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Introduction

Climate change is a pressing global challenge that impacts all nations, and Nigeria is no exception. In recent years, Nigeria has faced significant challenges, including unprecedented flood levels, increase in temperature, variable rainfall and unpredictable weather patterns generally. The potential effects of climate change and weather-related disasters continue to pose significant risks to agriculture, food security, and water supplies. These events have led to a growing emphasis on initiatives that aim to combat climate change, with a particular focus on climate mitigation projects. For the successful execution of climate mitigation projects, securing appropriate funding is crucial. There are various funding options available, each characterized by distinct features and governed by different legal requirements under local laws. It is essential for stakeholders to carefully evaluate the specific needs of their projects in conjunction with the characteristics of available funding models. This method ensures the selection of the most suitable financing solution for climate mitigation efforts.

This article explores the various financing models available for climate-related projects, emphasizing the legal frameworks that govern these models within the Nigerian context. By understanding these frameworks, stakeholders can navigate the complexities of funding and effectively support their climate mitigation initiatives.

Financing Models

Financing models play a crucial role in the execution of climate mitigation projects. The choice of a particular model depends on various factors such as the nature and scope of the project, its development timeline, and its commercial viability. In this article, we will discuss commonly used financing models, focusing particularly on their legal foundations and implications.

a) Green Bonds

Green bonds are a specialized category of bonds designed specifically to raise funds for environmental and climate-friendly projects. Like traditional bonds, green bonds can be issued by a variety of entities, including government bodies, private companies, and financial institutions. These bonds are directed towards investors looking to contribute to environmental sustainability while receiving a return on their investment.

For green bonds to be issued to the public, they must first be approved by the Securities and Exchange Commission (SEC).¹ This ensures that the capital raised is indeed used for projects

¹ See the SEC Rules on Green Bonds issued on 12th October 2018

with a positive environmental impact, such as renewable energy, clean transportation initiatives, combating deforestation etc. The SEC's 2018 Green Bonds Rules offer a structured framework for issuing these bonds, mandating that all proceeds be dedicated to eligible green projects.² This includes requirements for issuers to submit detailed plans on how the funds will be used, along with periodic reports on the progress and impact of the projects financed.

Nigeria set a notable precedent in December 2017 by becoming the first African nation to issue green bonds, raising ₦10.69 billion.³ This initial issuance funded solar energy projects and afforestation initiatives, highlighting Nigeria's dedication to addressing climate change and enhancing sustainability. The success of this initiative highlights the potential of green bonds as a mechanism for financing projects that benefit the environment, merging financial investment with environmental responsibility.

b) Climate Funds

Climate funds are specialized pools of capital created to finance efforts aimed at combating climate change. These funds differ significantly in their origin and structure and can be categorized into statutory funds established by legislation, corporate funds initiated by businesses, multilateral funds from international organizations, and international funds supported by international treaties.

In Nigeria, the National Climate Change Fund, established under the Climate Change Act 2021, plays a vital role. This statutory fund finances innovative climate mitigation and adaptation projects, drawing on financial contributions from the national budget, international grants, and revenues from mechanisms like carbon taxes and emissions trading. Similarly, the Africa Climate Change Fund, created by the Africa Finance and Development Bank (AFDB), extends its reach across the continent with a fund size of approximately \$25.71 million, sourced from nations including Germany, Italy, and Canada, to support various climate projects.⁴

Globally, significant funds such as the Climate Investment Fund and the Green Climate Fund illustrate the collaborative efforts of multiple countries and financial institutions aimed at mobilizing substantial financial resources for climate action worldwide. For instance, the UK's International Climate Fund seeks to finance climate projects in developing regions, highlighting the global commitment to tackling climate challenges.

² See Rules 2 and 4(i) of the Green Bonds Rules 2018

³ See article titled "Nigeria's NGN-10.69bn green bond slightly oversubscribed" available at www.renewablesnow.com/news/nigerias-ngn-1069bn-green-bond-slightly-oversubscribed-596631/ and accessed on 3rd June, 2024

⁴ See the AFDB's statement on Africa Climate Change Fund available at <https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/africa-climate-change-fund> and accessed on 3rd June, 2024.

