ALLIANCE FOR AFFORDABLE INTERNET
NIGERIA COALITION

Date: 19 March 2021

To: Nigeria Communications Commission

Subject: **Consultation Paper on Determination of Capital Structure for Licensees in the Communications Sector in Nigeria- A4AI Nigeria Comments**

The Alliance for Affordable Internet (A4AI) Nigeria Coalition (the Coalition) established in 2014 has actively been engaged on the issues of infrastructure sharing and open access , fiscal and consumer protection and has been privileged to have worked with the NCC on strategies towards achieving affordable and meaningful connectivity. The Coalition is pleased to submit these comments in the above-referenced proceeding.

I. Summary of submission

The Coalition appreciates the efforts by the Nigerian Communications Commission (the Commission) to strengthen and facilitate investment in the Nigerian communications market. Nigeria, like many other countries emerging from the current Covid-19 pandemic, will require robust digital connectivity to build back better. A healthy market and sustainable industry are essential to achieving the Government of Nigeria's broadband and digital economy goals as well as increasing connectivity across the country. The state of broadband connectivity and affordability in Nigeria is critical to understanding the context of our submission. According to A4AI's data, 60% of Nigeria's population find broadband unaffordable - paying more than 2% of their monthly income for 1GB of data. This means that for a significant proportion of the country, the UN Broadband Commission's "affordability target" is not met. Those who fall in the lowest quintile of the population spend up to 4.8% of their average monthly income for the same 1GB of data[1]. Furthermore , Nigeria ranks 131 in the World Bank's "Ease of Doing Business Ranking"[2], which is another indication of the fact that work has to be done in the direction of strengthening policy and regulatory efforts with the ultimate goal of fostering competition and decreasing the cost of connectivity in the country. Thus, regulatory changes should spur healthy competition and investment and should be pursued in such a manner so as not impose additional burdens to regulated companies.

Given the above facts, the Coalition believes that the Commission's proposed approach in its "Consultation Paper on Determination of Capital Structure for Licensees in the Communications Sector in Nigeria" (Consultation) may ultimately run counter to the desire of ensuring Nigerians are well connected with affordable internet in a dynamic and competitive market. Imposing overly rigid and/or burdensome recurring financial disclosure and capitalisation requirements on current and potential licensees may stifle investment, slow down competition, and ultimately inhibit the growth of a healthy, competitive and stable communications ecosystem. In particular, these requirements can undermine the Nigerian National Broadband Plan by deterring market entry for innovative service providers and negatively impacting broadband affordability and availability.

[1] A4AI 2020 Mobile pricing index. https://a4ai.org/extra/baskets/A4AI/2020/mobile_broadband_pricing_gni
[2] See World Bank's "Doing Business" 2020 https://www.doingbusiness.org/content/dam/doingBusiness/pdf/db2020/Doing-Business-2020_rankings.pdf

While the Nigerian Communications Act (2003) gives the Commission a wide range of powers,[3] this proposed approach goes beyond the scope provided by the Act. The Coalition, therefore, recommends that the Commission rely on existing processes and frameworks in place to help ensure that licensees are properly funded. We understand the importance of complying with the mandatory corporate governance requirement within the industry, therefore, the Coalition encourages the Commission where necessary, to consider the standard practice in other jurisdictions by taking a lighttouch regulatory approach, limiting its review of capital structures to a case-by-case basis where objective concerns regarding a particular licensee's / potential licensee's capitalisation and financial health exists.

Captured below are details of some of the key concerns highlighted in the summary.

II. Burdensome Financial Disclosure, Benchmark and Reporting Requirements Will Stifle Investment, Slow Competition and Inhibit Growth in the Communications Sector

Nigeria is at a pivotal point in developing and leveraging next-generation services to stimulate its digital economy. However, as a general matter, licensees in Nigeria are already subject to robust reporting obligations under the Corporate and Allied Matters Act, the Financial Reporting Council Act, Value Added Tax Act and the Code of Corporate Governance for the Telecommunications Industry. Thus, requiring additional financial reporting and disclosure obligation will no doubt impose additional cost implications for these operators and thereby impede the ease of doing business in the communications sector. Such additional costs have the potential of being passed on to affect consumer prices and thus overall affordability.

Secondly, burdensome financial disclosure requirements may deter potential and current licensees from entering/staying in the market, as they may be hesitant to share sensitive financial data, particularly where there may be valid reasons as to why this financial data may not represent a 'true' picture of the licensee's medium-long term financial stability (e.g., the licensee may have experienced one-off financial events in the previous year that it considers do not represent a true/fair picture, such as reduced revenue streams that might result from having made an acquisition. Conversely, one-off sales in the previous year could artificially inflate a licensee's revenue streams and might not be a true/accurate picture of its future financial stability). Likewise, such disclosures may diminish a licensee's ability to procure financing, therefore hampering the licensee before it can get off the ground / rebut negative perceptions around its financial stability. Lenders or investors may be less willing to invest in a licensee if it carries with it a risk that their own financial data would come under regulatory scrutiny. licensees, lenders and investors alike are likely to be concerned about how their financial data would be used and safeguarded.

