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EXPLORING PUBLIC-PRIVATE PARTNERSHIPS (PPPS) AS A STRATEGIC FINANCE MODEL FOR POWER GENERATION INFRASTRUCTURE IN NIGERIA

INSIDE TOLG ADVISORS

INTRODUCTION

In July 1924, in *The Atlantic* article “Life as We Know It” by Arthur D. Little, tried to predict the future. When he stated; that the rate of a nation’s economic progress is primarily a function of the abundance and cost of energy on one hand and the preparation and use of fuels. Energy generation is a basic industrial activity, which, in one way or another, vitally concerns us all, as progress will continue only if the energy that powers keep pace with the ever-changing nature of mankind.

This infrastructure deficit persists and has become more pronounced. The issue is not just about the availability of energy but also about the outdated and insufficient infrastructure that supports its generation and utilization. Much of the current infrastructure in Nigeria was built for outdated energy needs and is now inadequate to handle the current modern demands. Such deficits include ageing power grids, inefficient transmission lines, and insufficient storage capabilities.

Closing this infrastructure deficit demands significant investment and innovation, hence modernizing the energy grid, expanding renewable energy sources, and enhancing energy efficiency are vital steps toward narrowing the gap. Since the government may not have sufficient resources either due to budgetary limitations or limited financing, private collaboration and investment are crucial to aiding governments in constructing the infrastructure necessary to meet energy demands sustainably and resiliently.

Public-Private Partnerships (PPPs) as one of the modes of public financing presents a viable solution to address the persistent power generation challenges in Nigeria. In the context of a rapidly evolving global landscape, where burgeoning populations and escalating demands exert pressure on existing infrastructure, PPPs offer a strategic approach to bolstering economic progress and societal development by leveraging on the strengths of both public and private sectors. PPPs facilitate the creation of a robust infrastructure network, with a particular emphasis on ensuring reliable and accessible electricity. This collaborative model not only addresses the immediate need for increased power generation but also catalyzes advancements across various sectors critical to human welfare.

OVERVIEW OF THE NIGERIAN POWER GENERATION INFRASTRUCTURE

Electric Power (EP) is derived from a multitude of energy sources, each with its unique form, including; fossil fuels such as oil, coal, and natural gas, renewable sources like sunlight, wind, hydro, geothermal, and biomass, as well as nuclear energy through nuclear fission and fusion processes. Additionally, alternative energy sources like hydrogen and tidal waves contribute to the diverse mix. The process of converting energy available in various natural forms into electrical energy is commonly referred to as the generation of Electrical Power.

Regulatory Developments

In 2023, the Nigerian Electric Supply Industry (NESI) witnessed significant legal milestones due to constitutional amendments, enabling states to establish their electricity markets. This Act repealed the EPSRA (2005), introducing policies to propel the NESI into another post-privatization phase, providing a framework for energy transition. The Electricity Act specifies that once a state establishes its electricity market, the Nigerian Electricity Regulatory Commission (NERC) will no longer regulate electricity within that state.

In early January 2024, NERC issued the new *Mini Grid Regulations*, signed on December 29, 2023, which replaced the 2016 regulations. These regulations target mini-grids with generating capacities of up to 1MW per site. Mini-grid developers focusing on isolated systems with distributed power not exceeding 100kW can apply for a mini-grid permit under these regulations.

In the latest Multi-Year Tariff Order (MYTO) released by NERC in January 17, 2024, DisCos are now allowed to procure electricity directly from Generation Companies (GenCos), a significant shift from the previous system where the Nigerian Bulk Electricity Trader Plc (NBET) acted as an intermediary. The success of these bilateral agreements will depend on the creditworthiness of the DisCos and the implementation of cost-reflective tariffs to ensure commercially viable returns.