Corporate entities also contribute significantly to these efforts. An example is Amazon's Climate Pledge, which allocates substantial resources to finance sustainable projects. Funding from these sources can vary, including grants, concessional loans that mix grant and loan features, or standard loans based on prevailing market conditions. This diverse range of funding mechanisms underlines the extensive options available for financing climate mitigation projects, reflecting a unified global acknowledgment of the urgency to mobilize financial resources to address climate change effectively.

c) Private Climate Finance

Private climate finance refers to investment initiatives led by the private sector to support climate-related projects. These initiatives often involve collective investment schemes where private investors pool their resources to create a fund dedicated to financing environmentally sustainable projects. These schemes usually operate through debt mechanisms and are regulated by the Securities and Exchange Commission (SEC), ensuring they comply with the Investments and Securities Act, 2007 (ISA) and SEC Rules. This regulatory framework ensures transparency and accountability in the operations of such funds.

Investment schemes can be structured as unit trust investment schemes, where investors purchase ownership units that represent a share in the fund. These schemes can be either close-ended or open-ended, offering varying degrees of liquidity and investment duration.⁵ Legally, these investment schemes must formalize their structure and objectives through a trust deed and register with the SEC to protect investor interests.

Another significant aspect of private climate finance is private equity funds. These funds invest directly in companies engaged in activities that aid climate mitigation, such as producing solar panels or manufacturing lithium batteries. The regulatory oversight for these funds requires a minimum investment threshold of ₦1 billion to fall under the SEC's jurisdiction.⁶ They must adhere to strict rules against public solicitation and are required to cater exclusively to qualified investors. Fund managers of private equity funds must maintain transparency by regularly reporting to both the investors and regulatory authorities. This ensures that the funds' activities align with climate mitigation goals and comply with the set regulatory standards.

d) Carbon Finance

Carbon finance represents a range of financial tools designed to support the reduction of carbon emissions through the trading and monetization of carbon credits. A carbon credit is essentially a certificate granting the right to emit a specified amount of carbon dioxide or other greenhouse gases, with one credit equating to one ton of carbon dioxide. This system enables

⁵ See Sections 153 & 154 of the Investments and Securities Act 2007

⁶Rule 558 of the SEC Consolidated Rules 2013

projects that reduce emissions to generate revenue by selling these credits, thereby funding further climate mitigation efforts. The carbon market is divided into two main segments: the voluntary and the compliance markets.

The voluntary carbon market: This market operates independently of government intervention and does not require any regulatory or statutory framework for its establishment. It is based purely on the voluntary participation of entities that choose to offset their emissions, often motivated by goals related to corporate social responsibility, reducing their carbon footprint, or enhancing their public image through ethical environmental practices.

In Nigeria, the voluntary carbon market is still in its early stages, lacking full development and often reliant on external capacities for transaction completion. This market typically involves international parties and depends on foreign carbon registries for the verification and issuance of carbon credits.

The compliance carbon market: Conversely, this market is governed by legal frameworks that require certain entities to offset their emissions according to specific regulations. This market sets enforceable limits on emissions and trading capabilities, ensuring that participants meet prescribed emission reduction targets. However, the compliance market has not been fully established in Nigeria due to the absence of the necessary legal and regulatory infrastructure. It is important to note that the revenue generated from the sale of carbon credits, which are considered a financial asset, may be subject to capital gains tax.⁷

The Importance of Finance in Climate Mitigation

Finance plays an essential role in advancing climate mitigation efforts in Nigeria, a point that has been discussed throughout this article. Selecting the appropriate financing model is a complex decision that hinges on an understanding of the legal environment alongside the unique requirements of each project. Various financial avenues, such as the issuance of green bonds, the creation of climate funds, and the innovative application of carbon finance, each provide unique opportunities and challenges. It is crucial for all stakeholders, from government bodies to private sector players, to navigate these complexities with diligence, focusing on compliance, sustainability, and ultimate impact.

The Way Forward for Sustainable Development in Nigeria

As Nigeria faces the ongoing challenges of climate change, effectively leveraging diverse financial models is a crucial step towards sustainable development. The path is filled with complex legal and operational nuances that require careful and strategic planning. However,

⁷ See Section 6 of the Capital Gains Tax Act

with concerted and collaborative efforts from both the private and public sectors, achieving a greener and more resilient Nigeria is within reach.

For guidance on securing financing for climate-related projects, or for investors interested in establishing funds to support such initiatives, please feel free to contact us at: olayinka.alao@scp-law.com; or info@scp-law.com.

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