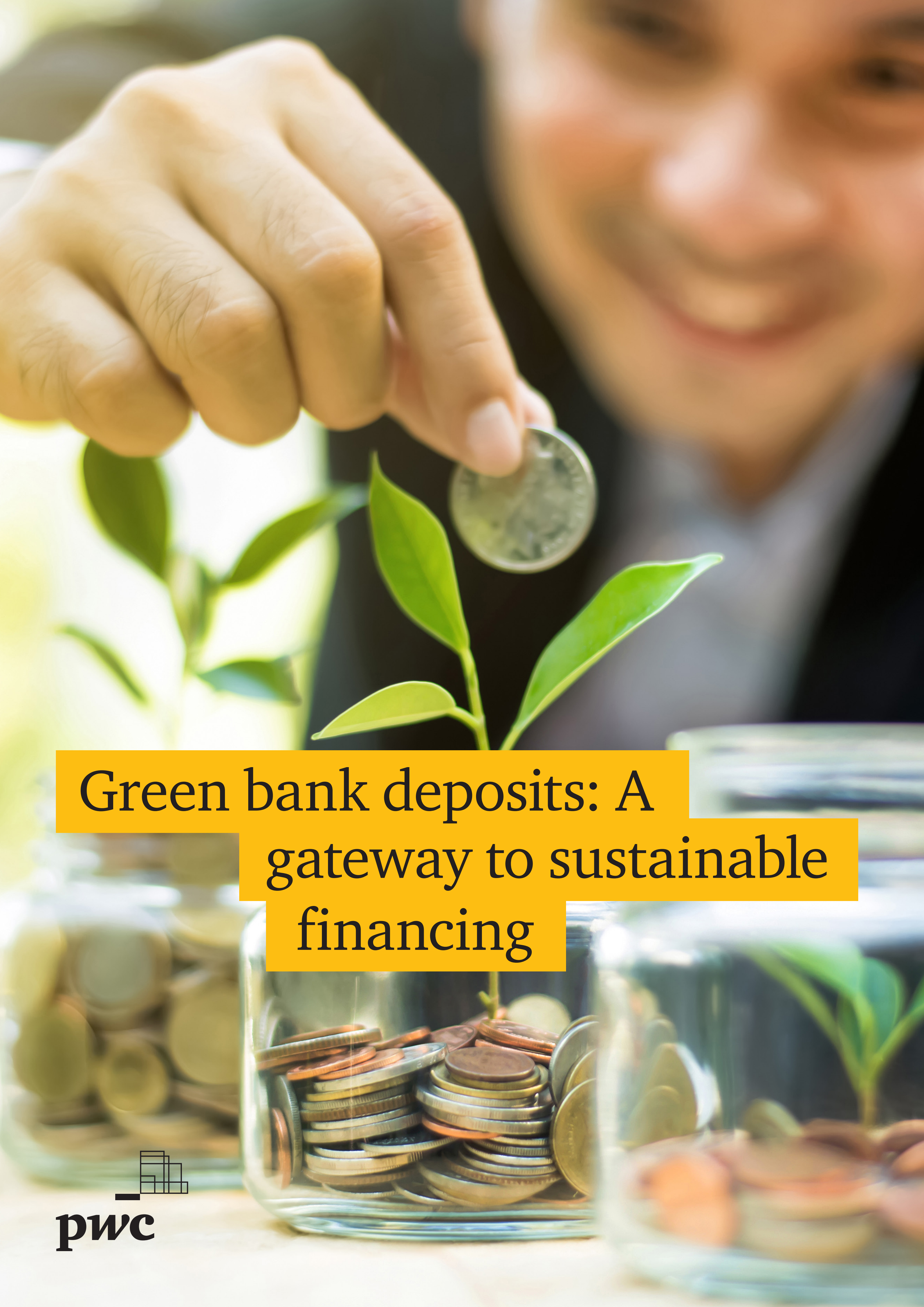
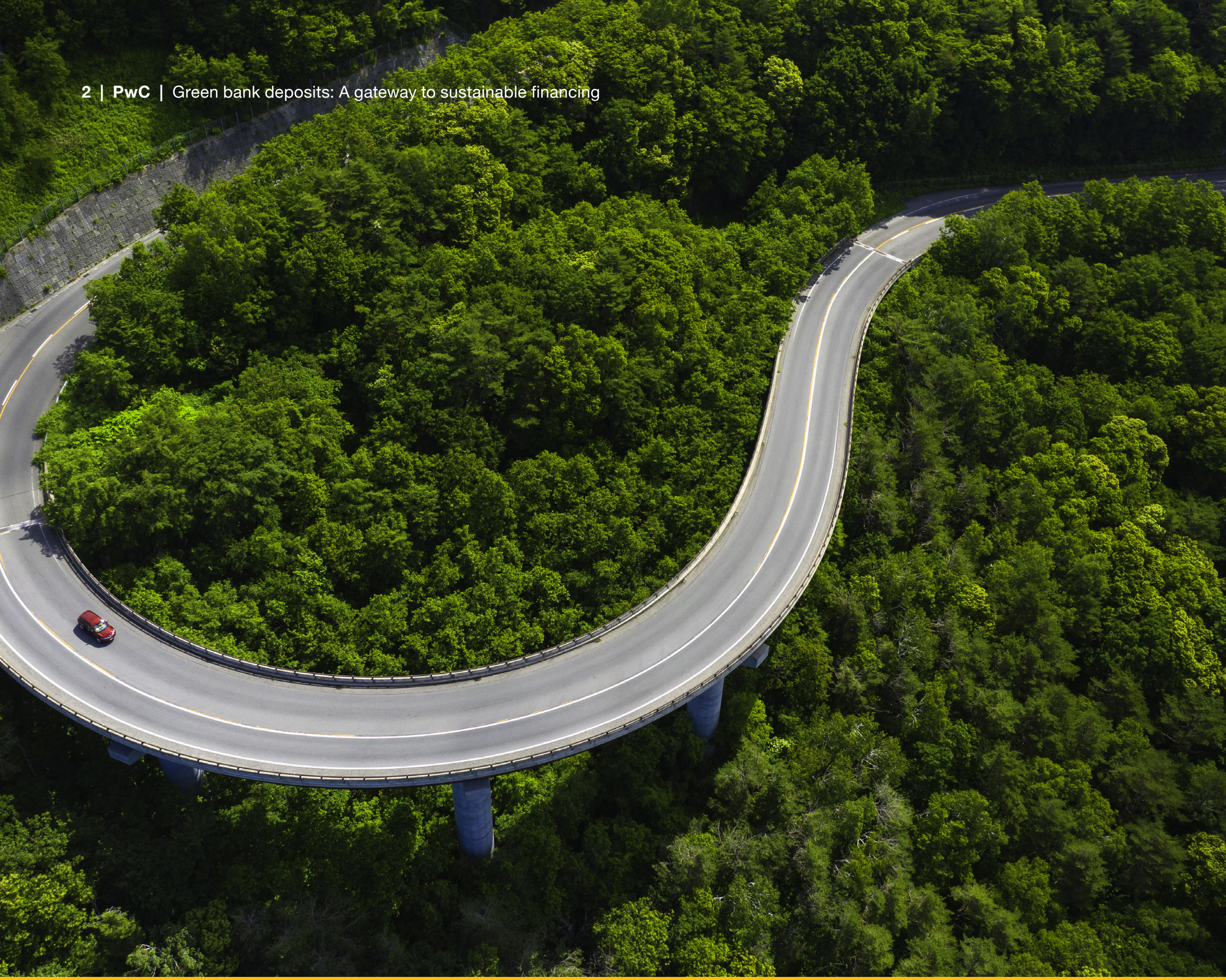