PUBLIC-PRIVATE PARTNERSHIPS (PPPs)

Nigeria operates a federal system of government having a central government and thirty – six states unit with a Federal Capital Territory. All of these federating units are entrusted by law and its citizens as provided by Chapter 2 of the Constitution of the Federal Republic of Nigeria, to make laws for “*the security and welfare of the people*”. To ensure the welfare of these citizens, there must be adequate provision of infrastructure by the government.

Governments are entrusted by their respective legal frameworks to provide essential infrastructure for their citizens, ensuring the fundamental needs of the populace are met. However, due to financial constraints and

budgetary limitations, there often exists a significant deficit in the availability and quality of such infrastructure. To bridge this gap, governments frequently turn to the private sector, inviting private entities to fund, develop, and maintain infrastructure projects.

This collaboration, known as Public-Private Partnerships (PPP), allows the private sector to invest in public infrastructure for profit, thus addressing the infrastructure deficit while fostering economic growth and enhancing public services.

What are PPPs?

There is no universal definition of PPPs, however, it usually presents a framework where the tasks, obligations, and risks for the provision of social infrastructure are transferred from the government to private individuals through a concession arrangement. PPPs may refer to informal and short-term engagements of nongovernmental organizations, the private sector and/or government agencies that join forces for a shared objective: to more formal, but still short-term private sector engagements for the provision of specific services, for example, annual outsourcing arrangements for janitorial services for a school or operations of the school cafeteria; to more complex contractual arrangements, such as build, operate, transfer regimes, where the private sector takes on considerable risk and remains engaged long term; or to full privatizations.

The International Monetary Fund defines PPPs as

An arrangement where the private sector supplies assets and services that traditionally have been provided by the government. In addition to private execution and financing of public investment, PPPs have two other important characteristics: there is an emphasis on service provision, as well as investment, by the private sector; and significant risk is transferred from the government to the private sector.

The Infrastructure Concession Regulatory Commission (Establishment) Act, 2005, states:

As from the commencement of this Act, any Federal Government Ministry, Agency, Corporation or body involved in the financing, construction, operation or maintenance of infrastructure, by whatever name called, may enter into a contract with or grant a concession to any duly pre-qualified project proponent in the private sector for the financing, construction, operation or maintenance of any infrastructure that is financially viable or any development facility of the Federal Government in accordance with the provisions of this Act.

Subsection 2 of the same section further provides that:

This Act applies to investment and development projects relating to any infrastructure of any Federal Government Ministry, Agency, Corporation or body.

The Lagos State Public-Private Partnership Law defines a Concession Agreement as follows:

“means any agreement between the Government and any person, firm, company or limited liability partnership for the construction, maintenance, operation or management of public infrastructure, assets and facilities over an agreed period including, but not limited to, the following types of agreements— (i) Design, Build, Operate and Transfer (DBOT), (ii) Build, Own, Operate and Transfer (BOOT), (iii) Rehabilitate, Operate and Transfer (ROT), (iv) Joint Development Agreement (JDA), or (v) Operation and Maintenance (OM)”.

Types of PPPs

There are different models or types of PPPs, these are primarily distinguished by two factors namely; the degree of risk allocation between the public and private sectors, associated investment levels and the length of the contract period.

The basic PPP contract types are: Service Contracts; Management Contracts; Affermage or Lease Contract PPPs; Concession Contract PPPs; Build–Operate–Transfer (BOT) and similar arrangements; and Joint Venture

LEGAL, REGULATORY AND INSTITUTIONAL FRAMEWORK FOR PPPs IN NIGERIA

The responsibility of establishing these legal and institutional PPP frameworks rests with governments. They must be capable of identifying and selecting suitable projects, conducting transparent tenders, structuring robust contracts, and implementing checks to ensure the proper execution of PPP projects. However, this is not quite the case as the PPP in Nigeria, especially with the federating units is not quite developed.

