

Update to Nigeria Governor's Forum on Electricity Sector Topics

Presentation by Special Adviser to the President on Infrastructure (Secretary
Power Sector Reform Working Group)

Wednesday 16th June, 2021

Agenda

1. Transfer of DISCO Equity to States – outcome of NEC Ad-hoc committee work
2. Leveraging VAT to cover electricity subsidy 2020 and 2021
3. Management of State and Local Government MDA debt and bills
4. AOB

Sector Overview and progress

Tailwinds +

Market Collections

- Tariff rose by 36% from September '20 ... **collections have grown by 60%+**
- Government subsidy has been reduced by N20 billion per month
- Record collections of N65 billion hit in December '20 cycle (from average of N39 billion)

Generation

- Delivered Average Power rose by a peak of 15% post Service Based Tariff implementation (as DISCOs improved service to higher bands)
- Peak Power of 5,800MW hit in March of 2021

Metering

- 580,000 meters received by DISCOs from January to June 2021 under the phase 0 National Mass Metering Program (425,000 installed)
- This exceeds the number installed in 18 months of the MAP program
- All meters being procured locally creating jobs in assembly/installation
- 6-million-meter gap being fully funded through CBN loans and W.Bank

Investment

- Return of investment with N105 billion Afam III,IV,V sale and Yola DISCO disposition of N19 billion, interest in Zungeru and NIPP Eol
- **N240 billion in Emergency CAPEX** provided by CBN for interface repairs and DISCO in network improvements



Headwinds -

Macro Economic Factors

- FX changes impacting cost reflective tariff
- Inflation impact limited but rising
- Delays in implementation of Gas Pricing committee report may impact July Tariff

Pace of CAPEX investments

- Power needs to be boosted to limit tariff impact, CAPEX investments launched in June, need acceleration
- Capacity of market to spend/absorb CAPEX funds needs ramp up

Labour

- Progress being made with joint FGN-Labour committee on agreement to ensure minor reviews continue on time
- Implementation Committee engagements positive thus far but need continued monitoring

Insecurity and MDA debt

- Challenges in power supply to Borno and environs due to vandalization from Insurgents ... multi-pronged solution in process
- Payments and funding for insecure areas unclear causing increased market shortfall and impacting collections/liquidity

Transfer of DISCO Equity to States – outcome
of NEC Ad-hoc committee work

Origin of the NEC Ad-Hoc Committee on Ownership Review and Analysis of DISCOS and Power Reform

Scope of Work

Ad-Hoc Committee on Ownership Review and Analysis of DISCOS and Power Reform

To review the status of the ownership structure of the partially-privatised electricity power distribution companies (DISCOs).

Committee Membership: Governors of Kaduna, Adamawa, Anambra, Edo, Kebbi, Lagos, Plateau and BPE, NDPHC, TCN

Terms of Reference

DISCO Ownership/Performance Sub-Committee

1. Ownership and Shareholding Analysis
2. Review of Collections and Remittance (NERC Open Review Data)
3. Review of investment and Capital Expenditure
4. Governance structures and processes

Participants: State House, EDSG, Ministry of Power, Ministry of Finance, NERC, BPE, REA, APGC, ANED, TCN, NBET, NDPHC, KPMG (independent consultants)

Reform Revitalization Sub-Committee

1. Privatization
2. Transactions/Decisions Review
3. Commercial and Financial Transactions Review
4. Reform Process Review
5. Market Design Review

Participants: BPE, NERC, APGC, ANED, TCN, NBET, NDPHC, PWC (independent consultants)

