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Does the Finance Bill 2022 advance Nigeria's ESG Ambition?

Background

The Federal Government of Nigeria reintroduced the annual Finance Bill in 2019 as a tool to effect fiscal changes that will drive the country's short to medium term macroeconomic objectives. Three of such bills have been signed into Acts so far and the fourth, the Finance Bill 2022, is expected to be signed soon.

It is heartwarming that Nigeria has made commitments to contributing to an environmentally and socially sustainable world through various declarations and partnerships in the past few years. During COP 26 in Glasgow in 2021, the Nigerian government reaffirmed its commitment to achieving net zero by 2060. Sequel to that, the Nigerian Energy Transition Plan (ETP) was launched in August 2022. Also in 2021, the Climate Change Act was passed. The Act seeks to provide a framework for achieving reduced carbon emissions and incorporate climate consciousness into national programmes.

Finance Bill 2022 and ESG

One of the policy drivers of the Finance Bill 2022 is climate change and green growth. Pursuant to that goal, the Bill proposes stiffer penalty for gas flaring by increasing the rate of company income tax for companies that flare or vent natural gas except in emergency situations. It also incentivises upstream gas development through the proposed introduction of the gas investment tax allowance.

Nigeria has an abundant reserve of natural gas and the government has identified it as key to its energy transition plan. Although natural gas is a fossil fuel, it is the cleanest fossil fuel. Yet, gas flaring is a major source of pollution in the oil producing region of Nigeria. This move by the government to further sanction gas flaring is therefore a welcome development from an environment standpoint. There are concerns about multiple and unaligned flaring prevention rules in Nigeria which could potentially create confusion for businesses. Nonetheless, protection of the environment remains very important.

Other than the provisions on natural gas, the Finance Bill 2022 does not have any other provision that directly advances Nigeria's sustainability ambition. However, provisions such as the proposed separation of the leadership of the management team of the country's tax administration agency from that of the board overseeing the agency are a welcome development for governance. Any measure that encourages independent oversight of public institutions and private organizations is a plus for ESG.

How did the previous Finance Acts fare on ESG scale?

The Finance Act 2021 did not have any provision that directly impacts the environment pillar of ESG. It only streamlined the claim of incentives available for gas utilization. The Petroleum Profits Tax Act (PPTA), Companies Income Tax Act (CITA) and Industrial Development (Income Tax) Relief Act (IDITRA) all have different incentives for gas utilization. Section 39 of CITA gives companies utilising natural gas a tax break of up to 5 years. The IDITRA also lists natural gas as one of the products that are eligible for tax holiday of up to 5 years. Prior to the Finance Act 2021, some companies claimed both incentives. The Finance Act 2021 now forbids companies from claiming any other tax break if they claim the section 39 gas utilization incentive.

By providing statutory backing for electronic exchange of documents, including tax assessment notices and objections by taxpayers, the Finance Act 2020 is playing a role in contributing to the reduction of paper wastage. MDAs in Nigeria are particularly notorious for having heaps of papers in their offices. The amendment of the CITA by the Finance Act 2020 to permit electronic exchange of statutory documents is healthy for the environment.

The Finance Act 2020 also has provisions such as tax exemption for workers earning minimum wage and exemption of compensation payment of up to NGN 10 million for loss of office from capital gains tax. By reducing the burden of low income earners and employees who lost their jobs, the Finance Act 2020 is contributing to the social pillar of ESG which is very important to attaining a sustainable and fair society.

The Finance Acts do not introduce a new piece of legislation. They only amend provisions of existing laws or introduce new provisions in existing laws. A new legislation still has to go through the entire lawmaking process. The Climate Change Act is an example in this context.

Although not much has been done with Finance Acts in moving Nigeria towards environmental and social sustainability, there have been some modifications to existing laws that seem to promote Nigeria's ESG ambition. The controversial VAT Modification Order 2021 added renewable energy equipment to the list of goods exempted from VAT in the First Schedule of the Value Added Tax Act. However, batteries for solar panels are not specifically exempt. Batteries are the most expensive component of a solar-powered renewable energy system. Exempting solar panels alone from VAT without including a very important component like batteries suggests there is a gap between relevant government agencies drafting tax incentives and the industries the incentives are intended to support.

IDITRA exempts waste production and disposal, manufacture of solar home electronic systems and electricity generation through renewable sources from income tax for up to 5 years. However, the same law also incentivises mining of coal, the dirtiest energy source.

What can we learn from other jurisdictions?

Africa contributes the least to global carbon dioxide emissions, but the continent is not immune to the consequences of climate change. It is also a thing of pride to be part of the move towards an environmentally safer world. Yet, Africa has abundant monetizable resources that could help its economy.

Unfortunately, the exploitation and utilization of some of these resources have adverse environmental effects. The concept of Just Energy Transition seeks to strike a balance between these conflicting realities and forces. We believe it is achievable.

Beyond the environment, Nigeria, and by extension Africa, even needs more actions on other pillars of ESG. Social and governance issues like pay, gender issues, business ethics, health and safety, diversity and responsible use of taxation need serious attention.

As a way of saving the environment, countries of the world are beginning to introduce green taxes and incentives1. Green taxes are taxes that seek to discourage production or consumption activities that harm the environment or encourage activities that protect the environment. These include taxes on pollution, energy, carbon emissions, waste production and disposal, motor vehicles etc. Green incentives are financial incentives, such as cash grants and tax liability reduction schemes, to encourage projects and investments that mitigate environmental harm.

According to PwC's Green Tax and Incentives Tracker, 19 countries have taxes that qualify as green taxes and 20 countries have incentives that qualify as green incentives. Nigeria does not have any standalone tax or incentive that qualifies for such taxonomies.

Conclusion

From a fiscal standpoint, it is clear that ESG still remains a nice-to-have rather than a must-have for economic agents in Nigeria. Before it becomes a culture, ESG may require enforcement through legislation. The passage of the Climate Change Act and the setting up of the Energy Transition Office are good developments. But Nigeria still has a lot to do to move towards sustainability. There are several existing laws in Nigeria that only require amendments to fit them into broader sustainability goals. The annual Finance Acts can be a veritable tool to achieve that. Future Finance Bills should place higher priority on green incentives.

Reference

1. https://www.pwc.com/gx/en/services/tax/green-tax-and-incentives-tracker.html

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