At the federal level, the relevant laws, regulations and policies are as follows: Infrastructure Concession Regulatory Commission (Establishment, Etc.) Act, 2005; the National Policy on Public Private Partnership 2008; Public Private Partnership Manual of the Infrastructure Concession Regulatory Commission 2012; The Unsolicited Proposals Guidelines issued by the ICRC; Public Procurement Act 2007; Public Procurement (Goods and Works) Regulations 2007 and Public Procurement (Consultancy Services) Regulations 2007; Public Procurement Procedure Manual 2011 (issued by the Bureau of Public Procurement, January 2011); The Public Procurement Act 2007; The Fiscal Responsibility Act 2007; The Debt Management Office Act 2003; The Electric Power Sector Reforms Act (EPSRA) 2005; Renewable Energy Master Plan (REMP) 2005; and the Public Enterprises (Privatization and Commercialization) Act 1998.

At the state level, it has been noted that the development of Public-Private Partnership (PPP) laws is still in its early stages, and in some instances, nonexistent, also only a handful of states in Nigeria such as Lagos, Rivers and Ekiti have formulated legislation specifically addressing PPPs. It is suggested that the constitutional principle stipulating that "federal law prevails where state law is silent" be applied to address this gap.

The NDPA marks a significant milestone in safeguarding personal data privacy within the country. Part V of the Act delves into the core principles and lawful bases governing the processing of personal data.

CASE STUDY OF SUCCESSFUL PUBLIC-PRIVATE PARTNERSHIP MODELS IN NIGERIA

Public-Private Partnerships (PPPs) enable governments to commence and deliver public infrastructure/services by leveraging the resources and expertise of the private sector, through risk-sharing arrangements. The private sector can also infuse and spur innovation, as seen mainly in major parts of Europe, Latin and Central America and illustrated by the Finnish Digital Cluster PPP ecosystem (DIMECC). Some of these PPP projects have been able to ameliorate the sufferings of its citizens in these countries, a quick survey of these projects will show that the public and private sectors needed to come together to ensure these projects are actualized. Some of these PPP projects are outlined below:

Burkina Faso

FasoBiogaz is a flagship and pioneering project for Burkina Faso. FasoBiogaz SARL is an enterprise located in the industrial zone of Kossodo in Ouagadougou, Burkina Faso, and operates the first industrial biogas plant connected to the SONABEL power grid. With an installed electrical capacity of 275 kW, the plant is transforming slaughterhouse waste and other available organic substrates into biogas and digest. While biogas is transformed into electricity and injected into the national power grid, the digest is commercialized as a biofertilizer. The project is financed by the Dutch private investor company Van Kersbergen Invest B.V. The initial investment amounts to 1,500,000 EUR for the implementation of a plant with an installed capacity of 500 kW. Operating revenues are generated through the sale of electricity and digest as biofertilizers. In 2015, FasoBiogaz was able to negotiate a Power Purchase Agreement (PPA) with SONABEL with a desirable tariff for 3 years. With a currently installed power of 275 kW, the plant can daily inject between 4,200 and 4,300 kWh into the grid.

Cameroon

Dibamba Power Plant, Multilateral Development Banks' Collaboration, Infrastructure Investment Project Briefs, World Bank April 2016, 2009 the Government of Cameroon awarded AES Dibamba Power Development Corporation (DPDC) the right to develop an 86-MW thermal energy Independent Power Plant (IPP). The Dibamba Project provides Cameroon with peaking and reserve capacity in electricity generation, to meet the growing public sector and industrial electricity demand.

Nigeria

Nigeria prides itself as the giant and is not left out in the drive towards PPP projects and there have been a few successful PPP projects, especially in the power sector.

