

APPRAISAL OF THE NIGERIAN ELECTRICITY SUPPLY INDUSTRY

Background

The Federal Ministry of Works, Power and Housing (MOP) recently issued the following documents: the Power Sector Policy Statement (the Policy Statement); the Power Sector Recovery Plan Policy Statement (the PSRP Policy) and the Power Sector Policy Directives and Timeline (the Directives). The Policy Statement and the Directives were issued in June 2019; the PSRP Policy was issued in February 2019. While forming his cabinet on August 21, 2019, President Muhammadu Buhari separated the Ministry of Power from Ministry of Works and Housing.

The three documents were developed further to the powers of the MOP to make policies (www.nigeria.gov.ng) and issue directives as contained in Section 33 of the Electricity Power Sector Reform Act (EPSRA). This article discusses the key highlights of the PSRP Policy, the Directives and their likely impacts on the Nigerian Electricity Supply Industry (NESI).



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Key Highlights of The Directives

The key directives to each stakeholder as contained in the Directives are summarized below:

Legend

Completed	
Work in Progress	
No Progress Reported in Public Domain	

1. Directives to Nigerian Electricity Regulatory Commission (NERC)

S/N	DIRECTIVES	STATUS
1	Abide by the requirement for periodic major and minor reviews and processing of valid claims for deficits in tariffs.	
2	Order a new minimum share capital for operation of a Distribution license and ensure compliance with same.	
3	Encourage and facilitate bilateral transactions with Competition Transition Charge (CTC) as compensation, where applicable, to the Distribution Companies (Disco).	
4	Permit all customers currently being supplied using 132 kv/330kv to contract as Eligible Customers directly from Generating Companies (Gencos).	
5	Granting license to Mini Grid applicants and Eligible Customer applicants expeditiously in accordance with the timelines prescribed in the regulations.	
6	Withdraw orders against, willing-buyer willing-seller transactions in particular, orders against Viathan and Cummins.	

2. Directives to Nigerian Bulk Electricity Trading

S/N	DIRECTIVES	STATUS
1	Design measures to refinance accumulated debts that the Discos owe and are in turn owed to Gen-cos and Federal Government of Nigeria (FGN) (through the Payment Assurance Programme).	
2	Enforce settlement calendar as captured in industry contracts, regulatory orders and the Market Rules and present for adoption any adjustments and variation necessary to recognize unforeseen development such as the Payment Assurance Programme.	
3	Enforce Disco securities after consideration of agreed minimum thresholds based on agreed ATC and C losses and verified tariff deficits.	
4	With the Market Operator, design, and present for policy direction and NERC regulatory action, a revenue management and collection distribution scheme for the energy purchased by NBET for a transitional period to impose a fairer distribution of the industry revenue collected by Discos.	

3. Directives to Bureau of Public Enterprises (BPE)

S/N	DIRECTIVES	STATUS
1	Perfect shareholder loan and options for loan recovery of FGN's investment in distribution companies under the Distribution Expansion Programme.	
2	Complete transfer of 40 percent shareholding to persons appointed by the President to represent FG shareholding.	
3	Manage the expiry date of 31 st December, 2019 (for nine Discos) and 31 st December, 2020 (for Kaduna) of the existing Agreements with the Discos to ensure compliance with the Business Continuity Regulation to be issued by NERC.	
4	Manage renewal with qualified, interested core investors or new investors on terms for capitalization, performance improvement, customer satisfaction, metering, franchising and bilateral power purchase etc.	

4. Directives to Transmission Company of Nigeria (TCN)

S/N	DIRECTIVES	STATUS
1	Spin-off an independent system operator after satisfying conditions precedent outlined in the ruling documents and effectively separate its operations, assets and liabilities from those of the Transmission Services Provider licensee.	
2	Support transmission requirements of bilateral contracts with investment, facilities and contracted maintenance to enable Transmission Use of Systems Agreements with a commercial tariff and service level guarantees and liquidated damages for default.	
3	Progress implementation of the Transmission Rehabilitation and Expansion Plan for medium and long-term expansion and the stability of the national grid generally. In the short term, TCN is also expected to complete and continue various measures to expand and stabilize the grid. The TCN is also to enforce compliance with the Grid Code and Market Rules.	
4	Enforce full payment of the Market Operator's invoice in accordance with the Market Rules.	

5. Directives to Federal Government of Nigeria (FGN) and National Economic Council (NEC)

S/N	DIRECTIVES	STATUS
1	State and Local Governments are encouraged to partner with Discos and develop/sponsor Mini-Grid projects and franchise operators of 33 and 11KV feeders. They are also encouraged to guarantee power payments to those feeders.	
2	FGN to implement the Distribution Expansion Programme to broaden paying customer base in NESI and ensure payment of electricity bills.	

