



The Nigerian Electricity
Regulatory Commission
*Issues Market Competition
Report 2022*

INTRODUCTION

Overtime, the Nigerian Electric Supply Industry (NESI) is expected to progress through four stages, which is to be determined by the extent of competition in the market.¹ In accordance with the provisions of the law, the Nigerian Electricity Regulatory Commission (NERC) makes the determination of the degree to which the market has progressed competitively.²

In principle, the application of the rules of vertical and horizontal unbundling, the introduction of consumer choice, the liquidity of trading (whether by contract or on the spot), the application of rules on third-party access to networks, and the extent of privatization in the market should all be taken into consideration when deciding the degree of competition in the market.³

On 3rd October 2023, NERC released its Market Competition Report for 2022 (the **Report**). Even though this Report was issued after the enactment of the Electricity Act 2023 (EA), it was nonetheless, released further to the provisions of the Electric Power Sector Reform Act 2005 (EPSRA). It is important to spotlight this issue at the outset as the question of who declares a more competitive market under the EPSRA on the one hand and the EA on the other hand, produces different answers.

In this newsletter, we will examine the contents of the Report in detail, provide a comparative analysis of the EPSRA and the EA on the issue, and share our insights on what to expect in the market in foreseeable future.



STAGES OF THE NIGERIAN ELECTRICITY MARKET

Statutorily, the NESI is expected to progress through four stages:

1. *Pre-Transitional Electricity Market*

This stage officially commenced with the privatization of the NESI through the sale of the successor generation companies (**GenCos**) and the divestment of 60% majority stake in the distribution companies (**DisCos**) in 2013.⁴

2. *Transitional Electricity Market*

This stage officially commenced on the 1st of February 2015 following a declaration by NERC.⁵ At this time, two important questions were raised regarding the market: (a) whether NERC in fact, and not the Minister of Power, could declare the Transitional Electricity Market? and (b) whether the Conditions Precedents prescribed in the Market Rules had been satisfied for the declaration of the Transitional Electricity Market?

1. The four stages as identified below include: pre-transition, transitional, medium-term, and final.
 2. See: section 24(2) EPSRA and section 8(1) of the EA.
 3. IEA/OECD, *Competition in Electricity Markets* (OECD Publishing, 2001) 1-165
 4. Report p. 9
 5. Report p. 9

3. **Medium Term Market**

During this stage of the market, while electricity transmission and distribution will remain regulated, the contract market in electricity generation will be partly regulated (with NERC setting the wholesale market rates), and partly unregulated. At this stage of the market, a balancing mechanism (spot market) which deals with imbalances between the metered and contracted quantities of energy, will be introduced.⁶

4. **Long-Term Electricity Market**

At this stage of the market, both the generation and retail (billing, metering, and collection- now bundled into electricity distribution), aspects of the electricity value chain will be unregulated. Transmission and distribution will remain regulated, being natural monopolies.⁷

DECLARATION OF A MORE COMPETITIVE ELECTRICITY MARKET

In accordance with the provisions of the repealed EPSRA and the EA, NERC is mandated to issue a yearly report on the extent of competition in the NESI. Even though NERC issues the yearly reports, there are important dissimilarities between the EPSRA and the EA on the appropriate authority to declare a more competitive market.

1. **Declaration under the EPSRA**

NERC is statutorily required to issue yearly reports on the degree or extent to which competition has occurred in the NESI. NERC was required to issue these reports to the Minister of Power in accordance with section 24(2) EPSRA, who was in turn, to present the reports to the President and the National Council on Privatization and National Assembly.

The Minister, in consultation with the President and the National Council on Privatization, makes the declaration of a more competitive electricity market if satisfied that the electricity market has developed to the point where a more competitive market ought to be established.⁸

In connection with this, the Report issued further to section 24(2) EPSRA, “offer(s) regulatory guidance to the Federal Government of Nigeria (“FGN”) towards a possible declaration of a more competitive market”⁹ while also providing a review of the level of competition in the NESI and an assessment of the progress for a transition to a more competitive market.¹⁰

2. **Declaration under the EA**

In accordance with section 8(1) of the EA, NERC, and not the Minister of Power is to make the declaration of a more competitive market going forward. All that NERC is mandated to do is present yearly reports on the state of the NESI to the President and the National Assembly, and then consult with the Minister before making the declaration.