• Azura Edo Power Plant

Azura-Edo is an independent power producer (IPP) committed to contributing to the growth of the energy sector in Nigeria. The power station is located in the ancient city of Benin which is the capital of Edo State. The plant is designed to help close Nigeria's > 10, 000 MW energy gap, whilst paving the way to a sustainable energy mix by providing grid stability and black start capabilities. The power station is owned by Azura

Power Holdings, an investment holding company for independent power projects in Africa. The majority equity investor in Azura Power Holdings is Actis Capital, a private equity firm headquartered in London with US\$7.8 billion under management. The minority equity investors in the plant include Africa50, a pan-African infrastructure investment platform, Anergi Group, an energy company active in Africa's emerging economies, Amaya Capital, an investment firm with a focus on the infrastructure sector in Africa and the Edo State Government, which holds a 2.5 per cent equity stake in the plant. The power station cost US\$900 million to build. The financing was obtained from fifteen financial institutions, in nine countries. It is also important to note that the International Bank for Reconstruction and Development (IBRD) provided partial risk guarantees; while the Multilateral Investment Guarantee Agency (MIGA) provided political risk insurance. Both IBRD and MIGA are members of the World Bank Group.

CHALLENGES FACING PUBLIC-PRIVATE PARTNERSHIPS IN NIGERIA

The development of Public-Private Partnerships (PPPs) projects in Nigeria has been unsatisfactory, taking into consideration the dire need for the sort of infrastructural projects that PPPs are so well suited to. This snail-paced growth is worrying, not only because of how much Nigeria stands to benefit from PPPs, but also in comparison to the rate of growth in other emerging economies of which Nigeria is projected to be one. PPP modules can be applied to increase growth in almost every sector of the economy, including education, transportation, health, communication, power, agriculture, and even human resource training. Therefore, it becomes crucial to identify and assess the barriers to PPP project implementation in Nigeria. This will enable the government at all levels and other stakeholders, particularly potential local and foreign private investors to recognize significant barriers in the implementation of PPP projects in Nigeria.

There are several challenges facing PPP development in Nigeria some of these challenges stem from a political clog or as the case may be a regulatory clog. These challenges are elucidated below, amongst others:

Project Financing Issues

One major snag to the success of PPPs in Nigeria is the scarce availability of long-term funding and this can be linked to the unavailability of a developed capital market, making it difficult to raise much-needed finance for projects. Instead, the limited funds that have been used for the financing of PPP projects have been short-term funding from local banks bearing high interest rates and often time onerous repayment terms.

Participation of development financial institutions such as; the World Bank and African Development Bank have come through in providing long-term funding, which in turn encourages private investors. Thus, the capacity and credibility of the government to secure and retain the involvement/participation of such institutions in PPPs is a key element to ensuring their success. Of course, like all private sector ventures, projects must be found to be viable, through asset-liability matching, inflation-linked returns, and lower risk profiles compared to equities.

Inadequate Public Acceptance

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Inadequate Public Acceptance

Another significant drawback that PPPs face the world over, and prevalently in Nigeria is widespread acceptability by the public. With the prevalence of corruption, taxpayers already feel short-changed by the government and do not understand why they should pay for services within the purview of the government's obligations. For PPPs to be more readily acceptable, the government must be seen to be transparent and educate the public on the PPP transaction structures. It will be the job of these agencies to enlighten and sensitize the public to the needs and benefits of projects, as well as to provide avenues for addressing public complaints. The Lekki Expressway concession is a typical example of such conflict where the Lagos State Government failed to appreciate the importance of carrying the public along when planning an otherwise good project.

STRATEGIC FRAMEWORK FOR IMPLEMENTING PUBLIC-PRIVATE PARTNERSHIPS (PPPs) IN THE POWER GENERATION SECTOR IN NIGERIA

Within the context of significant infrastructure deficits and fiscal limitations, PPPs emerge as a promising avenue for leveraging private sector expertise, capital, and innovation to complement public sector endeavours. These partnerships hold the potential to bolster power generation capacity, elevate service reliability, and facilitate broader energy accessibility throughout the nation. The strategic framework for PPPs in the power generation sector is characterized by its comprehensive nature, encompassing policy formulation, regulatory enhancements, institutional capacity building, and active stakeholder engagement. This holistic approach aims to establish a conducive environment for fostering successful PPP ventures that address critical energy needs while ensuring sustainability and resilience.

