KOGI STATE ELECTRICITY REGULATORY COMMISSION

NOTICE OF PROPOSED ESTABLISHMENT OF METHODOLOGY FOR A MULTIYEAR TARIFF ORDER: INVITATION FOR COMMENTS

In exercise of the powers conferred upon it by Section 44 of Kogi State Electricity Law, 2024; and of all other powers enabling it in that behalf, the Kogi State Electricity Regulatory Commission hereby establishes the Regulation on tariff methodology that shall apply in Kogi State Electricity Market.

Arrangement of Clauses

GENERAL

1. Short title and commencement

These Regulations may be cited as the Kogi State Electricity Regulatory Commission Tariff Methodologies Regulations 2025.

These Regulations shall come into force on the date on which it is approved by a resolution of the Commission. These Regulations shall be signed by the Chairman who shall also cause the seal of the Commission to be affixed thereon.

2. Interpretation

"Applicant" means a person who has made an application for a license, or for an amendment, or renewal, transfer, assignment, withdrawal of a license under the Law

"Building Block" means tool for spreading or amortizing the expenditure and cost of a regulated firm over time and not as a regulation.

"***Commission***" means the Kogi State Electricity Regulatory Commission.

"***Days***" means working days, excluding Saturdays, Sundays, and public holidays declared by the Federal Government of Nigeria or the Kogi State Government.

"***Law***" means the Kogi State Electricity Law, 2024.

"***License***" shall include all licenses which the Commission is empowered to issue.

"***Licensee***" means any person who holds a license issued by the Commission.

"***Major review***" means 5-yearly tariff review.

"***Minor review***" means a minor adjustment to the tariff made once yearly or six monthly or less to reflect the variation in fuel price, inflation and the exchange rate.

"***Month***" means a calendar month.

"***Tariff***" means prices allowed by the Commission in respect of any regulated activities of the Kogi State electricity market and charged to the customer for the electricity used.

"***Tariff Review***" means the application for a review and the processes employed to establish a tariff for a licensee or to make changes to the current tariff of a Licensee as prescribed in this Regulations.

"***Tariff Methodology***" means a method used to establish or identify the appropriate cost to be charged to the consumer as the tariff

"***USoA***" means the Uniform System of Accounts Regulations 2018 established by the Nigerian Electricity Regulatory Commission and as may be amended from time to time as adopted pursuant to section 44 (3)(a) of the Law

3. INTRODUCTION

The Commission, by this regulation and pursuant to the authority granted under Section 44 of the Kogi State Electricity Law, 2024, hereby outlines the foundational principles and pricing frameworks underpinning the proposed MYTO and details the procedural steps necessary to fulfill statutory requirements.

The methodology provides a 10-year tariff trajectory for the electricity sector, allowing for minor biennial reviews to account for changes in specific parameters such as inflation and gas prices. Additionally, comprehensive reviews will be conducted every five years to reassess all input in collaboration with stakeholders.

4. LEGISLATIVE AUTHORITY

4.1 Section 12(1)(i) of the Kogi State Electricity Law (KSEL), 2024, mandates the Commission to develop, introduce, and monitor the implementation of appropriate tariff methodologies applicable to all intra-State licensees and permit holders. Such methodologies shall be designed to:(a) Ensure full recovery of capital investments related to licensed undertakings; and (b) Guarantee a reasonable rate of return on such investments to promote business continuity and financial sustainability.

4.2 Section 44(3) further stipulates that: The holder of any license or permit issued under this Law shall comply with the methodologies and procedures specified by the Commission, as may be reviewed and updated from time to time, for determining

expected revenue recoverable under the terms and conditions of such license or permit.

4.3 While the Commission may adopt established methodologies such as those used by the Nigerian Electricity Regulatory Commission (NERC) as provided under Section 44(3)(a), it retains discretion to modify such methodologies to reflect:
(a) intra-State realities and peculiarities, pursuant to Section 44(3)(b) of the Kogi State Electricity Law, 2024.

(b) Factors that promote operational efficiency, economic utilization of resources, good performance, optimal investments, adherence to licensing conditions, and any other considerations the Commission deems appropriate.

4.4 Section 30(1) provides that every license or permit issued under this Law shall:

(a) Be in a form prescribed by the Commission; and
(b) Be subject to terms and conditions as may be stipulated, including provisions mandating the use of a tariff methodology duly approved by the Commission pursuant to Section 44 of this Law.