Result - Review of sale process

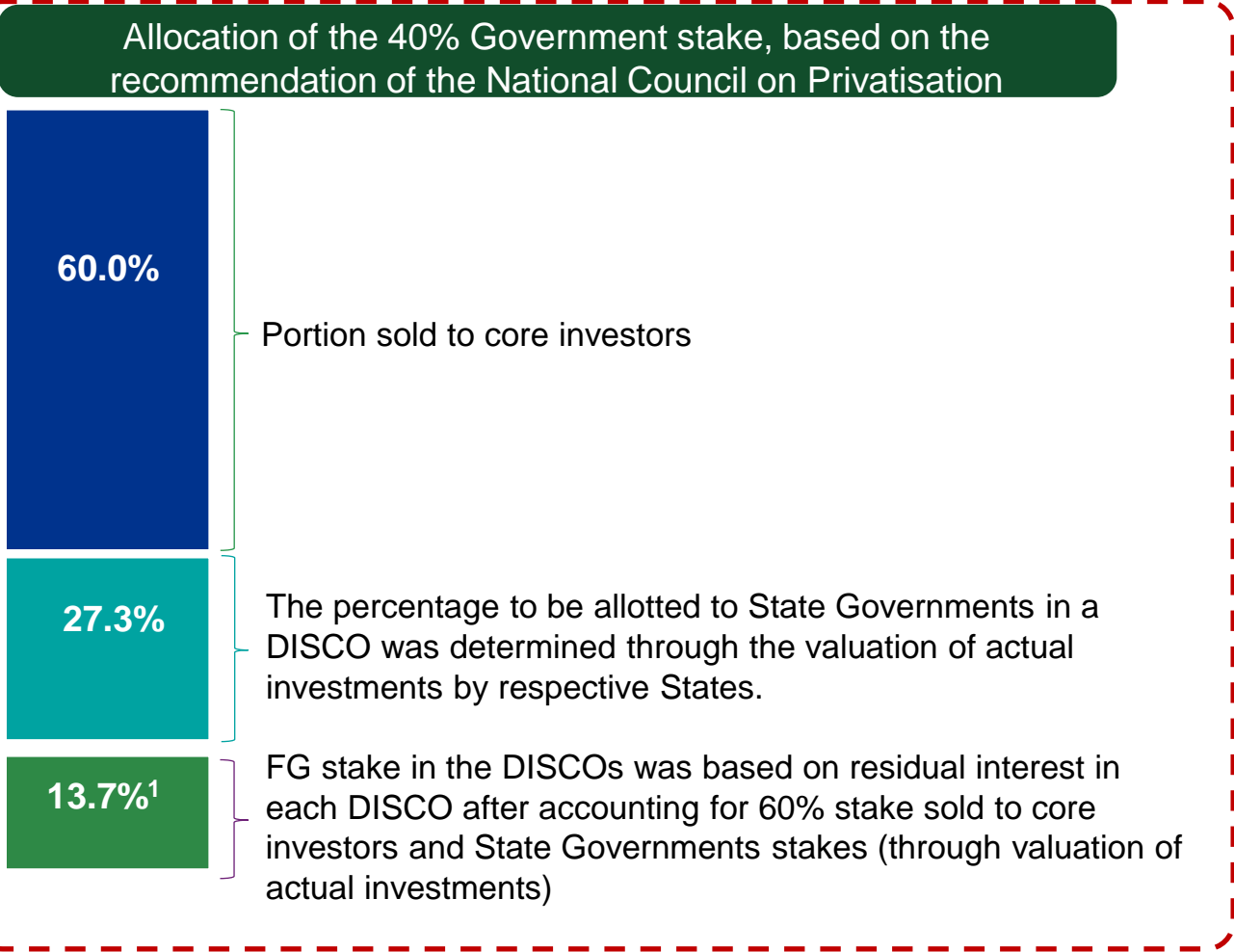
Pre-sale ownership structure



1. Presale ownership structure was based on the following representations;
 - Annual appropriations were made from Federal Government’s account to the defunct PHCN
 - Employees of the defunct PHCN were Federal Government staff
 - States Government were not compensated for their investments in each Disco
 - The NCP decision to allocate shares proportionate to States contribution to Discos Regulated Asset Base was to compensate the States for their investments (state government equity holdings were not determined at the time of sale)
2. Upon sale of 60% equity in each of the Discos, the proceeds were used to compensate former PHCN workers instead of reinvestment in Discos