6. See: NERC, “Nigerian Electricity Market” <https://nerc.gov.ng/index.php/home/operators/ltmr/405-nigerian-electricity-market>. See also clause 3.1 Definition of “Balancing Market” in Market Rules 2014

7. *Ibid*

8. See section 24(3) EPSRA

9. See: Report p.8

10. *Ibid* at p. 8

Thus, the section provides that: *“The Commission shall present to the President and the National Assembly each report made under section 7 (2) (c) of this Act, and when the Commission, in consultation with the Minister is satisfied that the electricity market in Nigeria has developed to a point where a more competitive stage than the preceding market ought to be established, having regards to the satisfaction of the pre-conditions and such features as may be prescribed under the market rules, the Commission shall issue a declaration that such a market stage be commenced.”*

In our view, empowering NERC, while divesting the Minister of Power of the important regulatory function of declaring a more competitive electricity market depoliticizes the process. With this, the EA bypasses a pivotal hurdle, that is, the need for NERC to procure the concurrence of the Minister that a more competitive market is to be declared. It also guards against regulatory arbitrariness on the part of NERC in taking a step ahead of the Minister in declaring a competitive electricity market.



INDICES ON WHICH NERC SHOULD BASE ITS REPORT

The EA and EPSRA differ on the pre-conditions to be satisfied ahead of the declaration of a more competitive market. The indices for NERC’s determination and recommendation to the Minister of Power to declare a more competitive electricity market under EPSRA are:

1. The degree of privatization that has occurred in the market;
2. The existence of a sufficiently large number of potentially competitive entities, to avoid the likelihood of an abusive market power; and
3. The existence of other preconditions, including the necessary metering and information technology infrastructures, required for the operation of a more competitive electricity market.¹¹

On the other hand, and as seen above from section 8(1), the EA simply creates an evolving framework by requiring NERC to declare a later stage of the electricity market upon satisfaction of the pre-conditions and such features as may be prescribed under the market rules.¹²

Both arrangements have their pros and cons. The arrangement under EPSRA provides some level of certainty but does not cater for market evolution and future contingencies. By contrast, while the EA does provide for some fluidity by anticipating future market developments as may be prescribed in the market rules, it nevertheless does not provide much-needed certainty of criteria on which NERC should base its discretion on.

11. Section 24(2)

12. Section 8(1)


NERC'S DETERMINATION IN THE MARKET COMPETITION REPORT 2022

NERC has made recommendations on the extent of competition in the NESI to the Minister of Power in the Report, but first it makes several determinations in accordance with the criteria specified in section 24(2) of the EPSRA. These determinations are as follows:

1. The degree of privatization that has occurred in the market:


On this, NERC has determined that:

On this, NERC has determined that:

11  generation companies previously owned by the government have been privatized

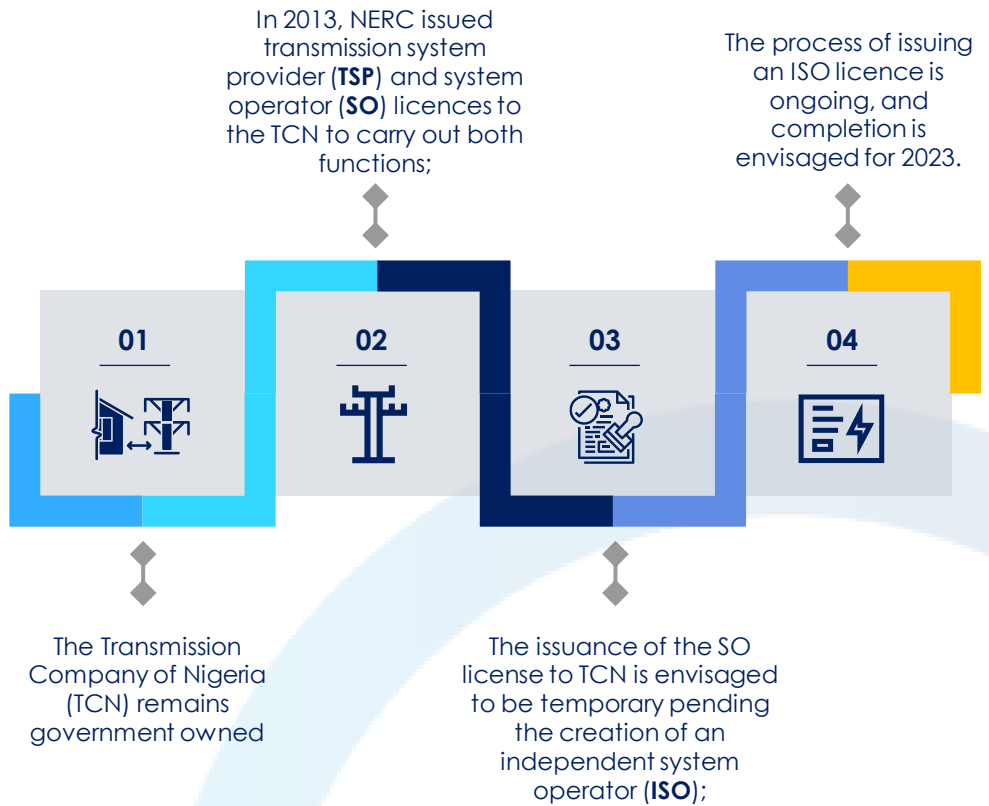
8  National Integrated Power Project (NIPP) power plants being managed by the Niger Delta Power Holding Companies Limited (NDPHC) are in the process of being privatized;

