INFRAPOLICYREVIEW

BRICKSTONE

Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry(NESI): Policy, law and regulatory review

Issue 2020005

Introduction

The Nigerian Electricity sector is one of the most significant in the country. Asides from its potential for huge financial contribution to the economy, its impact on businesses' growth and development is also invaluable.

The significance of electricity would reasonably explain why so much attention is always directed at ensuring steady electricity supply. Nigeria's electricity supply profile reveals that a lot of reform programs have been undertaken to boost electricity supply. In 2014, for instance, the electricity sector was privatised with the hope of opening up the sector for better service delivery. This government's action saw to the division of the sector into three groups with each having its own critical part to play in the provision of electricity to Nigerians.

One of the products of the 2014 privatisation is the Distribution Companies of Nigeria (DisCos) responsible for, among other things, providing connection and delivering electricity to consumers, and ensuring proper metering at all connection points.

Despite this privatisation, many issues are still being faced by the electricity service providers in delivering great electricity supply.

In response to these issues, the Nigerian Electricity Commission (NERC), targeting the DisCos, has issued guidelines on distribution Franchising in the Nigerian Electricity Supply Industry (NESI).

This paper considers the objectives of the reform policies, its merits and consideration for new entrants.

Photo Credits: thoughtco.com

Distribution Franchising in the Nigerian Electricity Supply Industry: An Insight

In compliance with the provisions of Electricity Power Sector Reform Act, the NERC licensed eleven (11) distribution companies (DisCos) to undertake a host of regulated activities among which are:

- Connection of customers for the purpose of provision of electric supply
- Installation, maintenance and reading of meters
- Billing and collection of electricity bills

Despite this, however, the DisCos have consistently struggled to satisfy the stakeholders' expectations in the provision of access to reliable and safe electricity services to millions of consumers within their franchise territories especially, the less economically viable. It is against the backdrop of this dissatisfaction, that DisCos sub-franchising became pertinent to improve better quality delivery.

With the introduction of DisCos operations and coverage area sub-franchise, improved quality electricity supply to end-consumer users through metering, billing, collection and network rehabilitation and expansion is expected.

Objectives of the Distribution Franchising in the Nigerian Electricity Supply Industry

Distribution franchising objectives are similar across all industries and NESI is not in any way different. Its objectives are simply:

- Increased business value;
- Increased Profitability;
- Penetration of other markets, in this case the local environment of franchisee under the franchising agreement;
- Capital expansion, lower risk and rapid growth;
- Increased productivity.

These objectives, if achieved, will ultimately benefit the franchisor and their end-user consumers whom it aims to provide better service.

Merits of the Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry

One merit of the guidelines is the ability to facilitate the implementation of quality service delivery to consumers and address some of NESI's operational and liquidity challenges.

Photo Credits: balkaneu.com

It would also provide a great opportunity for DisCos to leverage on emerging business opportunity structure and technology to raise service quality delivery.

It forestalls the possibility of conflict of interest by precluding parties related to DisCos such as its directors and shareholders from entering into franchise agreement with them.

Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry

The "franchising Guidelines" released by the NERC contains a wide variety of provisions. Over all, they are to help mitigate losses that arise due to inadequate metering, inefficient collection system and poor distribution infrastructure all from the DisCos.

A highlight of the key provisions will focus on: Applicable Distribution Franchise Models, Validity of Franchising Agreement, and Revocation of Franchising Agreement.

Distribution Franchise Models: Under this segment, the NERC following public consultation, recognizes four (4) franchising models to wit; (i) Metering, billing and collection; (ii) Total management of electricity distribution function in a ring-fenced area; (iii) Total Management of distribution feeders (iv) Loss reduction and provision of embedded generation.

Very laudable, these franchise models are not cast in iron. DisCos with innovative franchise models can approach the NERC and get approval for such.

Validity of Franchising Agreement: By the provisions of section 4 of the Franchise Guidelines, DisCos cannot enter into any franchising arrangement without NERC's prior approval. They are to obtain a "NO OBJECTION" from NERC. The guidelines do not provide for a timeline within which NERC is mandated to give its approval. However, the commission is to refrain from unreasonable withholding of approval. Similarly, before DisCos can obtain "NO OBJECTION" from NERC, there are commercial and contractual considerations that they must satisfy.

Revocation of Franchising Agreement: The guidelines provide that NERC may on its own accord or based on a third-party petition conduct enquiry into a franchise agreement and if found to have breached laid down rules, revoke agreements hitherto made and the DisCos will continue the provision of electricity services previously performed by the franchisee. Grounds for revocation are as well contained in the Guidelines.

Key Considerations for new entrants in the Industry

The Nigeria Electricity Supply Industry appears to be a viable sector for private investors, especially with the new guidelines on distribution franchising issued. However, there still remains some boxes to be checked by private investors before they make their entry into the industry. Some of these considerations are discussed below.

On the guidelines on conduct of interest, there appears to be a lack of precision with regards to the provision barring conflict of interest. It remains unclear if the parties extends to minor shareholders or stakeholders of a different DisCos seeking franchise agreement with another Disco where they have no stake.