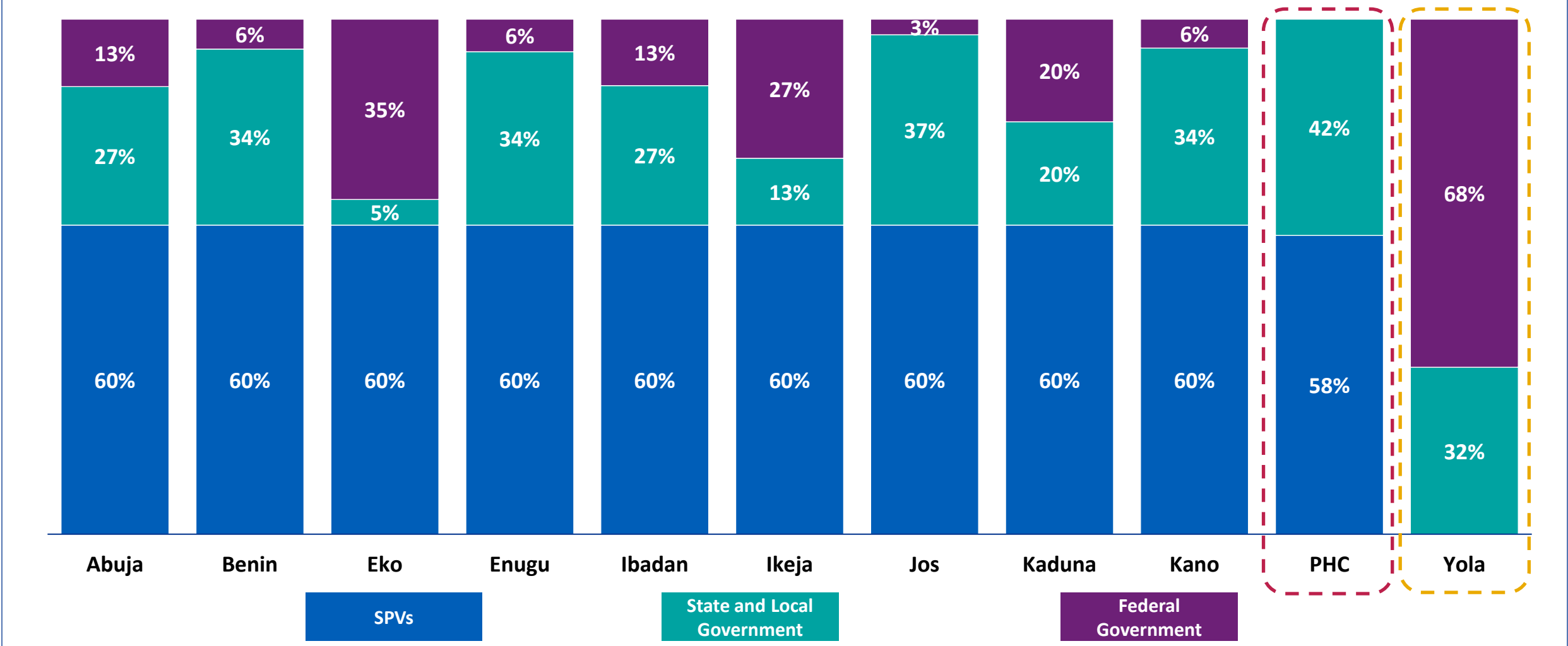


Post sale ownership structure



1. Included in the 13.7% is the equity allocated to former employees of PHCN. This translates to the lower of 2% of the total Discos stake and 10% of Federal Government’s stake (representing c.1.4%) is to be reserved to former PHCN employees

Result - Shareholding structure of the 11 DISCOs



Federal Government stake completely eroded by the State Government and Local Government

Yola DISCO is fully owned by the Government (Federal and State)