Key Highlights of The Power Sector Recovery Plan Policy Statement

The PSRP Policy Statement reflects the policy direction of the Power Sector Recovery Programme (PSRP) of the Ministry and provides guidance for regulatory action by NERC. The objective of the PSRP Policy is to reset the NESI to sustainably deliver electricity services at fair pricing.

The Policy seeks to achieve this by focusing on five areas:

- Collection Efficiency
- Payment Discipline
- Capitalization and Liquidation
- Tariffs
- Incremental power

The action points for each focus area are summarized below.

TARIFF

The PSRP is to be implemented over time through a simplified tariff methodology, which accurately reflects market realities and the cost of producing and delivering electricity with reduced consumer resistance. Some of the key action points to achieve this are highlighted below.

a	Completion of Minor Tariff Methodology in Q4 2017	
b	Completion of customer enumeration and asset mapping	
c	NERC to issue statement that tariff must cover all gas, generation, transmission and distribution costs across the value chain.	

INCREMENTAL POWER

The PSRP Policy is aimed at attaining an increment in generation, transmission and distribution above 4500 MWh/h.

a	<p style="text-align: center;">Completion of Legacy Projects</p> <p>The policy directs that both legacy projects and new projects, which sustain gas supply, generation, transmission and distribution output of above 4500 Mwh/h should be completed.</p>	
b	<p style="text-align: center;">Implementation of the Distribution Expansion programme</p> <p>The policy proposes that the Distribution Expansion Programme be implemented to ensure the offtake of 2,000 MW unutilized power. The required investment in the distribution network may be provided in two ways; either as shareholder's loan by the Federal Government through BPE/MOFI or through supply of distribution equipment by Federal Government or any investor.</p>	
c	<p style="text-align: center;">Implementation of the Transmission Expansion Programme</p> <p>The policy directs that Transmission Network Rehabilitation and Expansion plan be implemented via loans to be obtained from World Bank, African Development Bank, Agence France de Development and the Japan International Cooperation Agency.</p>	

COLLECTION EFFICIENCY

The policy looks to achieve and exceed the contracted and committed ATC&C loss targets and sustain aggregate collection efficiency above 60 percent. The action points to achieve this are discussed below.

a	<p style="text-align: center;">Establishing a centralized payment scheme for FGN MDAs</p> <ul style="list-style-type: none"> • The MOP, Ministry of Defence, the Armed Forces, NERC, NBET and Discos to agree a framework for implementing a centralized payment scheme by July 31st, 2019. • Deployment of automated meter reading platforms to enable power metering • MOF, M.O and NBET to agree bill verification and settlement procedures 	
b	<p style="text-align: center;">Acceleration of Meter Roll out</p> <p>Some of the key action points to achieve this include:</p> <ul style="list-style-type: none"> • Procurement of Meter Asset Providers (MAPs) by Discos • Execution of compromise with Ziklagnosis that converts the N119 billion judgement against the FGN into a N39 billion loan to Ziklagnosis to roll out meters as MAPs 	

c.	Issuance and operationalization of Franchising Regulation To ensure collection efficiency, the PSRP Policy provides that NERC issue the Franchising Regulations to empower investors and independent operators in deploying operations and infrastructure to deliver premium services to target underserved and underserved consumers.	
d.	Issuance and operationalization of Mini-Grid Regulations In order to empower unserved and underserved consumers to contract premium services from developers, the policy directs that NERC issue the Mini-Grid Regulation. Other key action points include: Discos partnership with Distribution Asset Providers and Mini Grid Developers to deliver premium services to target customers.	
e.	Issuance and operationalization of Eligible Customer Regulations The Policy directs that NERC issue and operationalize the Eligible Customer Regulations. Key action points include: Gencos to market their capacity to Eligible Customers; Discos to partner with Distribution Asset Providers to serve Eligible Customers and franchisees, the development of template for PPAs and TUoS Agreement for Eligible Customer transactions.	

CAPITALIZATION AND LIQUIDITY OF THE NESI

The policy looks to secure capital and liquidity to ensure that all market participants, particularly those upstream of Discos, are paid according to contracts and are adequately funded to sustain and expand operations.