4.5 Subsection (2) further clarifies that, "the Commission shall consider parameters that enhance operational efficiency, optimize resource allocation, and support economic performance in line with regulatory best practice".

4.6 The Commission has set a 10-day period from the date of this notice for stakeholders to submit comments, objections, and representations concerning the tariff methodology.
All responses to this notice may be submitted at the Commission directly or sent via the email:
4.7 Following the consultation process, the Commission will issue the finalized tariff methodology as a formal decision, which will be published in the Official Gazette.

Licensees will be required to comply with the methodology as part of their licensing conditions

5. BACKGROUND

5.1 The KSEL 2024 mandates that electricity pricing regulations be guided by a tariff methodology developed by the Commission. In formulating this methodology, the Commission has studied global practices in regulating the electricity supply industry and evaluated various approaches, which are further discussed in Section 2 of these regulations.

5.2 The Commission's approach to designing an appropriate tariff methodology is based on three core principles:

- *Fairness* – Ensuring outcomes that are equitable to all stakeholders.
- *Efficiency* – Promoting cost-effective solutions for Nigeria and fostering investment in electricity generation in Kogi State.
- *Simplicity and Transparency* – Keeping the methodology straightforward and minimizing regulatory costs.

5.3 Additionally, the Commission, as required by Section 12(2)(h) of Kogi State Electricity Law 2024, seeks to balance the interests of all stakeholders whose shared interest is to maintain a viable, reliable, adequate, and safe electricity supply system which ensures a fair deal to the customers and the investors. Efficiency, in this context, not only entails producing electricity at the lowest cost but also incentivizing new investments in the sector.

5.3 A fair and equitable tariff methodology must address two key areas: (1) Determination of the total allowable revenue that covers prudent cost of providing efficient service to the consumers.

5.4 Establishment of principles governing tariff structures to recover these revenues in equitable manners while considering affordability.

6. PROPOSED TARIFF METHODOLOGY

6.1 Methodology for Developing the Multi-Year Tariff Order (MYTO)

Setting Methodology: *Cost of Service Regulation*

The Commission adopted a Cost of Service (CoS) Regulation, also known as Rate of Return Regulation, as the foundation for determining electricity tariffs. This approach ensures that tariffs are set to allow utilities to recover efficiently incurred costs—both operational and capital—while earning a fair return on their investments. This methodology is particularly appropriate for electricity markets, which operate as natural monopolies with limited competition.

Under this framework, the Commission employs the Building Block Model (BBM) to determine the total revenue requirement of each licensee. The BBM comprises three key cost components:

Return on Capital: A fair return on the Regulatory Asset Base (RAB), computed using the Weighted Average Cost of Capital (WACC);

Return of Capital (Depreciation): Recovery of the initial investment over the useful life of the asset;

Efficient Operating Expenditures (OPEX): Reasonable and prudent costs required for sustaining reliable delivery service.

This approach treats OPEX and CAPEX on equal footing, thereby eliminating any bias in investment incentives, while also allowing for applicable tax recovery.

The revenue requirement is determined by using the formula:

$R = B \times r + E + d + T$, *where*:

R = Total revenue requirement

B = Regulatory Asset Base

r = Allowed rate of return

E = Operating expenses

d = Depreciation

T = Applicable taxes

All cost inputs must be agreed upon with the Commission and reflect only prudent, efficient, and justified expenditures. The review procedure is outlined in Schedule 1 of this Regulation.

These inputs will be used to calculate an average regulated tariff for each year of the tariff control period, with annual adjustments reflected as percentage changes.

To promote transparency and consistency, the Commission shall periodically publish the approved base cost parameters. These parameters will be updated and made available on the Commission's website for use by licensees and investors.

One of the key advantages of the rate of return methodology is its ability to provide predictability and stability in revenue for utilities. By linking tariffs to transparent, auditable cost components, it reduces regulatory uncertainty and strengthens investor confidence, thereby encouraging long-term investment in critical infrastructure.

However, a known drawback of this model is the potential for cost padding or "gold-plating", also referred to as the Averch–Johnson effect. This occurs when operators over-invest in capital assets to increase their regulated returns. To address this, the Commission will implement several control measures, including:

- Efficiency benchmarking and cost reviews across utilities;
- Regulatory audits and prudency check to verify cost necessity;
- Pre-approval of capital projects to ensure alignment with service needs;
- Performance-based incentives to reward operational efficiency;
- Depreciation and claw-back mechanisms to reduce returns on unused or delayed assets.

