to spur development. The development of a larger, more sophisticated power grid capable of lighting the state's poorer and rural areas thus became a key aspect of the government's overall development plan. At the same time, the RDP recognized the economic faltering that characterized the preceding twenty years of white rule. In addition, the RDP acknowledged the need to encourage the growth and integration of private sector enterprises owned and managed by previously disadvantaged groups in order for to grow the South African economy.

The United National Global Compact and Eskom

Eskom developed its preferential procurement process before the United Nations created the Global Compact (GC), though its BEE policies demonstrate the commitment Eskom has to creating fairer labor practices free of entrenched racial discrimination. Indeed, this commitment to a socially and economically advanced society emanates from those at the top echelon of the company, as captured in the Eskom Vision Statement, shown below.

“Together building the powerbase for sustainable growth and development” –Eskom Vision Statement

Together	One Eskom unified, working together in partnership with others
Building	Planning for the future, building South Africa’s economy
Powerbase	Providing the electricity foundation for positive sustainable development
Sustainable	Ensuring continued delivery on economic, environmental and social outcomes
Growth	Empowering South Africa, its people and the economy
Development	Securing a brighter future for all and integrating the first and second economy
Problem Facing Prospective	Eskom’s Response
BEEs Difficulty in securing financial capital	*Reducing lag time in payment of invoices from industry norm of 120 days to 30 days *Assistance in securing capital
Small scale of new BEEs	*Breaking up of traditionally large contracts into smaller parts to facilitate BEE participation; *Set aside of contracts for bidding only by BEEs *Price matching. In instances where white-owned

Table 1: Breakdown of the meaning of each key term in the Eskom Vision Statement

Indeed, in interviews conducted for this case study, Eskom leadership reinforced the sense that in the early 1990s there existed a sense that preferential procurement would be good for the country. In light of the political currents and strong national emphasis on rural and black-oriented economic development, such notions became policy. In 2004, the Department of Public Enterprises—the sole shareholder of Eskom—formally refocused state-owned enterprises as a catalyst for economic development as part of the government’s Accelerated and Shared Growth Initiative for South Africa (ASGISA), which aims to halve poverty in South Africa by 2014. Eskom has since revised its business model to develop an enterprise capable of meeting the current and future needs of a changing customer base by focusing on its core business – generating, transporting, trading and retailing energy, while leveraging the associated economic benefits to further develop black-owned and managed businesses in South Africa.

Implementation and Development of Policies

Eskom identified the need for Black Empowerment Enterprises in the early nineties, though at least one

senior level manager described its beginnings as “vague.” The shift in South African society had changed the socio-economic landscape in the country as black citizens gained full legal equality and an opportunity to reach equal economic status as well. This shift was not lost

[ESKOM, *Eskom Global Compact Case Study - Flexible Hot Water Load Management Control Sys*, South Africa: Eskom, 2008] [ESKOM, *Eskom Global Compact Case Study - Flexible Hot Water Load Management Control Sys, South Africa: Eskom, 2008*]

on Eskom, which understood potential changes in the political environment in South Africa and was not ignorant of the government’s emphasis on bringing electricity to previously underserved communities. While the government did not bind Eskom to the tenets of the RDP, the change in the business landscape necessitated a shift in strategy to match the developing political and economic environment.

In 1994 Eskom established a formal BEE policy that culminated with the creation of a Small Medium and Micro Enterprise (SMME) Development Section. Eskom tasked this SMME Development Section with developing a system by which such enterprises could effectively participate in the tendering (contracting) process. Within a year of research and stakeholder dialogue the Section circulated its first major working directive, “The Development and Support of Small, Medium, and Micro Enterprises by Eskom Pro”; the document required that all sections and services of the company reach a 25% procurement level from SMMEs within one year and at least 50% in each year thereafter.

Eskom regularly sources goods and services from contractors for such things as legal and management consulting, graphic design, coal, food products, engineering works and electrical contracting. But in the years immediately following Apartheid, there existed few BEEs able to meet Eskom standards; as a result of this lack of experience and skill in prospective BEEs, the company set out specific procedures and processes in order to promote tendering from existing BEEs and develop the capacity of emerging organizations. In addition to transparently advertising its tenders (contracts), Eskom developed other capacities, such as the Tender Assistance Centers outlined in Table 2, to assist emerging BEEs.