a	Payment Assurance Programme In a bid to improve liquidity in the market, the policy directs the CBN and NBET to execute N701 billion loan agreement to assure Gencos and their suppliers' payments through 2018.	
b	Disbursement of the Nigerian Electricity Market Stabilization Fund The policy directs that CBN and NERC ensure full disbursement of the NEMSF Fund.	
c	Disco Recapitalization The PSRP Policy directs that Discos issue and sell new shares to raise additional equity capital. It also directs that BPE adjust the share sale agreements to authorize where necessary, dilution of the shareholding of the private investor and/or the FGN.	
D	Debt Refinancing NBET, Debt Management Office (DMO), Central Bank of Nigeria and Ministry of Finance are to complete a bond issuance as a means of ensuring Discos repayment of any part of the Payment Assurance Programme exposure.	
E	MDA Debts In dealing with MDA debts, the strategy is to audit, verify and pay MDA debts post 1 st of February 2015 either by direct payment to upstream market participants or a discountable payment financial instrument.	
f	Discos Balance Sheets The PSRP Policy proposes the need to structure and secure accumulated debts beyond those taken care of by NBET's promissory note and bond.	
g	Forex The Policy directs as follows: <ul style="list-style-type: none"> • CBN provide forex for critical spare parts and service payments • CBN to convert to acquisition debts into naira • BPE, Ministry of Water Resources and Ministry of Finance to covert concession fees into naira 	
h	Debt Resets The PSRP Policy directs the CBN to reclassify electricity industry debts and facilitate direct payment of debt obligations by NBET under the payment assurance programme.	

PAYMENT DISCIPLINE

The policy seeks to promote actions that strengthen financial transparency and equal distribution of industry revenue to stakeholders.

a	Collection Administration The policy directs that a revenue settlement and collection scheme, which ensures fairer distribution regime be developed. NBET, the MO, Discos and CBN are to design the collection and settlement scheme.	
b	Strengthening Government Board Representation The policy proposes that efforts to achieve payment discipline need to be complemented by government's representation on the board of Discos.	

c	Forensic Audit The policy provides that a thorough forensic audit of the Discos is required particularly with respect to revenue collection accounts.	Yellow
d	NSE Listing Disco are required to take steps for listing on the stock exchange.	Red
e	Contract Effectiveness The policy proposes that industry contracts are made effective. To this end Gencos, NBET and Discos are directed to negotiate amendments as necessary to the power purchase agreements and vesting contracts as applicable.	Green

Highlights of The Policy Statement

The Power Sector Policy Statement, similar to the PSRP Policy, provides guidance for regulatory action by NERC. The Policy Statement has identified five key issues/objectives it seeks to achieve and highlights the regulatory direction for each objective. They are as follows:

1. Bilateral Market: The Policy Statement proposes that the NESI is opened up for more bilateral trading between Gencos and end users. The proposed structure for the proposed bilateral NESI is as follows:

- i. The Gas suppliers provide gas to the Gencos under a gas sale agreement
- ii. The Gencos supply power to end users under a power purchase agreement
- iii. The Gencos also execute a transmission use of system agreement (TUoS) with TCN as well as Distribution Use of System Agreement (DUoS) with the Discos.
- iv. The only contractual relationship between the Discos and the end users will be a service agreement.

2. Regulatory Framework: The Policy Statement proposes that policies and regulations, which enable customers procure services at negotiated prices with Discos, their partners or from independent investors/developers with minimal disruption of services, should generally be put in place. Such regulations (some of which are already in place) include: Eligible Customer Regulations, Meter Asset Provider Regulations, Electricity Distribution Franchising Regulations; and the Competition Transition Charge Regulation .

3. Licensing and Approval: NERC is encouraged to cooperate with consumers, project developers and investors and make conditions for the issuance, amendments, cancellation and enforcement of permits and licenses easy.

4. Distribution Expansion Programme: The Policy provides that the Federal Government, being a shareholder in Discos, will invest in new distribution infrastructure required to deliver available generation and transmission capacity to consumers.

5. Recapitalization of Discos: In order to improve the services of Discos through investment in distribution networks, the Policy Statement proposes that additional capital is raised by Discos.

6. Vision 30:30:30: The Government is enjoined to re-invigorate its initiatives to achieve 30GW delivered to consumers with 30 percent from renewable sources by the year 2030. This will be achieved through strategic projects like Zungeru, Mambilla, Afam Three Fast Power, Gurara etc. as well as the Transmission Rehabilitation and Expansion Programme poised to achieve 20,000 MW transmission capacity in 2023. (We note that the Policy mentions the Afam Three Fast Power as a renewable project however our research shows it is a gas-powered plant. Vanguard March 27, 2018) .

Key Considerations to The Implementation of The Directives and Policy Documents

This section highlights some of the key considerations necessary for the proper implementation of the Directive/Policy.

1. Development of framework for the migration to bilateral Power Purchase Agreements (PPAs):

It is imperative that a framework is established for the migration of vesting contracts into bilateral contracts between Genco's and Discos. A key consideration to be managed under such framework is the process for such migration/ procurement.

2. Development of Infrastructure: In order to effectively achieve the policy objectives, the infrastructure deficit in the industry needs to be remedied, particularly in achieving incremental power in the NESI. While we note that the policy enumerates key action points for investment in distribution and transmission lines, it remains to be seen if the infrastructure deficit can be remedied.

