Vance Center Virtual Workshop
P3 Considerations in Nigeria

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KEY CONSIDERATIONS FOR SUCCESSFUL P3 PROJECTS

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Introduction

Approx. US$14 billion is required to be invested for a ten-year period to address Nigeria's infrastructure gap*

P3s are a widely recognised tool for encouraging private sector participation in public infrastructure projects, and drawing private sector funding, innovation and efficiencies to the delivery of public services.

*https://ppiaf.org/documents/3154/download

Key Considerations For Successful P3 Projects

1. Economic Viability
2. Appropriate Risk Allocation
3. Robust Community Engagement
4. Political Support and Enabling Legislation
5. Proper Private Partner Selection Process
6. Engaging the Right Advisers
7. Certainty of Project Scope
8. Sanctity of Contracts
9. Performance Assessment and Monitoring

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Economic Viability

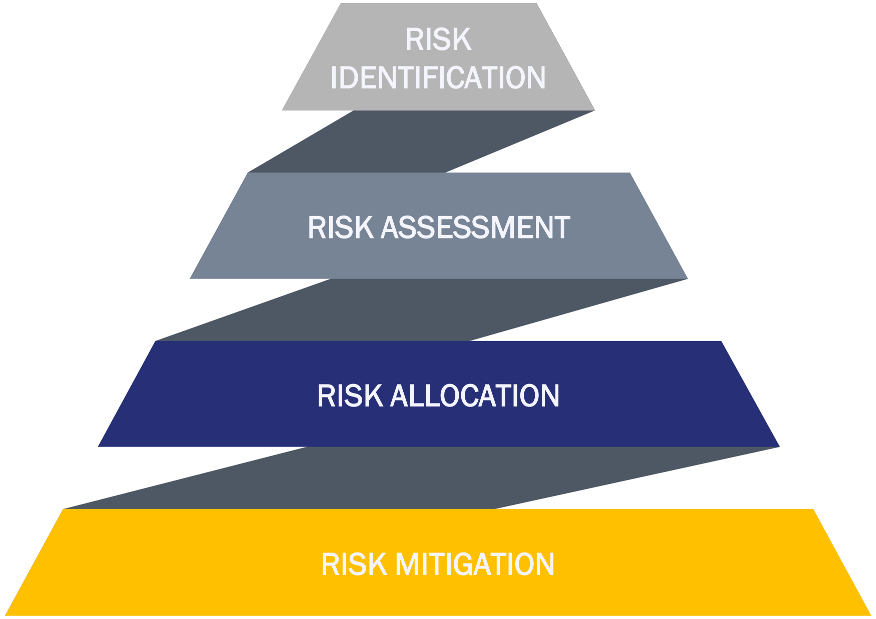
The Government Sponsor must independently determine whether the P3 project is economically viable both from ***its perspective*** and ***the perspective of its prospective private partner*** (and by extension, its lenders).

Why is it necessary to establish economic viability at the outset?

- critical in determining whether to proceed with a P3 project.
- useful in anticipating how the P3 project should be structured to achieve financial viability.
- useful in identifying key drivers of the private sector partner's/lenders') demands in negotiating the P3 contracts.
- Help identify the kinds of sponsor support that will be necessary to successfully execute the project.

Appropriate Risk Allocation

Risk is the possibility of an event occurring which would cause *actual project circumstances to vary from those assumed when projecting project benefits and costs* i.e., any factors that could result in an increase in costs or a decrease in revenues.



- Risk allocation takes on greater importance during the *project preparation stage (VfM analysis)* and at *negotiation of the P3 contracts*.
- Understanding how to assess and value risk factors and properly determining which party is best able to manage them is crucial to project structuring, bankability and ultimately, a P3 project's success.
- Risks should be allocated to the party best able to manage them or in relevant cases, the party that can control whether or not the risk materializes.
- P3 project risk categories (for a P3 project with design-build elements) – design risk, construction risk, force majeure, revenue risk, operations and maintenance risks, political risk, regulatory risk, macro-economic risks (currency risk, inflation etc.), strategic risks etc.

Robust Community Engagement

Community engagement is often overlooked by government sponsors in choosing to undertake infrastructure projects on a P3 basis; failure to do so can lead to the failure of P3 projects.