Thirdly, gathering the required data would add both time and cost to preparing a license application or separate regulatory submission if this financial review is incorporated into the licensing process or be required as an additional regulatory filing. This is particularly concerning if such reporting is required regularly. Imposing financial disclosure requirements also

[3] Section 4 (1) Nigerian Communications Act 2003

introduces additional constraints such as increased processing time for applications, requiring thorough review by qualified financial experts and analysis by the Commission. Such delays would be encountered as a result of the additional processes which would hamper the communications sector's growth as it diverts important time and resources away from licensees who can invest in the market (e.g., investment needed to upgrade existing infrastructure and/or roll-out of innovative infrastructure and offers to consumers). The additional time, effort and costs associated with gathering will no doubt impact consumers in the form of higher tariffs and/or reduced quality of services, as licensees are unable to invest as much, or at least not as quickly, as they would otherwise have been able to do . Higher tariffs will affect the realisation of the goals set in the Nigerian National Broadband Plan 2020-2025 ("**NBP**")[4] for ubiquitous broadband and its associated benefits to the Nigerian population, particularly the goal of increased data download speeds in both urban and rural areas.[5] In addition, Nigeria's economy would be deprived of the anticipated financial benefits and economic growth from increased connectivity[6].

An overly burdensome / rigid framework for financial disclosure and reporting also runs counter to the Government's stated objectives in the NBP that the "*Government, on its part, will create the enabling environment as well as relevant policies to ensure effective deployment and protection of telecommunications infrastructure*"[7].
Ubiquitous, robust, reliable, and affordable connectivity is critical for the Nigerian economy, and for individual businesses and consumers alike. Never before has this been so important, as during the current global Covid-19 pandemic; the importance of such connectivity in Nigeria's plan to emerge from this global crisis should not be underestimated. It would be a missed opportunity if, as a result of unduly burdensome / overly rigid financial disclosure and reporting requirements, licensees were diverted away from the task in hand, and if Nigeria were unable to realise the goals in the NBP and unlock the economic growth opportunities within that plan, failure of which could lead to an ever-widening digital divide.

Finally, the proposed framework as it currently stands injects uncertainty into the licensing process itself. The Consultation provides no benchmarks for determining a licensee's qualifications or compliance and fails to provide insights into how the Commission will conduct the analysis or oversight. Such uncertainty could potentially lead to inefficiencies in the capitalisation of the sector, reducing investment and slowing growth.

III. The Proposed Requirements Would Undermine the National Broadband Plan

Affordability is a major component that often constitutes a barrier to the adoption and usage of broadband. The NBP recognises the importance of ubiquitous, affordable connectivity as a

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[4] https://www.ncc.gov.ng/accessible/documents/880-nigerian-national-broadband-plan-2020-2025/file
[5] See for example, references in the National Broadband Plan 2020-2025 (NBP) that the plan is designed to deliver data download speeds of about 25Mbps in urban areas and 10Mbps in rural areas. It also targets covering at least 90% of the population and penetration rate of 70% by the end of the plan's lifetime, and at a price of not more than N390 per 1GB of data (2% of median income or 1% of minimum wage).
[6] As noted at page 5 of the NBP, the Government are aware of the economic growth opportunities afforded by the deployment of broadband technologies; and are told that every 10% increase in broadband penetration results in about 2.6% to 3.8% growth in GDP.
[7] See page 5 of the NBP.

driver for job creation, improved socio-economic development and sustained economic growth, amongst others. Improving connectivity across Nigeria calls for policies that improve the affordability and availability of the internet. Indeed, the Government also recognises in the NBP that "it is important to note that the successful implementation of the Plan requires synergy between government and the private sector"[8].

Setting the right conditions for investment to build back better will be as critical to implementing Nigeria's robust, future proof Plan for Nigeria . As discussed above, the proposed requirements and benchmarks inject uncertainty and delay into the regulatory process, potentially deterring or even denying market entry for innovative service providers. The proposed requirements could, for example, dampen a new entrant's appetite for devising creative financial structures or entering into partnerships that would enable an otherwise cost-prohibitive deployment in a rural area, for fear that such a proposal would be rejected. A less connected nation, and one that may be perceived as involving increased regulatory obstacles/bureaucracy, also risks undermining the Government's desire (as espoused in the NBP) to incentivise low-cost smartphone devices and promote local assembly/manufacturing of telecom network and end device components[9].Any processing delays and additional regulatory costs resulting from adopting these requirements would likewise impede the rollout of broadband infrastructure.

