

# OVERVIEW OF THE PROPOSED NEW RULE ON SOCIAL BONDS IN NIGERIA

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Social bonds, which are also known as social impact bonds, are a relatively recent concept. The first social bond was issued in 2010 by Social Finance Ltd. in the United Kingdom.<sup>1</sup> Recent examples of social bond issuance abound such as the €13 billion dual-tranche social bond issued by the European Union to mitigate the negative effects of the COVID-19 pandemic<sup>2</sup> and the \$463.9 million Kangaroo bond launched by the African Development Bank.<sup>3</sup>

The Securities and Exchange Commission recently made available the Proposed New Rule on Social Bonds. The rationale cited for this was the rise of interest in ethical investment and the recognition of social bonds being as a means of providing funding for specific projects. The realization of the potential use of social bonds to fund social projects was brought to the fore in view of the diversion of government spending to other affected areas during the COVID-19 pandemic.

## What are social bonds?

The proposed Rule defines a social bond as “a type of debt instrument, where the proceeds would be exclusively applied to finance or refinance new and/or existing eligible projects with clear and identifiable social objective(s) and which are dedicated to an identified population.”

From the definition, one can deduce the following:

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<sup>1</sup> [https://sibdatabase.socialfinance.org.uk/?project\\_id=7](https://sibdatabase.socialfinance.org.uk/?project_id=7)

<sup>2</sup> <https://cib.bnpparibas/eu-issues-e13bn-sure-social-bond-to-further-mitigate-pandemic-impact/>

<sup>3</sup> <https://www.afdb.org/en/news-and-events/press-releases/african-development-bank-launches-aud600-million-usd4639-million-kangaroo-social-bond-44119>

- It is a form of debt financing;
- The bond targets specific previously identified projects; and
- The project targets a specific group of people.

## What projects can be financed by social bonds?

The proposed Rule defines a social project as a project directly aimed to “address or mitigate a specific social issue and/or seek to achieve positive social outcomes whether or not exclusively, for a target population.” Social issues affect the welfare and proper functioning of society. The continuation of these issues is undesirable and as such attempts are made to find lasting solutions to them.

According to the proposed Rule, for a bond to qualify as a social bond, the proceeds should be used to provide and/or promote one or more of the following social projects:

1. Affordable basic infrastructure (such as provision of potable drinking water, sewers, sanitation, transport, energy, etc.)
2. Access to basic services (such as health, education and vocational training, healthcare, etc.)
3. Affordable housing
4. Job creation
5. Food security
6. Socioeconomic advancement and empowerment
7. Any other social project as may be approved by the Securities and Exchange Commission from time to time.

## Who is the target of social projects financed by social bonds?

Social projects financed by social bonds are intended to serve specific groups of people. The proposed Rule lists them as follows:

- People living below the poverty line
- Excluded and/or marginalised populations and/or communities
- Vulnerable groups
- People with disabilities

- Migrants and/or displaced persons
- Undereducated population
- Underserved population, due to lack of access to essential goods and services
- Unemployed persons

## Criteria for Approval of Social Bond

Under the proposed Rules, approval of the issuance of a social bond by the Securities and Exchange Commission is subject to the fulfilment of certain conditions. An issuer of a social bond is expected to comply with the general registration requirements for debt issuances stated in the Rules and Regulations of the Commission. In the same vein, an issuer of a social bond is expected to file the following documents:

1. A letter indicating a commitment to invest all the bond proceeds in eligible social projects or assets;
2. A feasibility report clearly stating the measurable benefits of the proposed social project or assets;
3. A prospectus specifying the social objects, project selection criteria, decision-making procedures, social and environmental benefits, risks associated with the projects and the use and management of the bond proceeds;
4. An independent assessment or certification issued by a professional certification authority approved or recognized by the Securities and Exchange Commission;

The Commission has the right to require the filing of other documents from time to time.

## Utilisation and Management of Social Bond Proceeds

The proposed Rule is strict on the requirement that the net proceeds be used solely for the social project or asset stated in the approved prospectus. In addition to this, the net proceeds are to be tracked as stated in the approved internal policy of the issuer as provided for in the prospectus. The net proceeds are to be domiciled with a Custodian in an escrow account specifically opened for this purpose and the issuer and the Trustees are to be signatories to the account.

The bond proceeds are to be applied within the timeframe stated in the prospectus made available by the issuer. In the event that there are unallocated bond proceeds, the proposed Rules require Trustees to invest such proceeds in money market instruments with investment grade rating that include projects which are consistent with the delivery of positive social outcomes especially but not exclusively for a target population(s).

## Reporting

Transparency is key when discussing and assessing the impact of a social bond. To this end, an issuer is required to provide a Social Bond Report to the Securities and Exchange Commission and any Exchange where the social bond is listed. This report is to be provided at least annually and shall cover the following:

1. The projects and assets to which bond proceeds have been allocated;
2. The expected impact of the project and assets;
3. Qualitative performance indicators and, where feasible, quantitative performance measures of the impact of the projects;
4. The methodology and underlying assumptions used to prepare performance indicators and metrics.

The proposed Rule goes further to require an issuer to publish an assessment report on its website or other media. This assessment report is to be issued by an independent professional assessment or certification agency. An issuer is expected to also make available the report on follow-up assessments of the projects funded by the bond and its impact.

## Refinancing

If an issuer intends to allocate a portion of the bond proceeds towards refinancing existing social assets, the prospectus must contain the details of the portfolio/assets/projects to which refinancing would apply.

## External Review

As part of efforts to strengthen transparency, the proposed Rule makes provision for external review of social bonds offered by an issuer. This review may be partial or full. Under the Rule, an issuer shall appoint an external review provider to confirm the alignment of the proposed bonds with all components of Social Bond Principles. The International Capital Market Association identifies the four components of Social Bond Principles as follows:

1. Use of proceeds;
2. Process for project evaluation and selection;
3. Management of proceeds;
4. Reporting.<sup>4</sup>

## Remarks

With social bonds, the focus is on an anticipated social outcome. Through this mechanism, societal development can be achieved with the involvement of private-sector investors. Thus, the proposed New Rule on Social Bonds is a welcome development by the Securities and Exchange Commission particularly in view of the current realities of the Nigerian economy.

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<sup>4</sup> <https://www.icmagroup.org/assets/documents/Sustainable-finance/2021-updates/Social-Bond-Principles-June-2021-140621.pdf>

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