Through this structured and transparent tariff-setting process, the Commission seeks to achieve a balanced regulatory outcome that ensures efficient cost recovery for licensees, incentivizes operational efficiency, and delivers just reasonable, and sustainable tariffs to consumers.

6.2 TREATMENT OF CAPITAL IN MYTO

Capital Investment Considerations

Two of the three foundational building blocks of the Multi-Year Tariff Order (MYTO) framework pertain directly to capital investments specifically, the return ***of*** and the return ***on*** capital. Given the capital-intensive nature of the electricity supply industry, it is essential that tariffs reflect both components. Investors must be assured of a reasonable return on their capital expenditure. If this assurance is lacking, it will discourage future investments, potentially leading to supply deficits and undermining the core objective of regulation.

Asset valuation under MYTO is dynamic. It is updated annually to reflect two movements: a reduction due to depreciation and an increase from new capital investments. These valuations are calculated based on replacement cost, actual capacity in service (not just nameplate ratings), and the remaining useful life of each asset, thereby providing a realistic view of the industry's capital base.

The capital cost structure under the MYTO framework comprises two elements:

- **Return of capital**: recovered through depreciation allowances.
- **Return on capital**: determined by applying the weighted cost of capital to the regulated asset base.

Both are applied to the rolled-forward asset value, ensuring the utility is compensated for its investment over the asset's economic life.

6.3 Treatment of Depreciation in MYTO

The MYTO shall apply the Straight-Line Depreciation Method for calculating depreciation-related costs in future tariffs. Under this method:

- The historical cost of each asset (or asset category) shall be depreciated evenly over its expected useful life, regardless of fluctuations in utilization or asset value.

- The annual depreciation expense will be calculated as the original acquisition cost of the asset divided by its economic life, with no indexing or revaluation.
- This approach ensures predictable cost recovery for capital investments and is simpler to administer compared to revaluation-based methods.

Unlike the Optimized Depreciated Replacement Cost (ODRC) approach, the straight-line method does not involve asset revaluation or downward optimization. However, for prudency and fairness in tariff setting, the 'used and useful' principle shall still apply. Only assets that are demonstrably contributing to service delivery will be eligible for inclusion in the rate base. In Kogi State, where most distribution infrastructures (such as transformers, feeders, and substations) are operating at or near full capacity, the Commission considers these assets to be fully utilized and eligible for full depreciation recovery.

To ensure consistency and alignment with sound regulatory practice, assets will be grouped based on asset classes with similar technical and economic life spans (e.g., buildings, vehicles, meters, switchgear), and straight-line depreciation rates will be applied accordingly. This grouping facilitates transparent and uniform application of depreciation policies across utilities.

In light of persistent supply deficits and high demand growth projections, the economic life of assets in the competitive segments (e.g., generation) shall be deemed equivalent to their technical life. This assumption ensures full recovery of investment for assets that are essential to system expansion and reliability in Kogi State.

6.4 Treatment of Third-Party Funded Assets in Tariff Regulation

When third parties such as communities, donor agencies, or government bodies fund and donate electricity infrastructure (e.g., transformers, lines, or substations) to a utility, regulators must apply a fair and transparent approach to their treatment in tariff setting.

As a general principle, the utility should not earn a return on capital for assets it did not finance, since it bore no investment risk. Allowing such a return would result in

windfall in profits and unjustified charges to consumers. However, under certain conditions, the utility may be permitted to recover the asset's value through depreciation (return of capital). This exception is justified where long-term replacement needs exist and is intended to help the utility accumulate funds to replace the asset at the end of its useful life.

Even so, donated assets should typically be excluded from the Regulated Asset Base (RAB) or entered at zero value to ensure consumers are not charged twice first by funding the donation, and again through tariffs. While capital recovery is restricted, utilities may still be allowed to recover operational and maintenance (O&M) costs for such assets, as they remain responsible for upkeep and service continuity. To this end, gifted assets shall be separately classified in the RAB to allow appropriate treatment.

To safeguard consumers and avoid inefficiencies or "gold-plating," KERC shall apply additional measures such as efficiency benchmarks, mandatory pre-approval of capital projects, performance-based incentives, and claw-back mechanisms for unused or delayed assets.

This balanced approach ensures sustainability and investment-readiness while upholding cost-of-service principles and protecting consumer interests.