Why is community engagement necessary?

- helps in confirming or reassessing whether a project will deliver value to the community/its users.
- in determining how a project can be structured and designed to better serve the needs of its users.
- identifying locally available inputs necessary for the project.
- assessing how the project may impact life and economic activity in host communities negatively and figuring out how to manage these negative consequences.
- Government sponsor/private partner are better able to manage risks and mitigate potential disagreements with communities impacted by the relevant project.
- opens channels of communication between the government sponsor (and later the private partner) before issues arise later in the P3 lifecycle.

Robust Community Engagement

"[Community] engagement is an inexpensive and efficient way of creating a better operational environment for a project. The consultation process reduces risks and increases its chance(s) of success."

~ World Bank PPP Reference Guide*

Rationale? Helps avoid delays and extra costs during construction and operation while increasing the benefits for the communities served by the project.

A good example of proper community engagement for land acquisition is the integrated stakeholder engagement process adopted on the **Azura IPP Project** which led to the development of a Compensation Plan and a Resettlement Action Plan.

*https://pppknowledgelab.org/guide/sections/39-stakeholder-communication-and-engagement

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Robust Community Engagement

Community Engagement Principles

- Early engagement & outline the purpose of the engagement
- Identify the communities affected by a P3 project
- Develop a Community Engagement Plan
- Document everything
- Involve the private party in the engagement process as early as possible

<u>Other key points to note</u>:

- Performance Standards & Private Partner Obligations
- Two-Way Engagement
- Bankability
- Flexibility & Transparency

Robust Community Engagement

Festac Phase II Housing Development Project Concession – Federal Ministry of Lands, Housing and Urban Development/The Federal Housing Authority (FHA) and New Festac Property Development Company Ltd.

A 30-year concession granted to the Concessionaire in 2014 for the development of a 1.126 ha of swampy land located at FESTAC Town into a national mass housing project.

The land was acquired over 40 years ago by the FGN but was left undeveloped, save for the portion developed for the Festac Phase I Housing Estate.

There is ongoing dispute between the FHA and the Amuwo community on whether the project land was properly acquired the FHA.

The Amuwo community instituted an action against the FHA claiming that about 4.017 hectares of the project land belongs to the Amuwo community and was not properly acquired by the FHA.

The development of the project is currently stalled as a result of the ongoing court dispute.

The Court of Appeal held that the project land was properly acquired by the Federal Government, due compensation was paid, a proper survey of the land as well as necessary demarcation carried out, amongst others.

The Infrastructure Concession Regulatory Commission (ICRC) is discussing with the parties on ways of resolving the land ownership dispute with the local community.

Political Support and Enabling Legislation

- **Political Support** - the support of all relevant Government-side stakeholders over the life of a P3 project is critical to its success.

- Such stakeholders include the government sponsor <u>*and also other relevant MDAs and even opposition political parties*</u>. **Consider the Azura-Edo IPP Project.**

- **Political Support** extends to relevant government entities refraining from interfering with the execution of a P3 project and deviating from the terms of an executed P3 contract. **Consider Lekki Toll Road and Enron IPP examples.**

- **Enabling Legislation** – a clear legal and regulatory framework is critical for attracting private partners.

Query –

- interplay between general P3 legislation, procurement legislation and relevant subject-matter legislation;
- public revenue issues;
- prohibition of certain forms of government support in some state P3 legislation; and
- validity of unsolicited proposals.

Misalignment between the four-year election cycle and the typical over-fifteen-year lifecycle of P3 projects.

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Political Support and Enabling Legislation –
The Azura IPP Project

The project involved the design, financing, construction, commissioning, operation and maintenance of a 450MW gas-fired plant by Azura Power West Africa Limited.

First fully privately financed independent gas-fired independent power project, and first to receive the World Bank Partial Risk Guarantee and a PRI from the Multilateral Investment Guarantee Agency.

The project's success is attributed to the collaboration of the private partner, a State Government, the Ministry of Finance, Nigeria Bulk Electricity Trading Company Plc, the Debt Management Bureau and the Federal Ministry of Power - all of whom had the political will to see the project through.

The foregoing is evidenced by the government's willingness to execute contracts with novel structures for the Nigerian market, such as the Put/Call Option Agreement etc.