IV. Current Systems Exist to Manage Financial Risks of License Holders

The existing financial system, which is made up of lenders, banks, investors and other public and private sector actors, leverage different financial mechanisms to ensure that licensees have adequate capital structures and liquidity. The Commission's efforts to undertake this type of review would be duplicative as such actors are already subjected to similar requirements under the Corporate and Allied Matters Act, the Financial Reporting Council Act, Value Added Tax Act and the Code of Corporate Governance for the Telecommunications Industry, as mentioned above. Duplicating these efforts could lead to conflicting 'value' judgments and regrettably, increased risk of litigation, particularly given the impact a negative value judgement could have on an existing and/or prospective licensee.

Secondly, we are concerned that the outlined proposal in the Consultation document may not properly enable the Commission to effectively evaluate the credit quality and asset valuation of a potential licensee and that perhaps it may be best to rely on the assessment from a financial regulator. While the Nigerian Communications Act (2003) gives the Commission a wide range of powers,[10] these powers in the Coalition's view, do not include the activities proposed by the Commission in the Consultation. The framework also places the Commission in the position of effectively approving debt transactions and injections of equity capital. The premises advanced by the Consultation do not reflect all of the dynamics that drive investment decisions. For example, the Consultation conflates liquidity with capital structure, which are different concepts. An entity can be very liquid with high debt or equity and very liquid with <u>both</u> as well. There are several reasons why a company may want to use financing versus straight equity. A company can also obtain more financing when credit is looser, providing opportunities for a dividend recap. Under the proposals being advanced, such structures would require the Commission's

[8] Page 6 of the NBP.
[9] Page 11 of the NBP.
[10] Section 4 (1) of the Nigerian Communications Act 2003

approval. The additional administrative burden being conferred on the Commission and the responsibility to make what could become difficult/tricky value judgements should not be underestimated.

The Consultation also does not consider that the cost of capital (and capital structure optimisation) may be different for foreign and domestic investors. Generally speaking, financing terms in Nigeria are short, which is often not optimal for financing infrastructure projects or assets that take a longer time to earn a return on investment. Also, when global credit is cheaper, it can make sense to take advantage of leverage for some (but not all) players. As such, there could be differences in the cost of capital and, therefore, capital structure optimisation based on how the licensee sources its funding.

In addition, the Consultation raises a host of other questions which we would like the Commission to elaborate on notably:

a) How will the appropriate debt to equity ratios be determined? For example, what are the different needs between an Open Access Fibre (InfraCo) License, Metropolitan Fibre Cable Network (MFCN) license, Internet Service Provider (ISP) License, Wholesale Wireless Service License and a Unified Access Service License (UASL), and why?

b) How will asset value be determined?

c) How are financial terms available within the market taken into account? Will the Commission supplement current banking market offerings with governmental instruments in order to meet the capital structure requirements outlined?

d) Would the “optimal capital structure” ratios differ between local and for foreign investors?

e) Does the “optimal capital structure” change with market dynamics?

f) Would any “optimal capital structure” apply to the license holder only or extend to the parent entity as well?

g) How would some of the currency rules for the Commodity Channel Index (CCI) be handled in relation to any proposed framework?

h) What are the consequences of failing to meet any benchmarks?

We understand this process will be complex and welcome a clarification of the above mentioned issues. Given the complexities and nuances that drive investment decisions, the Coalition respectfully encourages the Commission to reconsider its interest to expand its role into the financial analysis of licensees, and recommend that instead, it rely on information from the financial and/or corporate governance regulators with expertise in this area. Such an approach would mitigate some of the potential pitfalls already highlighted in this submission , such as the Commission having to engage additional resourcing and financial experts and/or having to take difficult/tricky ‘value’ judgements that could be subject to appeal/litigation. We encourage the

Commission to continue to rely on and enforce the existing rules that are designed to address a licensee's qualifications, such as requiring prior Commission approval for certain changes in licensee shareholding structures, assignments or pledges of a license, and licensing conditions that state that the inability of a licensee to pay up its debts is grounds for suspension or revocation of license.

V. Any Framework/Disclosure Requirements, If Adopted, Should Be Applied Only on Case-by-Case Basis

Should the Commission move forward with a capital structure framework, the Coalition encourages the Commission to consider a light regulatory touch in line with international best practices. The Coalition also recommends that any disclosure requirements should be required only on an as-needed basis (in light of objective financial concerns that exist). Additionally it will be beneficial to ensure any benchmarks and deadlines for compliance are clearly defined.

VI. Conclusion

In summary, the Coalition considers that Increased reporting and financial burden to companies could ultimately impact broadband prices for consumers. The potential for longer license processing times could significantly impact investment and deprive Nigeria consumers and businesses of healthy competition for services needed to advance affordable access. Additional imposed burdens could introduce a real risk of inability to procure the needed funding to improve connectivity in line with the economic opportunities identified in the National Broadband Plan.

In light of the above, the Coalition encourages the Commission to explore the full scope of current frameworks in assessing the financial health of its licensees .Where regulation is necessary, the Commission should consider applying Capital structure requirements on an as-needed basis.

The Coalition is grateful for the opportunity to present its recommendations for this Consultation and looks forward to collaborating with the Commission in its quest to improve affordable internet and expanded connectivity to develop the digital economy of Nigeria.

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