9  operational Independent Private Plants ("IPP") connected to the grid

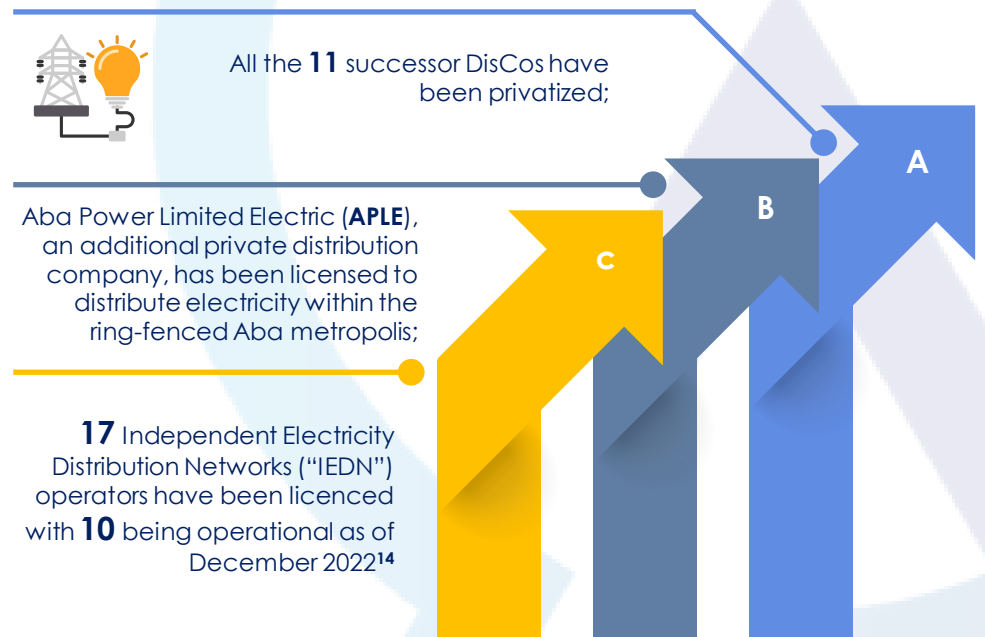
 Several off-grid and embedded generators have been licensed and currently operate in the NESI¹³



For electricity transmission



For electricity distribution



Based on the foregoing, NERC concludes that the NESI is sufficiently privatized.¹⁵

14. Ibid pp. 9, 34, 35

15. bid at p. 53

2. The existence of a sufficiently large number of potentially competitive entities, to avoid the likelihood of an abusive market power:

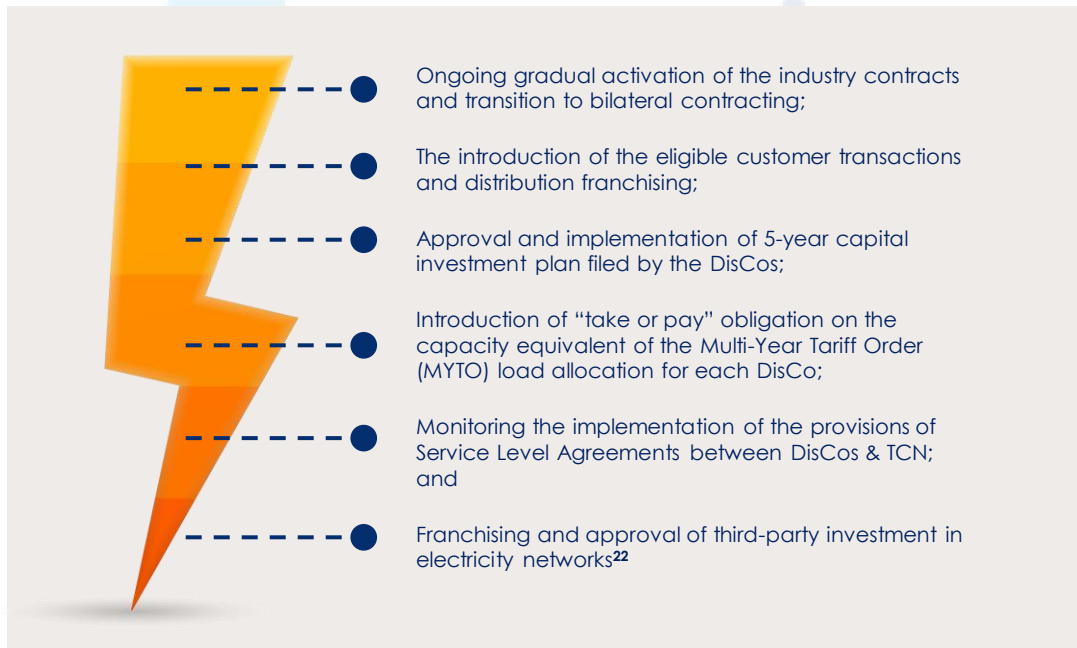
The important question here is to what extent are electricity generators diffused in the NESI and what is the opportunity for competition in other aspects of the electricity value chain?

According to the report, there are currently 28 grid-connected operational generation companies and 12 grid-connected distribution companies in the NESI showing a sufficiently large number of potentially competitive entities.¹⁶ Recent review indicates that at least three of the DisCos are creditworthy to contract directly with GenCos.¹⁷

Regarding the penetration of competition in electricity generation, compared with 2015 when electricity generation assets were handed over to private investors and December 2022, there has been an increase in the number of electricity generators¹⁸. There has also been an increase in average generation¹⁹, as well as an increase in generation capacity utilization²⁰.

Additionally, using the Herfindahl-Hirschman Index (HHI) for the level of market concentration in NESI, available capacity and actual generation is estimated to be less than 1,500 points (i.e., low concentration) indicating a substantial level of competition in electricity generation. More generation capacity is also expected to be available with the ongoing construction of additional power plants in the country.²¹

Besides, there are ongoing steps to increase generation capacity and utilization. These include:



- Ongoing gradual activation of the industry contracts and transition to bilateral contracting;
- The introduction of the eligible customer transactions and distribution franchising;
- Approval and implementation of 5-year capital investment plan filed by the DisCos;
- Introduction of "take or pay" obligation on the capacity equivalent of the Multi-Year Tariff Order (MYTO) load allocation for each DisCo;
- Monitoring the implementation of the provisions of Service Level Agreements between DisCos & TCN; and
- Franchising and approval of third-party investment in electricity networks²²

16. *Ibid* at p. 22

17. *Ibid* at p. 53

18. There are 28 actively participating on-grid electricity generators in NESI.

19. The 3,892MWh/h recorded in 2022 was 9.42% more than the daily average generation of 3,557MWh/h recorded in 2015.

20. Capacity utilization refers to a percentage representing the extent to which a generating unity fulfilled its capacity in generating electricity over a given period. In NESI, the capacity utilization rate rose by 40.31 percentage points from 55.57% in 2015 to 95.88% in 2022. See Market Competition Report 2022 p. 11,