While the process to transfer equity to States is kickstarted, there are proposals for NSIA to take over the management of Government equity in the DISCOs

Next Steps

NGF BPE meeting

- DG BPE to provide updates on process to be followed to hand over shares to Nigeria Governors Forum

NCP ratification of share transfer

- The outcome of the ad-hoc committee's report will be presented to the NCP for approval to allow BPE formally commence process for share transfer

NERC approval of new share-holding

- BPE to work with representatives of Governors Forum to finalise share transfer within each DISCO ahead of submission to NERC for ratification

Official transfer of shares

- Upon NERC ratification, there will be formal transfer of shares to the different states in each DISCO and agreement of new board representations.



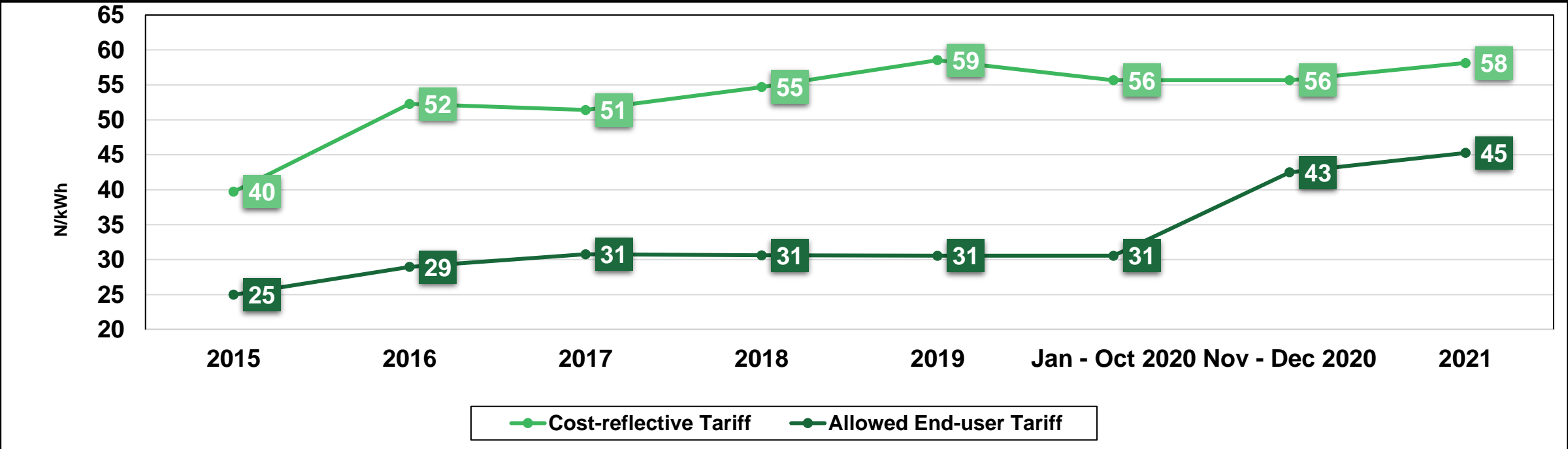
Proposed NSIA intervention

- The process to transfer equity to the states will take time and a number of process steps
- It is also clear that BPE does not have the specialisation to hold active management of equity in companies (i.e. the DISCOs) and hold the private sector investors to account
- There have been exploratory conversations about the transfer of Government shares to the Nigeria Sovereign Investment Authority (NSIA) for management
- In this capacity, NSIA will be responsible for providing adequate representation on the boards of the DISCOs as well as monitoring the day-to-day performance of the core investors
- Furthermore, ongoing reforms mean there could be a need for new equity injection into the DISCOs; the Government parties need to match contributions by private sector players to prevent dilution of equity. This could be in the form of convertible loans.

