JEE Sector Thought Leadership Series

MUCH ADO ABOUT COST REFLECTIVE TARIFF

Taiwo **Adeshina**
Sector Head, Energy & Natural Resources.

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Introduction

Following the handover of the 11(eleven) Distribution Companies (DisCos) and the 6(six) Generation Companies (GenCos) to the core (private) investors and the great expectations that greeted the announcement in November 2015, it would appear that all hopes for improved electricity supply in Nigeria have gradually faded away. Three years post-privatization, Nigerians are still far from being convinced that the core investors in the unbundled power companies truly possess the requisite technical expertise, experience and financial capability to improve the state of electricity generation and distribution across the country. Some consumer groups have already called for the reversal of the entire privatisation process by the Federal Government describing it as a failure. Other stakeholders have expressed the view that the issues which characterized the power sector pre-privatization such as poor electricity supply, broken-down infrastructure and non-meeting of consumers remain prevalent across the country.

In their reactions to the public outcry and contrary to popular opinion, the core investors argue that the successor companies are engulfed with various legacy issues which they inherited from the now defunct Power Holding Company of Nigeria (PHCN). More specifically, the investors have consistently expressed a view that suggest that their poor performance can majorly be attributed to the absence of a Cost Reflective Tariff (CRT) for electricity in Nigeria. Where a tariff is cost reflective, it is expected that such tariff reflects all the costs of electricity generation, transmission and distribution. By implication, the costs are passed-through to and borne by the consumers.

In Nigeria, the Nigerian Electricity Regulatory Commission (NERC) is primarily responsible for the regulation and approval of electricity tariff. In exercise of its powers under the law, it established a methodology for regulating electricity prices called the Multi-Year Tariff Order (MYTO). The MYTO provides a 15-year tariff path for the Nigerian electricity industry with limited minor reviews each year in the light of changes in a limited number of parameters (such as inflation and gas prices) and major reviews every 5 years, when all the inputs are reviewed with stakeholders. One key objective of the MYTO is to ensure that the prices charged by licensees are fair to customers and sufficient to allow the licensees to finance their activities and to allow for recovery of their (efficient) costs, including a reasonable rate of return on capital.

As a defence to the public criticism for their failure to meet the expectations of Nigerians in relation to improved power supply, the electricity generation and distribution companies argue that the current tariff for electricity generation and distribution by the NERC falls significantly short of the expectations of a CRT. As a result, most private sector investors and financiers are disinterested in financing projects embarked upon by the power companies because there is no guarantee that they would reap a return on their investments.

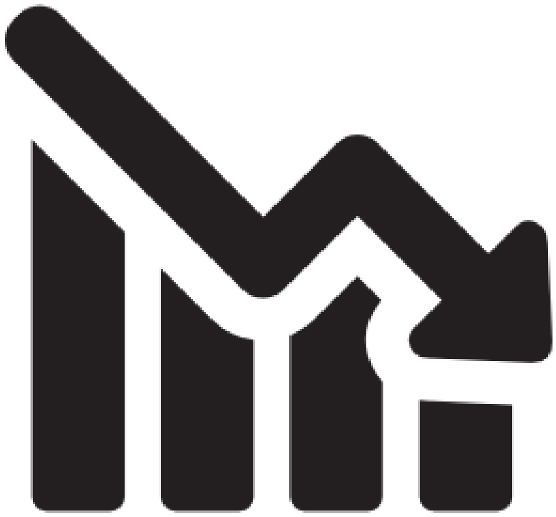
As attractive as this 'CRT argument' may appear, it does not appear that the approval of a CRT will have such a significant transformational impact on the electricity sector. Some more pressing issues that impact the sector are: legacy debts; Aggregate Technical and Commercial Collection (ACT & C) losses; liquidity constraints; infrastructural challenges; metering; and economic realities of Nigeria.

Legacy debts

It is no more news that legacy debts inherited by the successor entities pose a significant threat to the business of the players in the Nigerian power sector. Currently, the legacy debts owed to the DisCos, GenCos, Transmission Company of Nigeria (TCN), the bulk trader (Nigerian Bulk Electricity Trading Company) and feedstock suppliers run into trillions of naira therefore leading to significant revenue shortfall to the sector. Given that the primary source of revenue for the electricity market participants is the payment received from the consumers for electricity consumed, the inability of the DisCos to efficiently collect payments and the debts owe by the consumers over the years has consequently resulted in the huge debts owed to the sector. The Ministries, Departments and Agencies (MDAs) of government are the biggest legacy debtors to the power sector and efforts by the DisCos to recover these debts are yet to yield any visible results.