21. Report pp. 10-12

22. *Ibid* at p. 12

3. Existence of Robust Metering and Information Technology Infrastructure

The important question to be determined here is the extent of metering at the wholesale and retail markets, and the use of information technology (IT) to achieve this. In this regard, NERC has determined that there has been a significant improvement in metering and IT infrastructure compared to 2013, and further implementation of necessary technology is still in progress, at various stages, in both the wholesale and retail markets based on the following:²³

A. Wholesale Market

According to NERC:



Grid metering has been largely achieved in the wholesale market as the Market Operator (MO) has completed installation of grid meters;

Even though the TCN has not fully deployed the Supervisory Control & Data Acquisition (SCADA) system for full coverage of the transmission system, TCN has deployed Internet of Things (IoT) and smart meters at GenCo-TCN interfaces for real-time reading of generation output;



DisCos have substantially installed smart meters on **33kV** and **11kV** feeders- as of December 2022, **94%** of **11kV** feeders and **96%** of **33kV** DisCo feeders have been metered;

The proposed unbundling of the SO from TSP/TCN will ensure that infrastructure necessary for System and Market Operation is given priority, for example SCADA, EMS and smart grid meters, System Telecoms, and the maintenance and upgrade of control rooms.²⁴



23. Ibid at p. 43

24. Ibid at p. 44 et seq

B. Retail Market

In the retail market:

01

As of 31st December 2022, Ikeja, Eko, Abuja and Benin DisCos had metered more than **50%** of their registered customers;

02

As of 31st December 2022, most of the DisCos had metered more than **82%** of their Maximum Demand (**MD**) customers;

03

In continuation of the efforts to intensify the roll-out of meters, NERC has issued the MAP and NMMP Regulations 2021 which provides a framework that allows for a smooth and concurrent implementation of both MAP and NMMP schemes to fast-track meters deployments;

04

In pursuit of mitigating the risk of financing outside the electricity market, NERC made provision for the establishment of a Meter Acquisition Fund in the December 2022 Tariff Order to support the deployment of end-user' meters.²⁵

Based on the foregoing and the CPs set out in clause 6.5.3 the Market Rules of a more competitive electricity market, which have substantially been met, in addition to all the Panels/Committees required as CPs for the commencement and operation of the Transitional Electricity Market and the evolution of a more competitive market in the NESI being currently operational, NERC has determined that *"the Nigerian electricity market has evolved substantially and the NESI is ripe for transition to a more competitive market."*²⁶



CONCLUSION AND RECOMMENDATIONS

NERC has made proposals for the Minister's consideration aimed at transitioning to the medium-term electricity market. We think this is by no means premature given the recent enactment of the EA and the potential for increased regulation, competition, and investments in the electricity sector. Quite remarkably, only three DisCos are creditworthy to engage in direct bilateral contracting with electricity generation companies. Following a declaration for the three DisCos to transition to direct contracting with GenCos, the role of the Nigerian Bulk Electricity Trading (**NBET**) will gradually be phased out. Achieving a competitive electricity market is often a phased and gradual process- in the main, certainty in the revenue stream of DisCos must be guaranteed through increased metering in the sector.

25. *Ibid* at pp.45-49

26. *Ibid* at p. 15

27. *Ibid* at p. 50

NERC's proposals to the Minister include:

-  Declaration for the creation of an ISO;
-  Clear policy on settlement of energy bills by host communities;
-  Accelerated implementation of government intervention on infrastructure programs being run by the Federal Government of Nigeria;
-  Engagement with the relevant ministers and other stakeholders in prioritizing Domestic Gas Supply Obligation to power;
-  Prioritization the development of Integrated Resource Plan;
-  Ministry of Power's compliance with regulations;
-  Fast-tracking the ongoing privatization of NIPPs.



We envisage that based on current market trends as determined by NERC on the extent of competition in the NESI, NERC may soon exercise its powers under section 8(1) of the EA to declare a more competitive electricity market.

For More Information, Please Contact :



Wolemi Esan
Deputy Managing Partner
wesan@ofaniwunajayi.net



Ibi Ogunbiyi
Partner
iogunbiyi@ofaniwunajayi.net



Chinenye Ajayi
Senior Associate & Team Lead
cajayi@ofaniwunajayi.net



Osamede Osasu
Associate
oosasu@ofaniwunajayi.net