Also, it is a matter of concern that the Guidelines is silent on key protections that investors would typically expect. To illustrate, there is no clearly stated liability of a franchisee in the event of a DisCos breach of terms/ conditions governing its operations.

Due to the structure of the 2014 privatisation, it may be difficult for the DisCos or any of its franchisee to independently achieve better power supply. For emphasis, the DisCos rely solely on the Generating and Transmission Companies of Nigeria to supply electricity to consumers. If there is no corresponding attention paid to the other two groups involved in electricity generation and transmission, it may be difficult for any investment in the DisCos to yield its optimum returns.

The financial capacity of consumers in franchised areas should also be a major consideration for new entrants.

Photo Credits: science.howstuffworks.com

The poverty level in Nigeria is high; it would therefore be an unguarded assumption that if power is supplied, people would pay for it. Beyond supply, attention should be paid to financial viability of consumers to settle the electricity bills without delay. New entrants need to investigate the financial capacity of end-user consumers in Franchised Areas to ascertain if they can pay for the cost of electricity supply and how much they are willing to pay.

One great thing, however, is that new entrants are now afforded a level playing ground. Requirement of open competitive approach as much as practicable in engagement of prospective franchisees by DisCos as well as barring conflict of interest have paved the way for new industry players in NESI.

Asides this, a new developmental reform issued by the Central Bank of Nigeria in August 2020 on the electricity market collection as it concerns the DisCos may hold some ray of hope for the consumers, private entities and even the DisCos alike. The CBN in this reform, tend to ensure transparency in the electricity sector.

"

Before now, DisCos had almost always hinged their inefficiency on a very low collection rate of electricity tariff which has been affecting its financial liquidity and contributing to its revenue shortage. With this new CBN reform and with a designated DisCos' electricity tariff account, commercial banks can now directly collect electricity tariff payment from consumers and be responsible for collecting all DisCos' remittances to both Nigeria Bulk Electricity Trading Plc. (NBET) and Transmission Company of Nigeria (TCN).

It is believed that this new arrangement would help guarantee transparency by ensuring that the cash inflow for DisCos electricity tariff are available to pay down loans and all other obligations to market stakeholders. It would also guarantee the visibility of DisCos' cash flow from electricity tariff. Where this is done, money would be properly monitored, and this would help to mitigate credit risk, such that when loans are given out to DisCos, their income on can be easily traced to know and determine the loan performance.

One unclear thing however is whether the CBN has inherent powers to direct the DisCos, a private entity, on how and what method through which it will receive its income. It is hoped that this issue would be urgently ironed out to avoid friction.

Conclusion

The Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry is a commendable development for the industry. Its provision will promote franchising arrangement which in the long run may be the game changer for the electricity sector of the nation. However, lack of effective implementation may dash the hope of progress the Guidelines raise. It is hoped that proper attentions would be paid to achieving the objectives of the guidelines franchising.

Bibliography

1. Banwo&Ighodalo Newsletter August 19 (2020) “Distribution Franchising in the Nigerian Electricity Supply Industry” Banwo & Ighodalo Law firm

2. Bloomfieldhttp://bloomfieldlaw.com/Publications/Overview_of_the_NERC_Consultation_Paper_for_Franchising_of_Electricity_Distribution_in_Nigeria.pdf

3. Central Bank of Nigeria (2020) “LETTER TO ALL BANKS; DMB LED ELECTRICITY MARKET COLLECTION”. August, 2020.

4. Olaniwun Ajayi Newsletter July 20 (2020) “NERC’s GUIDELINES ON DISTRIBUTION FRANCHISING”

5. Thisday “understanding electricity distribution franchising in Nigeria” https://businessday.ng/energy/power/article/understanding-electricity-distribution-franchising-in-nigeria/amp/

6. Templars Newsletter (2020) “Highlights of the NERC Guidelines on Distribution Franchising in the Nigerian Electricity Supply Industry (NESI)” Templars Law.

Disclaimer

This publication does not necessarily deal with every important topic nor cover every aspect of the topics with which it deals. It is not designed to provide policy, investment legal or other advice. If you do not wish to receive further information from Brickstone Africa about events or research or developments which we believe may be of interest to you, please either send an email to nomorecontact@brickstone.africa

Brickstone is an **Accelerator** with strong competences in the **Appraisal** , **Advisory** and **Project Development** of large scale industrial and infrastructure projects in Africa.

BRICKSTONE

- AGRI-INDUSTRIAL & HEAVY MANUFACTURING
- COMMERCIAL DEVELOPMENTS & HOSPITALITY
- ENERGY & NATURAL RESOURCES
- POWER & RENEWABLES
- TRANSPORTATION & LOGISTICS
- TECHNOLOGY INFRASTRUCTURE

Address

9A Ibeju Lekki Street,
Dolphin Estate
P.O.Box 50939
Ikoyi Lagos

Midel Center , Suite 106
Plot 14,Off Oladipo Diya Way,
Sector Centre D, Gudu District
Abuja

Telephone

+234-814 990 6488
(Direct Line)

Email

hello@brickstone.africa
www.brickstone.africa