Aggregate Technical, Commercial and Collection (ACT & C)

Aggregate Technical Commercial and Collection (ACT & C) losses refer to the total losses arising from the difference between the amount of electricity received by a DisCo from the TCN and the amount of electricity for which the DisCo invoices its customers plus the adjusted collections loss. Technical losses occur naturally and consist mainly of power dissipation



in electricity system components such as transmission and distribution lines, transformers, and measurement systems[1]. While the Commercial and Collection losses result from the non-technical issues such as electricity theft, non-payment by customers, and errors in accounting and record-keeping by the power companies.

In Nigeria, the GenCos, TCN and DisCos record very high ATC & C losses due to their infrastructural inadequacies and other factors including the alarming rate of electricity theft, non-payment by customers and metering. Given the huge impact of these losses on the sector, the DisCos have been required by the Federal Government to submit ATC & C reduction plans with a view to allow for monitoring and ensuring that significant efforts are being made to reduce these losses to the barest minimum which would invariably pave way for improved profitability in the power sector.

Liquidity constraints

Liquidity remains one of the pressing issues facing the participants in the Nigerian power sector. The power sector liquidity crisis has primarily been attributed to the inability of the DisCos to settle the invoices issued by the bulk trader which consequently results in revenue shortfalls for NBET, TCN and the GenCos in the value chain. This challenge has led the Federal government to introduce various initiatives such as the 'Power Assurance Guarantee' (PAG) (for the NBET to guarantee payment for the evacuation of electricity produced by the GenCos to the national grid who will in turn be able to pay gas suppliers) and Nigerian Electricity

1 http://siteresources.worldbank.org/EXTESC/Resources/Background_paper_Reducing_losses_in_the_power_sector.pdf

Market Stabilisation Facility (NEMSF) through the Central Bank of Nigeria (CBN) as palliative measures to address the liquidity challenges in the sector. This liquidity crisis has also severely affected the ability of the power companies to attract financing required for projects which would improve the productivity of the sector.

Metering

The failure of the DisCos to provide meters for the electricity consumers across the country is another key issue that directly impacts their ability to collect payments for electricity consumed by consumers which consequently leads to significant revenue shortfall. The practice of estimated billing (inherited from the era of the defunct PHCN and NEPA) has entrenched a culture of non-payment of electricity bills by most consumers across Nigeria. This practice is widely perceived by consumers of electricity as exploitative given that there were no clearly-defined parameters for measurement of electricity consumed by consumers. There have been reported cases where some DisCos delivered electricity bills to consumers despite not supplying electricity for the period covered by

the bill. The continuation of such practice is completely unacceptable at this period and age in any market.

In 2013, NERC introduced a Credit Advance Payment for Metering Implementation (CAPMI) which was a willing-customer financing scheme initiated which allows electricity consumers who are yet to be metered by the DisCos to finance the procurement of their meter and be repaid over time through deductions from their monthly bills. However, some bottlenecks identified with the scheme forced the NERC to suspend the scheme as it failed to address the issue of metering gap across the sector. In another bid to address the metering gap, NERC recently introduced the Meter Asset Provider (MAP) Regulation 2018, which introduces meter asset providers as a new set of service providers in Nigeria Electricity Supply Industry. The MAP regulation provides for the third-party financing of meters, under a Permit issued by the Commission, and amortization over a period of 10 years. The electricity distribution companies, in line with their licensing terms and conditions, are obliged to achieve their metering targets as set by the Commission under this new regulation. The expectation is that this regulation would facilitate the closing of the metering gas given that the DisCos would no longer be responsible for the financing of the meters to be supplied to consumers.

Prevailing economic realities

The prevailing economic realities across Nigeria also go a long way in determining the impact of a CRT on the improvement of the electricity situation in Nigeria. Where we are today, a larger percentage of the rural dwellers may not be able to afford a CRT given their low purchasing power. It is therefore important to balance the agitations for a CRT with the realities of the Nigerian economy possibly by cost socialisation in the enforcement of it to achieve success across the country.

Conclusion

In the light of the foregoing, it may be argued that the absence of a cost reflective tariff cannot be a sustainable defence for the poor performance of the various DisCos post privatization. This issue is one in the long list of issues which militate against the productivity of the Nigerian power sector therefore the presupposition that the approval of a CRT may be the panacea to the challenges rocking the sector is not supportable. At best, the approval of a CRT may serve as a significant step in addressing the liquidity issue in the power sector.

For further information, questions and clarifications, please contact:

Taiwo Adeshina
Sector Head, Energy & Natural Resources.
taiwoadeshina@jacksonettiandedu.com