Leveraging VAT to cover electricity subsidy 2020 and 2021

History of tariff under-recovery and subsidy

	Unit	2015	2016	2017	2018	2019	Jan - Oct 2020	Nov - Dec 2020	2021
Cost-reflective Tariff	₹/kWh	40	52	51	55	59	56	56	58
Allowed End-user Tariff	₹/kWh	25	29	31	31	31	31	43	45
Tariff Shortfall	₹/kWh	15	23	21	24	28	25	13	13



Presidential directives on electricity tariffs.

1| Approval to proceed with tariff adjustment ... effective 1st September 2020

2| Directive for the immediate implementation of the following conditionalities...

- i) **Payment Discipline:** Measures aimed at improving payment discipline by deducting funds directly from the accounts of DISCOs to pay off market liabilities and punitive actions aimed at sanctioning defaulting discos (MoF and CBN)
 - ii) **Protection for the Poor:** Introduction of service-based tariff that will allow DISCOs to charge richer consumers that are metered and receiving higher quality of service a cost reflective tariff. No tariff will be experienced by poor Nigerians receiving low quality of service (NERC, MoP)
 - iii) **Mass Metering:** The implementation of a mass metering scheme to be supported by the Central Bank of Nigeria and the World Bank (MoP, NERC, CBN, MoFBNP)
 - iv) **Arbitrary Billing:** Instituting a ban on arbitrary billing by DISCOs pursuant to a subsisting Nigeria Electricity Regulatory Commission (NERC) capping regulation (NERC, MoP)
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3| Directive for the Vice President to coordinate relevant stakeholders for successful implementation of the overall reform

4| Consideration of report of the ad-hoc committee set up by Mr. President for “noting and further action”

Tariff reform and labour engagements – summary of labour engagements

28/09/20: Organised Labour and FGN committee agreed to 2-week suspension of SBT and created Technical Committee (TC) to examine the tariff increase and advise on next steps

15/10/20: Technical committee completed phase 1 of its work – tariffs were to be reduced by ~N2/kWh and the gap was to be funded from VAT collections in the NESI

29/11/20 – 03/12/20: As part of its phase 2, the TC conducted site visits to the 3 DISCOs in the South West conducting engagements with various stakeholders to evaluate the implementation of the SBT

14/01/21 – 22/01/21: Due to COVID-19 disruptions, the TC conducted hearings with only the leadership of the remaining 8 DISCOs and NERC, NEMSA, REA and the Ministerial gas pricing review committee in Abuja

01/02/21: Main Labour/FGN committee grants TC 3-week extension for the submission of its final report

08/02/21 – 12/02/21: TC report finalisation and off-line engagements with Labour leadership to syndicate key recommendations

Highlights of resolution with Labour

- The sanctity of the tariff review process set out under subsisting laws and regulations **must be protected**
- Tentative agreement for the resumption of the January tariffs
- FGN will take all actions required to ensure that the effective tariff only increases due to migration for 2021
- FGN to take major actions to reduce the cost reflective tariff –
 - **Accelerated completion of TCN interface projects**
 - **Further optimisation of gas prices**
- NCP/BPE to ensure that the DISCO performance agreements are reviewed timely (before Q4 2020) and aggressive targets are set for core investors to reflect increased metering and infrastructure

2020/21 NESI VAT collections are required to augment FGN funding for the financing plan to cover the cost of subsidised electricity has been provided to the citizens

What is the financing plan

- The PSRP Financing Plan has been prepared by a multi-agency technical committee, led by the Federal Ministry of Finance, Budget and National Planning.
- The Power Sector Recovery Plan (PSRP) Financing Plan quantifies the FGN funding required by the sector for the period 2020-2026 to clear historical tariff shortfalls and fund new tariff shortfalls
- The Financing is underpinned by the following 3 key principles –
 - Credible and realistic
 - Complete
 - Fiscally affordable and sustainable

Key take aways –

- The financing plan envisages cumulatively liabilities of N1.3 trillion – this excludes the ~N1.5 trillion which the Federal Government is to settle directly with the CBN.
- Through a combination of loans from the CBN, World Bank as well as Annual budgetary allocation, the Federal Government will be solely **responsible for 90% of the liabilities**.
- Effectively States and Local Governments are only being requested to forgo N55 billion in VAT revenues to help maintain the sanctity of the 3 core principles of the plan