Green bank deposits: A gateway to sustainable financing



Introduction

On 11 April 2023, the Reserve Bank of India (RBI) released a circular on ‘Framework for the acceptance of green deposits’. This circular supplements the RBI’s ‘Report on the survey on climate risk and sustainable finance’, ‘Discussion paper on climate risk and sustainable finance’ and ‘Framework of sovereign green bonds’ issued by the Government of India. The framework’s objective is to aid depositors to achieve their sustainable agenda, address greenwashing concerns and facilitate flow of credit to green projects. These deposits would be interest-bearing and received by the regulated entities (REs) for a fixed duration, the proceeds of which are earmarked to be used for the purpose of financing green projects alone.

The list of green activities/projects is defined in the circular, and the same has to be considered for selecting green projects till the time green taxonomy is finalised by the RBI. The list includes activities in the areas of energy efficiency in resource utilisation, reducing carbon emissions and greenhouse gases (GHGs), promoting climate resilience and/or adaptation and value, and improving natural ecosystems and biodiversity.

Operationalisation framework at a glance

The framework can be split into some key components as illustrated below.

Board-approved green deposit policy

Use of proceeds
green activities/projects that could be financed by the RE in accordance with the permissible list of activities

Project evaluation and selection
by the RE, including the monitoring and validating the sustainability information provided by the borrower

Management and allocation of proceeds
to measure and track the allocation of proceeds and temporary use of funds

Reporting
the selected impact indicator and the use of proceeds until its full allocation

List of green activities as per the RBI framework

Who prepares, recommends (e.g. sustainability committee, green finance officer, etc.) and approves green projects (e.g. credit manager)

Steps/guidelines on how to manage use of proceeds, including supervision, tracking and ring-fencing of proceeds

Description of how to track and report use of proceeds and impact indicators per eligible use of proceeds

Green deposit financing framework

Third-party review/external assurance

Green deposit information for stakeholders/investors

Annual impact assessment report

Track and report use of proceeds (investment amount) per eligible use of proceeds.

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List impact indicators to be used to report impact per project type (e.g. waste reduced, GHG emissions saved,etc.).

Reporting and disclosure

Important timelines

Applicable from 1 June 2023 ⟶ Impact assessment mandatory from FY25

Global benchmarking of sustainable financing initiatives

Globally, there are multiple accepted guidelines on green bonds and sustainable finance – including the ICMA Green Bond Principles 2021, Social Bond Principles 2021, Sustainability Bond Guidelines 2021, LMA Green Loan Principles 2021, Social Loan Principles 2021 and the EU taxonomy. These global frameworks can act as a guide to form similar guidelines relevant to the Indian context to help REs formulate their policies around sustainable financing.