In order to properly account for the donated assets, the Distribution licensee shall be required to submit to the Commission:

- An annual donated asset register;
- Signed evidence of asset handover by third parties;
- Exclusion from RAB unless specifically approved by KERC with public disclosure.

6.5 Treatment of the Cost of Capital (Weighted Average Cost of Capital – WACC)

The cost of capital is a key driver of electricity tariff design, as it determines the allowable return on both existing and future investments. The Commission will apply the ***Weighted Average Cost of Capital (WACC)*** methodology, which reflects the

expected cost of financing a utility business with similar risks. WACC combines the cost of debt and equity into a single rate, weighted according to their share in the utility's capital structure. The formula for Weighted Average Cost of Capital (WACC) is:

WACC = (E/V x Re) + (D/V x Rd x (1 - T)), Where:

E = Market value of equity
D = Market value of debt
V = Total market value of the firm's financing (E + D)
Re = Cost of equity
Rd = Cost of debt
T = Corporate tax rate.

This approach captures the varying risk levels of each funding source. While debt costs are based on observable market rates, equity costs are inferred from industry benchmarks. As equity carries higher risk, its required return is usually higher than debt, placing WACC between the two. This ensures a fair return without overburdening consumers.

6.6 Treatment of Operational Expenses in MYTO

The initial operating cost inputs for tariff setting in Kogi State will be derived from the historical data of the Abuja Electricity Distribution Company (AEDC), which previously served the state since 2013.

The Commission shall validate such AEDC historical operating cost data with independent cost audits and field-based data within Kogi State to reflect post-demerger operational realities. The projected costs will be adjusted using standard efficiency benchmarks while taking into account Kogi State's specific energy allocation profile. Operation and Maintenance (O&M) expenses will be directly tied to service delivery performance. For example, increasing the number of customer service centers and deploying more field maintenance teams will raise operational costs in the short term, but these investments are essential to reduce outage times and improve customer satisfaction.

Given that the Kogi electricity market is in its formative stage, operational costs are expected to be relatively high initially. However, as systems stabilize and operational experience grows, efficiency gains—such as fewer emergency repairs and better planning—are expected to lower costs over time.

Additionally, revenue collection efficiency is projected to rise steadily over the next five years, driven by widespread metering deployment, automated billing systems, and improved customer engagement.

7. Miscellaneous Provisions and Tariff Review Framework

To ensure transparency, efficiency, and predictability in electricity pricing, the Commission has established structured provisions for tariff setting, review, and adjustment across all regulatory periods.

7.1 Annual Tariff Reviews:

Every year, the licensee shall conduct a tariff review, subject to the Commission's approval. However, tariff adjustments during these annual reviews will be limited strictly to exogenous factors such as inflation, changes in input fuel costs (e.g., gas), and exchange rate fluctuations. These reviews must begin in the final month of the current tariff period and conclude within one month.

7.2 Mid-Year Adjustments:

In cases where there are rapid and significant fluctuations in inflation, fuel prices, or exchange rates that materially affect either consumers or licensees, the Commission may approve a six-monthly tariff adjustment. Any such mid-year review must also be concluded within one month and cannot be implemented without the Commission's prior approval.

7.3 Major 5-Year Tariff Reviews:

A comprehensive tariff review shall be conducted every five years. Initiated by the licensee and approved by the Commission, this major review will reassess and update the input assumptions of the Multi-Year Tariff Order (MYTO) model to reflect current realities. However, while the values of input will be updated, the structural assumptions set by the Commission shall remain unchanged. Each major review shall begin at least one year before the start of the next tariff cycle and be concluded within six months.

7.4 Special Major Reviews:

If significant deviations in industry parameters occur before the end of a five-year cycle, the licensee may request an early major review. Such a request must be justified with clear evidence that current tariff assumptions are no longer valid and threaten industry viability. Such mid-cycle major reviews may be triggered where: (i) inflation exceeds 10% deviation from assumptions; (ii) fuel input prices change by over 15%; or (iii) foreign exchange shifts exceed 20% from the base rate.

7.5 Data and Methodological Standards:

To support these reviews, the Commission shall define and validate key economic and technical inputs, including but not limited to, electricity demand forecasts, interest rates, Weighted Average Cost of Capital (WACC), technical and non-technical loss estimates, and exchange rates for foreign-denominated costs. A uniform system of accounts (USoA), as developed by the Nigerian Electricity Regulatory Commission (NERC), shall guide all reporting. This includes capital expenditure, projected and actual sales, operating and fuel costs, and statutory obligations like taxes.