Proper Private Partner Selection Process

- **Compliance with Applicable Law -** selection of the private sector partner should be in line with the process prescribed by applicable P3 legislation and relevant conditions and requirements of applicable law must be complied with

- **Fair and Transparent Process -** a fair chance that a prospective private partner's investment in putting together a P3 proposal will be successful.

- **Bankability** - Ensuring that applicable law is complied with in the selection of a private partner is important for bankability.

- **Limited Grounds for Future Challenges** - by: (a) an unsuccessful bidder, or for (b) a subsequent government looking to terminate the P3 contract.

Engaging the Right Advisers

Qualified Advisers –
Engaging the right external advisers allows the government sponsor to leverage these advisers' knowledge of global best practices critical to structuring transactions, preparing P3 contracts, and handling stakeholder communications.

Early Engagement –
it is also important that advisers are selected early enough in the process. The government sponsor should have right advisers assisting with project feasibility studies, right at the point of evaluating whether to proceed with a P3 project.

Certainty of Project Scope

"A major contribution to unsuccessful projects is the lack of understanding for defining project and product scope at the start of the project. A properly defined and managed scope leads to delivering a quality product, in agreed cost and within specified schedules to the stake-holders."

~ APMG International, PPP Certification Guide

The P3 Contract should clearly define the scope of the service to be delivered by, and rights granted to, the private partner.

Certainty and clarity of contract scope is critical in reducing uncertainty and avoiding disputes between the parties.

The public authority must pay attention to the project scope. This takes on greater importance during the selection of private partner and at negotiation of P3 contract(s).

Certainty of Project Scope

MMA2 TERMINAL –
FEDERAL AIRPORTS AUTHORITY OF NIGERIA (**FAAN**) AND BI-COURTNEY AVIATION SERVICES LIMITED (**BASL**)

Dispute over Contract Scope

1

Concession to Design, Finance, Construct, Operate, Manage, Maintain and Transfer of the Murtala Muhammed Airport Ikeja – Lagos Domestic Terminal (Lagos) was granted by FAAN to BASL for a period of 12 years.

2

The initial agreement executed in 2006 was for 12 years, however BASL obtained ministerial approval for the extension of the concession term to 36 years. BASL also contends that the concession extends to the General Aviation Terminal (**GAT**).

3

FAAN insists that it did not endorse 36 years for the concession (but 12 years) and that the GAT was not part of the agreement and is to be operated independently from the part of the terminal to be developed by BASL.

4

BASL insists that it has a valid concession with a 36-year term, and which includes the GAT.

5

This longstanding dispute has contributed to the neglect of two other concessions granted to BASL – the concession for the construction and development of a conference and a four-star hotel at Murtala Muhammed Airport Ikeja, Lagos.

Sanctity of Contracts

Sanctity of contracts represents one of the major political/government risks when doing business with the public sector in Nigeria. Failing to honour contract obligations has stifled the flow of foreign investment into the country.

The impact of changes in government and the misalignment between the four-year election cycle and the typical life cycle of a P3 Project.

To mitigate/manage this risk, private partners often request:

- the adoption of dispute resolution mechanisms over which the Government Sponsor can exercise little to no influence – international arbitration (as against Nigerian courts).

Possible consequences of failing to honour contractual obligations – the P&ID example.

Sanctity of Contracts – **Case Study**

THE P&ID CASE

In a bid to reduce gas flaring, the Nigerian government **in 2010** entered into a 20-year agreement with P&ID to design and build a gas processing facility. P&ID would refine wet gas supplied by the Nigerian government and supply it to the government. The Nigerian Government was responsible for constructing the gas pipeline system leading to the gas facility and the supply of the wet gas.

In 2012, P&ID initiated arbitration proceedings after failure of the FGN to provide necessary gas pipeline infrastructure to supply gas to the gas facility which had not yet been constructed by P&ID. Nigeria fails to respond in the ongoing proceedings until 2014 when the Nigerian government reached a $850 million settlement with P&ID.

In **2015**, the new Buhari-led government ignores the settlement and pursues a dismissal of the suit instead.

In 2017, an independent tribunal in London found that Nigeria was liable to pay **US$6.6 billion in damages** following its failure to deliver on the terms of a Gas Supply and Purchase Agreement. The government was also ordered to pay 7% interest accruing from 2013, bringing the total sum payable to **US$9.6 billion**.