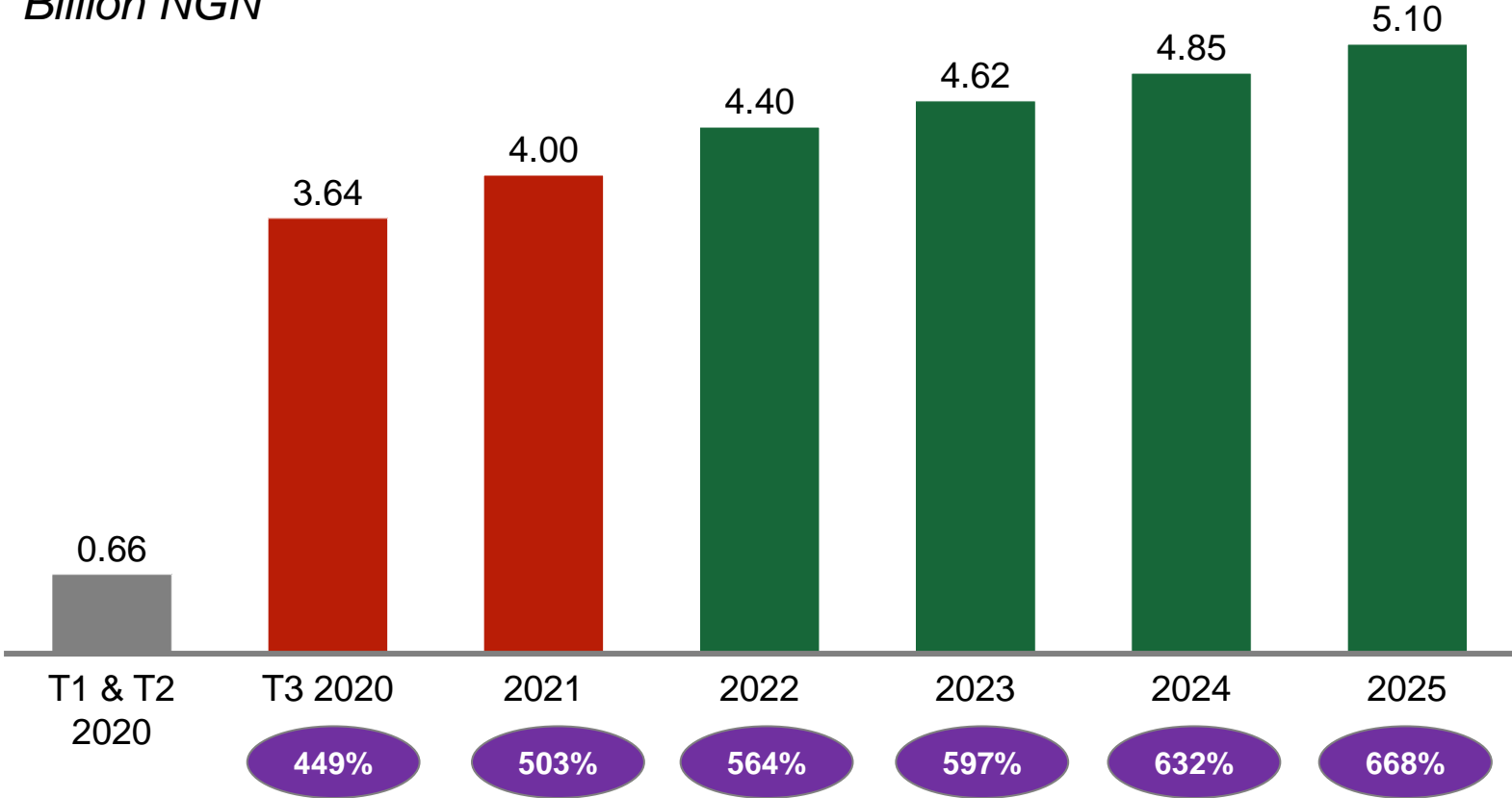
Use of Funds (Billion Naira)	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	Total 2020-2026
Historical (2015-2019) tariff shortfall arrears	-	-	-	-	-	-	193	119	119	119	551
NEW Sector tariff shortfalls funded Yt	115	430	581	286	62	-	-	-	-	-	348
NEW Sector tariff shortfalls funded Yt+1	-	-	-	-	217	238	-	-	-	-	454
CBN PAF Debt Service Payment	-	43	66	-	-	0	0	0	0	0	-
Total Use of Funds	115	473	647	286	279	238	193	119	119	119	1,354