Below is a strategic framework to effectively implement PPPs in Nigeria's power generation sector:

Establish a National Power Sector PPP Policy;

The Electricity Act has been amended to now permit states to generate, transmit, and distribute electricity. Consequently, this development is expected to foster Public-Private Partnerships (PPP), which can enhance efficiency, drive innovation, and attract investments in the energy sector at the state level. By leveraging PPP models, states can potentially improve their electricity supply, reduce aggregate transmission and distribution losses, and ensure more reliable and sustainable energy for their citizens.

However, this innovation is not without its challenges. States will need to carefully navigate a range of issues, including; regulatory and compliance complexities, investment and financing, capacity Building, coordination and integration. Addressing these issues will be critical to maximizing the benefits of this legislative change and ensuring its success in improving the power sector at the state level.

Institutional Strengthening;

Establish and empower PPP units within state ministries to act as focal points for power generation PPPs and facilitate coordination between relevant government agencies and where need be, the Federal Government.

Funding and Financial Structuring;

Leverage various financing mechanisms such as green bonds, climate finance, and concessional loans to fund power generation projects. Use guarantees, political risk insurance, and liquidity support facilities to enhance the bankability of PPP projects and encourage the involvement of domestic financial institutions and pension funds in financing power generation projects.

Technology and Innovation;

Promote projects that include the integration of smart grid technologies to enhance the efficiency and reliability of power distribution and prioritize PPP projects that incorporate renewable energy sources such as solar, wind, and hydro to diversify the energy mix and promote sustainability.

INNOVATIVE PPP FINANCING MODELS AND MECHANISMS IN THE POWER GENERATION SECTOR

PPPs have become essential for developing and financing power generation projects. Here's an analysis of various innovative PPP financing models and mechanisms that can be particularly effective in the power generation sector:

Loan Syndication

A syndicated loan represents a collaborative debt arrangement involving two or more lenders extending funds to a borrower, blending aspects of private and public debt. In this setup, the lead arranger or lead bank serves pivotal roles: (i) directly engaging with and evaluating borrowers in a relationship-oriented manner, (ii) retaining a significant portion of the loan, (iii) holding authority for renegotiations or modifications concerning crucial loan aspects like principal, interest, maturity, and collateral, and (iv) subsequently dispersing a portion or the entirety of the loan to other lenders (participant lenders) within a capital market framework. The lead arranger also earns an arranger's fee for orchestrating the transaction.

Many public-private partnership (PPP) initiatives establish a special purpose vehicle (SPV), often referred to as (the "Project Company") entrusted with executing the project, and with its shares held in trust for the lenders. The SPV typically assumes the borrower's role and shoulders the project's legal and financial responsibilities.

Hybrid Annuity Model

Under the Hybrid Annuity Model (the "HAM") framework, the government (usually represented by a relevant authority or agency) awards a project to a private entity through a competitive bidding process. The private entity, often referred to as the concessionaire, is responsible for designing, building, and financing the project.

Unlike traditional BOT models where the private sector assumes most of the project risks, in HAM, the government provides a fixed annual payment to the concessionaire throughout the concession period, typically spanning 15-20 years.

Capital Markets

By leveraging capital market financing, PPPs in power generation can access a diverse pool of investors, optimize capital structure, and enhance project feasibility and sustainability. However, effective structuring, risk management, and alignment with investor preferences are essential for successful capital market transactions in PPPs. Here's how capital market financing can be utilized in PPPs for power generation:

Bond Issuance: Power generation entities can issue bonds in the capital markets to raise debt financing. These bonds may be structured as project bonds, where repayment is primarily sourced from project cash flows, or as corporate bonds backed by the project company's balance sheet. Bond issuances allow PPPs to access long-term financing at fixed or variable interest rates, depending on market conditions and investor demand.

Equity Offerings: Capital markets provide a platform for private entities to raise equity capital through initial public offerings (IPOs) or secondary offerings. Publicly traded power generation companies can attract equity investors seeking exposure to the sector's potential returns. Equity offerings enable PPPs to raise funds for project development, expansion, or refinancing, while also enhancing liquidity and visibility in the market.