3. Credit worthiness of Off-takers: While the Directives, the Policy and Policy Statement focus on the improvement of bilateral trading in the NESI, a key issue that arises is the credibility of the off-takers. Eligible customers, sub-franchisees and other trading entities must be credit worthy to meet payment obligations under the bilateral contract, otherwise the illiquidity issues in the market will subsist.

4. Licensing of Traders: Since privatization in 2013, NBET has remained the sole trader in the NESI, carrying out bulk purchase of electricity from Gencos for resale to the Discos. In view of the intention to increase bilateral trading and subsequently phase out of NBET, NERC will need to develop a framework for granting of subsequent trading licenses to interested entities.

5. Tariff Structure for Bilateral Contracts: Pursuant to the Multi-year Tariff Order (MYTO) 2015 (Section 15 of MYTO 2015 for Abuja Electricity Distribution Company from 1st of January, 2015 to December 2024), where a Disco elects to

procure electric power from a Genco or an Independent Power Producer (IPP), NERC is to recognize such bilateral rates to be agreed, provided that procurement procedure is done prudently even where the agreed prices are higher than the MYTO benchmark price for generation. While this suggests that parties are able to agree a cost-reflective tariff, developers must be mindful that the current regulated Disco customer tariffs are not cost-reflective. As such, there is still a credit risk in dealing directly with the Discos.

6. Injection of Capital/Fresh financing: The Directives, the action points contained therein and policy documents all show that an influx of capital is required in the NESI. We note that while this funding is required in the NESI, the industry does not have a good credit reputation for reasons that include over-exposure in the NESI, single lender obligation limit and poor collections and remittance. These limitations are also unlikely to change until some improvement is seen in the market. Stakeholders are encouraged to explore alternative funding options to meet the capital requirements in the NESI.

7. Enforcement of Payment Security: One of the action items to NBET under the Directives is the enforcement of the payment securities provided by the Discos under the vesting contracts. (Paragraph 2e of the Directives.) This directive may be impossible to execute in light of the subsisting injunction given by the Federal High Court, Abuja restricting, among others, NBET and Gencos from enforcing the payment securities provided by the Discos. The injunction will need to be lifted in order for NBET to comply with the directive.

8. Regulatory Framework: The proper implementation of the Directives is contingent on the establishment of a permissible framework for competition transition charge, distribution franchising and distribution asset providers, which are an integral part of the action plan contained in the Directives and policy documents.

9. Political Will and Stakeholder Willingness: In order to achieve its intended objectives, a key consideration required for all stakeholders (especially government parties) is the willingness and drive to ensure the compliance and execution of the Directives and PSRP. Although the Directives are direct instructions from the Ministry, which must be followed by stakeholders, the PSRP Policy and Policy Statement are policy documents with limited effect under law. Thus, since stakeholders may not necessarily be penalized for non-compliance with the PSRP, the onus then lies on all stakeholders to promote the Ministry's agenda for the NESI.

Impact of The Directives and Policy Documents

The following are likely implications of the Directives and policy documents on the NESI:

- 1. Medium-Term Market Phase:** Based on a combined review of all the documents, it appears the MOP is intent on transitioning the market to the Medium-Term Market Phase as both documents contain provisions, which enable bilateral relationships between generating companies and distribution companies/end-users, thereby promoting competition and full liberalization of the NESI.
- 2. Improved Access to Electricity:** In view of proposals to increase bilateral arrangements between Gencos and end users, it is expected that access to electricity will improve as the unserved or underserved end-users will have the ability to procure electricity directly from generating companies.

3. Improved Distribution and Transmission Network: As highlighted above, if properly implemented, the distribution expansion plan will lead to increased investment in the distribution and transmission networks, ultimately improving the strength and capacity of electricity networks.

4. Ceding of Disco Franchise Areas: Based on the Directives, it is expected that the Distribution Franchising Regulations will be established. This regulation will provide a framework for the ceding of distribution franchise areas to qualified investors and operators. As is, many Discos are unable to provide electricity at optimal service levels to all end-users within their franchise areas. The franchising regulations will therefore create an opportunity for Discos to cede portions of their franchise areas, which will ultimately lead to improvement in services. (AEDC & Ors. v. NERC & NBET (Judge Abang presiding) and EEDC & Ors. v. NERC (Justice Ademola))

5. Improved Liquidity in the NESI: If implemented properly, the Directives and policy documents are poised to improve liquidity in the NESI. It should be noted that as the market liquidity improves, the credit ranking of the NESI will also improve and participants will be able to access more financing for projects.

6. Minimization of Government Intervention in the NESI: If properly implemented, it is expected that the improvement in the market's liquidity will reduce and eventually eliminate NESI's reliance on government interventions or grants.

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