7.6 Location of Generation and DUOS Charges:

To enhance efficiency and affordability, electricity generators may be required to locate near distribution networks or load centers. Furthermore, Distribution Use of System (DUOS) charges will apply to medium-voltage licensees and be determined using the building blocks method. These charges will cover capital and operational costs of the distribution network, including losses and metering.

7.7 The right to Public Hearing:

In line with regulatory due process, the licensee may, within fifteen (15) days of receiving the Commission's tariff determination, submit a formal request for a public hearing. This provides an opportunity for wider stakeholder input and further scrutiny of the licensee's tariff submission prior to final approval.

SIGNED BY ORDER OF THE COMMISSION

On this 16TH day of SEPT. 2025.

Engr. Ibrahim S. Abdwaaris
CHAIRMAN/CEO

Schedule I

Procedure for Review of Tariff Cost Inputs in the Tariff Model

Any applicant seeking a license—whether new, amended, renewed, or extended—is required to approach the Commission for a review of cost inputs to be applied under the tariff methodology.

For generation license applicants, the Commission shall, within 21 days of receiving the application, review and agree with the applicant on allowable cost components. These include all "Used and Useful" costs and other inputs prescribed and locked into the tariff model by the Commission. During this period, the Commission will accept a Power Purchase Agreement (PPA) that is initialed but may not yet contain the final tariff schedule.

The applicant must submit relevant commercial agreements—such as the Fuel Supply Agreement (FSA), Engineering, Procurement & Construction (EPC) contract, and Operations & Maintenance (O&M) contract—along with all documentation listed under Schedule 2.

Applicants for Transmission and Distribution (including Medium Voltage Distribution) licenses must submit documentation as per Schedule 3, while Electricity Retail Companies (ERCs) must comply with Schedule 4 requirements, including the executed PPA.

Schedule 2 – Generation Tariff Review Information

Description	Unit	Amount	Remarks
Generator Type			
Generation Capacity			
Capital Cost	₦		
O&M Cost (Fixed)	₦		
O&M Cost (Variable)	₦		
Capacity Factor	%		
Auxiliary Requirement	%		
Fuel Cost	₦/GJ or equivalent		

Economic Life of Plant	Years		
Construction Period	Months		
Sent-out Efficiency	%		
Availability Factor	%		
Ancillary Consumption	%		
Load Factor	%		
Capacity Degradation	% per year		

Notes:

1. Applicants must attach supporting evidence for all cost claims, indicating the type of evidence in the "Remarks" column.
2. Cost breakdowns must be detailed by components.
3. All financial data should be stated in Naira (₦).

Schedule 3 – Transmission / Distribution Tariff Review Information

Description	**Unit**	**t-2**	**t-1**	**t**	**t+1**	**t+2**	**t+3**	**t+4**	**t+5**	**Remarks**
Fixed Assets Register										
Depreciation Schedule										
O&M Cost (Fixed)	₦									
O&M Cost (Variable)	₦									
Administrative Cost	₦									
CAPEX Projection	₦									
Transmission/Distribution Loss	%									
System Capacity	MW or kVA									
System Length	Km									
Ancillary Service Costs	₦									

Notes:

1. Provide evidence for each item and indicate the type.
2. Submit detailed breakdowns by component.
3. Express all financial data in Naira.
4. "t" refers to the initial year of the regulatory control period.
5. Provide actuals for t-2 and t-1.
6. Breakdown data by physical location, business unit, and functional area.

Schedule 4 – Electricity Retail Companies Tariff Review Information

Description	Unit	t-1	t	t+1	t+2	t+3	t+4	t+5	Remarks
Cost of Power	₦								
Fixed Asset Register									
Depreciation Schedule									
CAPEX (including metering)	₦								
O&M Cost (Fixed)	₦								
O&M Cost (Variable)	₦								
Administrative Cost	₦								
CAPEX Projection	₦								
Distribution Loss – Technical	%								
Distribution Loss – Non-Technical	%								
System Capacity	MW/kVA								
Actual Sales	MWh								
Projected Sales	MWh								
Distribution Length	Km								
Miscellaneous Costs	₦								
Total Customers	No.								
Customer Numbers by Class	No.								

Notes:

1. Submit data by customer class and location.

2. Include executed PPA.
3. Provide documentary evidence for each claim.
4. Express all costs in Naira.
5. Provide actual values for t-1 and t-2.

"t" is the start year of the regulation