Infrastructure Investment Funds: Infrastructure investment funds, including infrastructure-focused mutual funds, exchange-traded funds (ETFs), and private equity funds, offer investors diversified exposure to power generation projects and other infrastructure assets. PPPs can partner with these funds to access capital for project financing, with investors benefiting from stable cash flows and potential capital appreciation over the project's lifecycle.

Green Bonds: With increasing emphasis on sustainability and renewable energy, PPPs in power generation can issue green bonds to finance environmentally friendly projects. Green bonds are specifically earmarked for investments in renewable energy, energy efficiency, or other environmentally sustainable initiatives. These bonds appeal to socially responsible investors and may offer pricing advantages, reflecting investor preferences for green investments.

Securitization: PPPs can securitize future revenue streams from power generation projects by issuing asset-backed securities (ABS) or collateralized debt obligations (CDOs) in the capital markets. Securitization allows PPPs to monetize future cash flows upfront, providing immediate funding for project development or expansion while transferring investment risk to bondholders or institutional investors.

CONCLUSION

The power generation sector in Nigeria is currently at a critical point in its proposed advancement, it is however faced with the formidable task of meeting escalating energy demands which threatens to further cripple the energy accessibility of the majority of the population while simultaneously modernizing its infrastructure to drive the desired economic advancement. By way of seeking to mitigate against the pressing challenges, there has been a perceivable shift towards leveraging Public-Private Partnerships (PPPs) as a strategic tool for driving the desired change in the sector. However, despite the global establishment of public procurement regulations, the development of modern and secure legal, regulatory, and institutional Public-Private Partnership (PPP) frameworks to facilitate private investments in infrastructure in Nigeria has not progressed as expected and there continues to be a disparity. The onus of establishing these legal and institutional PPP frameworks rests with the government. They must be capable of identifying and selecting suitable projects, conducting transparent tenders, structuring robust contracts, and ensuring that the necessary checks and balances are in place to ensure the proper execution of PPP projects. However, this is not the current state of things for the PPP in Nigeria, at the state level, it has been noted that the development of Public-Private Partnership (PPP) laws is still in its early stages, and in some instances, nonexistent, also only a handful of states in Nigeria have formulated legislation specifically addressing PPPs. It is suggested that the constitutional principle stipulating that "federal law prevails where state law is silent" be applied to address this gap and bring the needed succour.



Vittas Nigeria International Limited's Series 1 Private Note Issuance Exercise

TOLG Advisors is pleased to announce our role as Transaction Counsel in connection with the N352,265,549.43 Series 1 Private Note Issuance Exercise under the N10bn Private Note Issuance Programme of Vittas Nigeria International Limited.

We are proud to be one of the few law firms in Nigeria to advise on such significant transactions in the fintech space in 2024.

Congratulations to our Advisory Team.



TOLG Knowledge Sharing Session and Ask Me Series with MO

The Firm hosted a fascinating and informative Knowing Sharing Session, which was moderated by our Global Chairman, Mr. Michael Orimobi. This presented an opportunity for the staff to enhance their proficiency in their respective areas of practice.



TOLG Quarterly TGIF Hangout

In light of the Firm's dedication to its culture of Energy, Fun and Sophistication, a day was set out for staff to relax and have fun. This enabled staff to relax from previous work activities and strengthen their relationships with one another in a relaxed atmosphere.



Father's Day Celebration

In honour of the 2024 Father's Day, the Firm held an insightful and memorable Knowledge-Sharing and Team-Bonding event. The topic of discussion was "Work-Life Balance: Building a Functional Family Life in Nigeria". Furthermore, in the spirit of team bonding, the men shared Health and Skin care tips with one another.

This Article was written by the Energy, Power & Natural Resources, Infrastructure & Project Finance, and Real Estate Teams at TOLG Advisors.

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