Table 2: Eskom responses to key BEE problems

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Small scale of new BEEs	*Breaking up of traditionally large contracts into smaller parts to facilitate BEE participation; *Set aside of contracts for bidding only by BEEs *Price matching. In instances where white-owned enterprise has provided the lowest price, Eskom reserves the right to offer contract to BEE if it is able to meet this lowest price
SME confusion over Eskom standards and requirements	*Establishment of Tender Assistance Centres, which offer technical assistance relating to tenders, including information regarding procurement mechanisms, standard terms and conditions, price schedules, invoicing and payment processes, delivery, lead time and delivery rate schedules
Lack of professional business experience and sustainability	*Establishment of Tender Assistance Centres, which conduct training and provide assistance to BEEs after awarding contracts to qualifying companies. Training topics include: financial arrangements, negotiations to obtain competitive prices from raw

In later restructuring of the company, line management took control of preferential procurement; because this effort took division resources away from their core duties, the restructuring led to a de-emphasis of the developmental focus of preferential procurement. However, the new structure offset this potential weakness by bringing Eskom's largest subcontractors under scrutiny. These organizations had previously escaped notice from the SMME Development Section and company executives for their contracting policies and procedures. As a result, Eskom began evaluating its largest suppliers—including those based overseas—according to their practice of black empowerment.

In 1996, the government introduced its "10 Point Plan", which spelled out a comprehensive points-based system by which companies could implement BEE policies along their respective supply chains. Instead of adopting the non-binding government findings, Eskom's Board of Directors called for a simplification of the system as the company drew up its overall preferential procurement policy. The points-based system developed by Eskom measures suppliers and prospective BEEs in terms of black ownership, black management, skilled black personnel,

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procurement from other BEE suppliers, black female managers, disabled black employees and other initiatives that Eskom regards as significant to its procurement program.

The BEE rating criteria for supplier and tender evaluation is shown in Table 3. In order to qualify as a BEE supplier, a company must score at least one point each on black ownership, black management, skilled black personnel, procurement from other BEE suppliers and black female management.

Table 3. Eskom’s BEE rating criteria for suppliers

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Small scale of new BEEs	*Breaking up of traditionally large contracts into smaller parts to facilitate BEE participation: *Set aside of contracts for bidding only

Incentivization and Accountability

In order to facilitate a corporate culture that considers BEE progress as core to its mission, Eskom holds all relevant procurement, operational and management staff accountable for attention to BEE activities in their respective sections. Accordingly, ESKOM includes a section on preferential procurement on the annual appraisals of relevant staff, and vested a senior level manager with overall responsibility to reaching preferential procurement goals. The responsibility at the corporate level for BEE policy rests with the Corporate Black Supplier Program Manager. At the group or divisional level, which includes electricity generation, transmission, and distribution, the individual group or division is responsible for meeting company BEE procurement goals.

Conclusion

In terms of overall procurement, Eskom continues to grow its reliance on BEE suppliers. In 2006, the company purchased goods and services worth approximately R11.4 billion, a figure ten times that of its overall BEE procurement in 1998. Overall, the company has exceeded its BEE projections by more than 30%. Its supplier database of black-owned and controlled companies lists 14,000 BEE businesses of all sizes and on average utilizes around 30% of its registered BEE suppliers at any one time. In 2006/2007, the company projects it will spend approximately 67% of its discretionary expenditures toward BEE suppliers, of which 18% will go to black womenowned businesses.

The success of Eskom's BEE policies results from the leadership and support by company executives and the Board of Directors and because its increasingly well-articulated objectives and mission fit as a leader in the development of the modern South Africa. Furthermore, the company's strong focus on supplier development, as evidenced by the advent of pre-tender briefings and more comprehensive offerings of Tender Assistance Centres, enable emerging suppliers to ensure their own sustainability. Because traditional financial institutions find new suppliers as a credit risk, Eskom often finds it necessary to undertake long-term contracts with its BEE suppliers.

Eskom continues to face challenges. The company has had to come to grips with "fronting", whereby contracting companies misrepresent themselves to Eskom in order to win points in their bid for contract. While the company has limited resources to audit each company competing for contracts, it has come to rely on targeted investigation and self-policing by competitor contracting companies.

Furthermore, new government policies that seek to streamline the private sector's implementation of BEE policies differ from Eskom's commitment to supplier development initiatives. The move in the South African government to move towards broad-based BEE **Codes of Good Practice** allow companies without black ownership to receive preference, which, if implemented at ESKOM, could compromise the company's commitment to developing blackowned businesses and a redirection of support to other suppliers not necessarily controlled by blacks.