Source of Funds (Billion Naira)	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026	Total 2020-2026
CBN Payment Assurance Facility	115	430	581	165	-	-	-	-	-	-	165
FGN Budgetary contribution	-	43	66	81	139	119	130	119	119	119	828
Retained VAT Monies	-	-	-	-	62	-	-	-	-	-	62
WB PSRO \$730m facility	-	-	-	40	78	118	63	-	-	-	299
Total Source of Funds	115	473	647	286	279	238	193	119	119	119	1,354

State and Local Governments still stand to receive ~N200 billion more than in VAT proceeds due to the payment discipline reforms over the next 5 years

Average monthly VAT collections from DISCOs: 2020 - 2025

Billion NGN



As a result of the reforms on VAT collections, total VAT collections from the NESI will increase by ~N250 billion between 2020 and 2025

Remitted to FAAC
 Funds to augment financing plan
 To be remitted to FAAC

Take-aways

- In total, the VAT collections reform will increase remittances to FAAC by ~N250 billion over the next 5 years.
- The request being made is for the use of the VAT collections for T3 2020 and the whole of 2021 worth ~N60 billion to augment the Power Sector Financing Plan and fund subsidies provided to the citizens under the SBT
- Upon the attainment of cost reflectiveness in 2022, NESI VAT proceeds will be paid in full to FAAC for distribution among all tiers of Government.

X % increase in VAT collections relative to T1 & T2 2020

Management of State and Local Government MDA debt and bills

We require a long term solution to resolve non-payment of electricity bills by MDAs across all tiers because of the moral hazard it creates for the Government

DISCO	Total DisCo Bills	Total DisCo Collection	MDA Outstandings	MDA share of uncollectibles
ABUJA	90,217,653,379.37	79,040,455,704.06	4,660,274,817.83	42%
BENIN	83,212,986,614.92	43,969,947,712.27	484,417,679.70	1%
EKO	102,576,191,967.20	79,801,150,392.73	3,712,795,807.89	16%
ENUGU	61,230,000,000.00	45,493,787,863.98	1,116,751,569.82	7%
IBADAN	97,836,138,796.81	59,373,917,402.36	1,859,795,152.45	5%
IKEJA	128,025,352,860.00	87,062,258,475.72	2,486,866,745.61	6%
JOS	30,239,647,772.90	17,482,663,583.76	2,029,773,392.83	16%
KADUNA	38,727,000,000.00	20,758,753,526.70	9,389,938,361.27	52%
KANO	50,226,210,045.60	31,614,318,773.36	2,635,001,547.43	14%
PH	59,816,433,968.26	29,524,787,437.64	602,824,586.33	2%
YOLA	17,883,440,550.65	10,340,757,352.61	1,540,535,681.24	20%
TOTAL	759,991,055,955.71	504,462,798,225.18	30,518,975,342.39	12%

TAKEAWAY

- Cumulatively across the DISCOs, MDAs only account of **8% of bills but accounted for 12% of non-payments**.
- Under the payment discipline regime, DISCOs are required to make 100% market payments irrespective of their actual collections.
- This means DISCOs are sometimes forced to take loans to cover non-payment by MDAs which creates a moral hazard for the Government.
- Between Sep 2020 – May 2021, DISCOs borrowed ~N25bn to cover MDA non-payments**
- The MDA loss component in ATC&C loses leads to an increase in the cost reflective tariff which causes hardship on citizens.