Although green (linked) bonds are more popular globally for raising funds towards sustainable financing, there are a few banks that have policies around green deposits as well.

In the Indian context, several public and private banks offer green deposits and have frameworks in place to identify and finance sustainable initiatives through standard products like green, social and sustainability linked loans.

Issuance of the RBI guidelines will help in standardising and improving comparability on sustainable financing across REs. The requirement of the guideline to publish the use of proceeds for the deposits raised will increase competitiveness among the REs, and lead to better product offerings. Further, for stakeholders focusing on improving their environmental, social and corporate governance (ESG) performance, these guidelines will be instrumental in increasing transparency and visibility. The requirement for an impact assessment report will also pave the way for REs to start measuring their scope 3 emissions, thus taking the first step towards the net zero goal.

Key challenges and the way forward

1. Asset liability mismatches (ALM): Capital-raising activities for long-term projects must be based on instruments of similar tenor to avoid ALM mismatches. Any deposit scheme catering to green agendas must be cognisant of tenor and must be designed accordingly. REs may choose to keep longer lock-ins or offer higher interest rates to make these deposits more attractive for retail depositors.

2. Lower uptake: Given the large size of the domestic market and much smaller penetration of green instruments so far, there are many opportunities that remain to be tapped. To meet India's target of achieving net zero emission by 2070, it is crucial to mobilise household savings, as a substantial part of the deposits comes from household savings. Thus, REs have a unique opportunity to increase the retail participation of India's green ambition, and in turn, provide alternate saving options for retail investors.

3. Treatment of existing green deposits/funds: The framework does not specify how the existing green deposit schemes or other schemes funding the green agenda will be treated under it. As of now, funding for renewable energy projects is permissible under the priority sector lending requirement. There is no explicit grandfathering approach mentioned in the framework to this extent.

4. Taxonomy: A formal definition is an important requirement. Green taxonomy would help REs to better assess the climate risk in their loan portfolios, scale up green and sustainable finance and mitigate the risk of greenwashing.

5. Enhancement in data, system and process: Incorporating ESG-specific parameters in the evaluation of borrowers, into the rating models of the REs, is necessary to ensure a robust borrower evaluation. This would also require a revision of the credit-appraisal process of the FI. Moreover, the development of additional system requirements to enable the continuous capture of ESG-specific information, to enable effective impact assessment and a robust reporting framework, is needed.

6. Governance: Board oversight and supervision will play a crucial role in achieving the strategic objectives. The RBI has recognised the importance of effective governance in the framework. Going forward, setting the right tone will be important, and REs will need to invest in people and resources who have the right expertise to drive the agenda forward.

7. Impact on liquidity ratios: Depending upon how REs positions their green deposits (CASA or term deposits), there might be an impact on liquidity ratios. Term deposits with premature withdrawal options might increase the outflow of deposits, which in turn will impact the liquidity ratios.

How PwC can help

PwC has always been at the forefront to identify emerging climate risks, where we assist organisations in leveraging their capabilities. REs have a key role to play in driving the green agenda forward and mitigating climate impact. Furthermore, REs can be instrumental in limiting access to funds for sectors contributing to high GHGs and providing access to capital for sectors that will lead to lowering of the GHGs. In addition to risk, there are opportunities that can be leveraged in terms of access to green deposits, green finance and raising capital for new technologies that will promote carbon neutrality. Therefore, we follow a five-step approach to assist REs to identify and set-up the green foundation transparently, in an effective manner.

	Setting-up the green foundation		**Ensuring transparency and effective execution**		
	Green deposit policy	**Financing framework (FF)**	**Impact assessment**	**Third-party verification**	**Reporting and disclosure**
Regulatory guidance	Board-approved policy on issuance and allocation of green deposits	Board-approved FF for effective allocation of green deposits	To be carried out annually with assistance of external firms to measure and publish impact associated with green lending	To be carried out annually by third party on the allocation of green deposits	Annual review report to be put up to board on the deposits raised and end use of funds
Key offerings	**A comprehensive green deposit policy** which will include but not be limited to: • governance structure • guidance on product offerings, which include denomination, interest rate and tenor of deposits • roles and responsibilities.	**Benchmarking** with international best practices and equivalent green financing standards **Defining the criteria/checklist for selection of green projects** under eligible categories **Defining policy guidelines around** • use of proceeds risk identification, assessment and monitoring defining impact indicators and thresholds.	**Defining impact indicators –** qualitative and quantitative – for each green deposit category **Creating a logical data dictionary** for necessary fields/information to be captured to measure impact indicators Assisting in the aggregation of this information and publishing the **impact assessment report**	Third-party verification report which will include: • initial **planning and review** of policies • **evaluation of design** of key structures, systems and processes for managing and reporting the use of proceeds • **performing substantive testing** selectively, to check that the identified assets adhere to the framework	**Internal reporting and steering** • Development of reporting templates, dashboards and management information system (MIS) • **External reporting and assurance** • **Stakeholder communication**

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