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SBP ENERGY SECTOR UPDATE:

NBET: ORDER ON TRANSITION TO BILATERAL TRADING IN THE NIGERIAN ELECTRICITY SUPPLY INDUSTRY

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On July 26, 2024, Nigeria's electricity sector saw a significant change as the Nigerian Electricity Regulatory Commission (NERC) introduced a new *Order for the Transition to Bilateral Trading in the Nigerian Electricity Supply Industry (NESI)* (the "Order"). This order marks the end of the Nigerian Bulk Electricity Trading Company's (NBET) role as the sole electricity trader.

The Order hands over electricity trading responsibilities from NBET to various market participants, encouraging greater competition and market-driven pricing in the sector. This shift is expected to bring notable changes to the industry, which will influence everything from generation and transmission to distribution, and ultimately impacting the end-user.

WHAT WAS NBET'S ROLE AND WHAT LED TO THE ORDER?

The Nigerian Bulk Electricity Trading Company (NBET) was incorporated in 2010 and licensed by the Nigerian Electricity Regulatory Commission (NERC) as a bulk trader of electricity and ancillary services to power distribution companies (DisCos) in 2011. NBET was established as a creditworthy offtaker to act as an intermediary between the power generation companies (GenCos) and DisCos for the bulk procurement, sale and purchase of electricity. The Federal Government provided credit facilities to NBET enabling it to guarantee payments to GenCos for the electricity supplied, thereby ensuring a steady revenue stream for power generation and supporting the development of other bankable independent power projects. The license issued to NBET by NERC was for a period of 10 (ten) years from 2011 and was subsequently renewed in 2021 for an additional period of 3 (three) years. Since 2022, NERC has also granted trading licenses to ten (10) private companies that have expressed interest in bilateral energy trading with DisCos and qualified customers. Request for regulatory approval have also been made by DisCos, requesting for the ability to purchase electricity directly from GenCos or other trading licensees.

In light of the Electricity Act 2023 ("the Act"), Section 7(2) mandates a shift away from NBET's role in bulk electricity procurement. Under this provision, NBET is required to transfer its existing contractual rights and obligations to other licensees and is no longer permitted to enter into new contracts for the purchase and sale of electricity and ancillary services.

It is on this premise that the Order on the Transition to Bilateral Trading in the Nigeria electricity Supply Industry has been issued.

THE ORDER AND ITS OBJECTIVE

The Order is as follows:

1. NBET has been ordered to desist from entering into any new contract for the purchase and resale of electricity and ancillary services in NESI. Any contract in contravention of this order shall be treated as an infraction by NERC.

2. NBET shall continue to administer fully effective contracts with only the following 5 (five) GenCos:

   a. Azura Power West Africa Limited (APWAL)
   b. Omotosho Power Plc
   c. Olorunsogo Power Plc
   d. Nigerian Agip Oil Company Limited
   e. The Shell Petroleum Development Company of Nigeria Ltd

3. All other power plants with "take and pay", power purchase agreement's (PPAs) or interim energy sales agreements with NBET have been ordered to negotiate and contract with DisCos, on bilateral agreement basis, the current capacity contracted with NBET within 60 days from the commencement date of the Order.

4. The maximum capacity a DisCo can trade in the bilateral market ("bilaterally tradable energy" or "BTE") shall be the difference between its energy offtake as contained in the July 2024 MYTO Order and its share of the "NBET Firm Capacity".

5. There is hereby created an NBET Interim Pool which is made up of the gross residual capacity from all the GenCos that is not traded with DisCos and so traded to NBET on an interim agreement basis.

6. The following framework for dispatch and payment prioritisation has been established – while NBET is to be largely funded by the Power Sector Recovery Program (PSRP) Financing Plan and payment prioritisation shall be as follows:

   a. Bilaterally traded energy between DisCos and GenCos.
   b. Firm contracts of the NBET with 5 GenCos.
   c. NBET pool energy under interim "take & pay" framework PPAs.

OBJECTIVES

The objectives of the Order are as follows:

Steer the electricity market towards bilateral contracting for energy and capacity between generation and/or trading licensees with distribution licensees thereby reducing the Federal Government's fiscal exposure to market risks.

Promote a more competitive market structure as envisioned by the Act by redefining NBET's role as the sole bulk electricity trader in NESI.

Ensure an equal opportunity for all hydro and thermal GenCos with existing "take-and-pay" contracts with NBET to reduce their contracted capacities by trading directly with DisCos on a bilateral basis.

Transition the contractual framework for bulk energy trading in the NESI to "take-or-pay" contracts, thereby enhancing market certainty and discipline among participants.

NUANCES AND OPPORTUNITIES

Note: The current energy trading report with NBET shows that barely 8 out 28 GenCos trading with NBET have fully effective contracts backed by some form of payment guarantee, thus leading to significant operational challenges and debt for energy supplied. Thus, without adequate financial backing and clear-cut commercial terms driven by a "willing seller, willing buyer" methodology, and a "pay as you go" tariff structure tailored to the ability of the consumers to pay for power consumed, GenCos may still find it challenging to enforce bilateral contracts in case of default by off-takers.

1. Infrastructure and Technology: The transition to bilateral trading requires significant adjustments for both GenCos and DisCos, including the need to upgrade the metering infrastructure, grid modernisation and expansion, trading platforms, data management, etc.

2. Competitive Market and Boost in Private Investments: Bilateral trading in the NESI will potentially encourage competition among more GenCos and DisCos, which will in turn lead to better pricing and service quality. In addition, bilateral trading in the NESI creates a myriad of opportunities for private investors in the electricity market, including investments in power generation projects, renewable energy solutions projects, infrastructure upgrades, etc.

3. Reduced Fiscal Burden: A successful transition to bilateral trading could alleviate the financial strain on the government. By enabling market participants to engage directly in energy transacti]ons, the government can limit its exposure to market risks and reduce the need for substantial financial backing of electricity procurement. This shift allows the government to focus on regulatory oversight rather than acting as the primary financial intermediary. Consequently, the reduction in financial obligations can free up resources for other critical public services, fostering overall economic stability and promoting sustainable growth in the energy sector.
4. Regional Market Development: The decentralization of electricity trading can facilitate the development of regional power markets. States may engage in cross-border trading, optimizing resources and enhancing energy security.

CONCLUSION

The issuance of this Order is a timely and strategic move that aligns with the objectives of the Electricity Act 2023. As Nigeria revamps its electricity sector, this development holds significant promise for transforming the landscape of power generation and distribution. This Order shows a shift toward a more competitive market framework. By encouraging direct interactions between GenCos and DisCos, the Order is expected to enhance operational efficiency and reduce costs, ultimately benefiting consumers.

Also, the potential for increased private investment cannot be overstated. With a more market-oriented approach, investors are likely to find the sector more appealing, leading to an influx of capital that can support the development of infrastructure and innovative technologies. This is particularly critical in light of the Electricity Act, which facilitates state-level market participation, thereby broadening the investment base and encouraging a diverse range of stakeholders to directly engage in the power sector.

Ultimately, this development is not just a welcome change, it represents a significant step towards improving the financial viability of both GenCos and DisCos. By offering flexibility in contract negotiations and pricing, this Order can lead to more sustainable business models and foster a robust energy market that meets the demands of Nigeria's growing economy.

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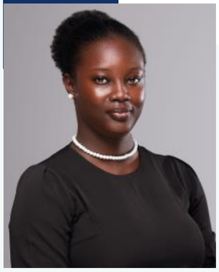

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