Performance Assessment and Monitoring

Monitoring by the government sponsor throughout the term of the P3 contract is essential to ensuring that the project produces the required outcomes.

Achieved via robust performance-related obligations, quality requirements, construction milestones (*for the construction phase*), performance indicators (*for the operations phase*), and will enable the government adjust the private partner's payments to reflect failure to meet contractual obligations (where appropriate).

Case Study – Lekki Toll Road Concession

Asset & Resource Management Limited submitted an unsolicited proposal to Lagos State Government (LASG) in 2000 to upgrade a 49km road in Lekki peninsula, Lagos that became the Lekki Expressway (the Project). The Project was ostensibly attractive to LASG due to budgetary constraints.

New P3 legislation (Lagos State Roads, Bridges and Infrastructure (Private Sector Participation) Development Board Law) was enacted, and a competitive procurement process was initiated. ARM's project company, Lekki Concession Company Limited (**LCC** or the **Concessionaire**) was selected as preferred bidder for the project.

The first version of the concession agreement largely reflected a traditional procurement approach and was subsequently replaced with a P3 contract modelled after a P3 for a highway concession in South Africa. LASG neither had an external advisory team, nor a financial model of the project, at this time – *Engaging the right advisers*

The concession was for a term of 30 years, and the Concessionaire was granted concession rights to upgrade, maintain and toll the Lekki Expressway, construct a parallel coastal road (and the option to construct a bypass).

An open tolling system and three toll plazas were envisaged. Users could avoid paying tolls by using alternative routes to be constructed by LASG. Tolling rates were set out in the concession and indexed against the CPI.

The concession did not have a detailed performance regime penalizing LCC for failure to meet key performance indicators – *Performance Assessment and Monitoring*.

Case Study – Lekki Toll Road Concession (Contd.)

LASG was liable to:
1. pay compensation if it unfavorably impacted the revenues and/or costs of the project.
2. cover Project senior debt if the project was terminated for default either by LASG or LCC in accordance with the schedule of debt service in the financing documents.

Use of a Federal Government Support Agreement - any shortfall in termination payments by LASG was to be settled from the LASG's share of funds from the Federation account. The FSA also included federal level consents for the project relating to the interface between the project and federal roads etc.; negotiation of the FSA was protracted.

Construction ought to have been completed by 2011, but there were delays caused by issues that were LASG's responsibility, such as the construction of an alternative route, relocation of utilities, a request from LASG to redesign a portion of the expressway. LASG had to compensate the Concessionaire for the costs and loss of revenue associated with these delays

Following completion of the first portion of the expressway in July 2010, the concessionaire started collecting tolls at the first toll plaza. LASG very quickly asked the concessionaire to stop collecting the tolls allegedly because it had not completed the alternative route, but many attributed the suspension of tolling to public protests about the tolls and upcoming elections. To compensate LCC, LASG paid shadow tolls – *Community Engagement, Political Interference*.

In 2013, LASG constructed the Lekki-Ikoyi Bridge which diverted traffic from the first toll plaza. In addition, tolls were due to increase by 20%, in line with inflation and currency fluctuations. The Concessionaire was prepared to cover at least part of these claims by an increase in the tolls, but this was politically unacceptable. Eventually, the LASG and the Concessionaire's investor agreed to a settlement that included LASG buying out the equity investors – *Political Interference, Economic Viability*.

Case Study – Lekki Toll Road Concession (Contd.)

Key Learnings

Engaging the Right Advisers

LASG failure to engage advisers at the outset of the concession process probably meant it did not negotiate the best possible commercial terms with the Concessionaire and did not fully appreciate the implication of the obligations it assumed under the concession agreement. Given the size and novelty of the project in Nigeria at the time, this was a significant oversight.

Political Interference

the Lekki Toll Road concession shows that political interference/support is a significant factor in determining the success of a P3 project. It also illustrates the significant costs a government sponsor can take on for failing to honour the terms of the P3 contract.

Community Engagement

Some have suggested that public opposition to paying tolls on the road was attributable to LASG's failure to consult with relevant stakeholders and host communities.

Q&A

questions

answers

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