There are two potential options for managing State/LG bills going forward in a way that ensures settlement to the DISCOs on verified bills

DEBT:

Jan 2015 – July 2021

Verification:

- I. To be covered under FGN funded verification exercise
- II. Verification exercise will involve representatives from the relevant MDAs and state ministry of finance

Settlement:

- I. States to give approval to Ministry of Finance to do **direct deduction** from January **2022 FAAC allocation** to cover debt



BILLS:

August 2021 and beyond

Proposal:

- I. DISCOs will be required to meter all State and LG facilities with Automated Meter Infrastructure (AMI) which can be read remotely.
- II. A secretariat within the ministry of finance will be set up to track consumption
- III. The State Ministry of Finance will have a chance to verify bills as well before payment.
- IV. Each state will grant the Federal Ministry of Finance the right to deduct verified bills from its FAAC allocation on a monthly basis.
- V. If (IV above fails),
 - A. NESI VAT collections will be escrowed each month and the funds will be used to settle all verified State/LG bills
 - B. Any leftover funds after settlement will be moved to the FAAC account

Appendix

Result - Summary of NERC valuation of state shares (1/2)

S/N	DISCO	Name of SPV	SPV holdings in DISCOs	States holdings*	Total state holdings		
1	Abuja	KANN Utility Company Limited	60.00%	FCT Niger Kogi Nasarawa	11.20% 8.30% 4.20% 3.20%	26.90%	13.10%
2	Benin	Vigeo Consortium	60.00%	Delta Edo Ondo Ekiti	14.00% 8.40% 6.60% 5.20%	34.20%	5.80%
3	Enugu	Interstates Electrics	60.00%	Enugu Imo Anambra Abia Ebonyi	9.60% 7.40% 6.70% 6.00% 4.00%	33.70%	6.30%
4	Ibadan	Integrated Energy Distribution & Marketing	60.00%	Osun Kwara Ogun Oyo	9.60% 7.30% 6.90% 3.30%	27.10%	12.90%
5	Ikeja	New Electricity Distribution Company Limited	60.00%	Lagos	13.00%	13.00%	27.00%
6	Jos	Aura Energy	60.00%	Bauchi Benue Gombe Plateau	16.50% 10.50% 9.60% 0.40%	37.00%	3.00%

*Based on NERC's valuation of State Governments contributions between 2005 and 2013 and does not include contributions from 2014 to 2019

Result - Summary of NERC valuation of state shares (2/2)

S/N	DISCO	Name of SPV	SPV holdings in DISCOs	States holdings*	Total state holdings	Percentage	
7	Kano	Sahelian Power SPV Limited	60.00%	Katsina Kano Jigawa	15.00% 11.90% 7.50%	34.40%	5.60%
8	Port Harcourt	4Power consortium	58.00% ¹	Akwa Ibom Rivers Bayelsa Cross River ²	22.70% 7.20% 6.70% 5.40%	42.00%	0.00%
9	Yola	N/a	0.00%	Taraba Yobe Borno Adamawa	9.30% 8.90% 7.80% 6.40%	32.40%	67.60%
10	Eko	Westpower and Gas Limited	60.00%	Lagos	5.00%	5.00%	35.00%
11	Kaduna	Northwest Power Limited	60.00%	Sokoto Kebbi Zamfara Kaduna	9.20% 4.70% 3.60% 2.60%	20.10%	19.90%

1. Our review of agreed ownership of based on technical proposal submitted (58%) is inconsistent with the internal memorandum from Nigerian Electricity Regulatory Commission (60%).
2. Cross River ownership stake reduced to 5.4% to cap total state holdings to 42%, as against 42.5% presented in the NERC valuation report.