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Insight

Ajay Goel
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P14

5th Annual Pharma Legal & Compliance Summit 2016

7th October 2016, NOVOTEL, Juhu Beach, Mumbai P40

5th Annual Media, Advertising & Entertainment Legal Summit 2016

20th October 2016, Le Meridien, New Delhi P44

Defogging the Cloud for The Indian Inc. BFSI

An Overview of the Round Table Series by Lex Witness & Microsoft P28

Litigation Management – A Dire Need

A Coffee Table Conversation between Anindya Majumdar - Head Legal, Meru Cabs and Parimal Chanchani, Director, Uberall Practice League P31

expert speak

Hardeep Sachdeva
Senior Partner
AZB & Partners

Anshmuan Singh
Senior Associate
AZB & Partners

P35

GST & The Indian Taxation Platter

P08 Getting all Spices Together? Are We Ready?

expert speak

Girish Rawat
Partner
Dhir & Dhir Associates

Surbhi Narang
Associate
Dhir & Dhir Associates

P20

expert speak

Dr. Manoj Kumar
Founder
Hammurabi & Solomon

P39

Let's arbitrate

S. Ravi Shankar
Senior Partner
Law Senate

P37

The Indian Saga of Green Bonds

Girish Rawat & Surbhi Narang

The introduction of Green Bonds promises to resolve the issues of funding in the fast evolving renewable energy sector. India has set an ambitious target of 175 GW of renewable energy by 2022 and an estimated investment of US$200 Billion is required to achieve the said capacity. The unavailability of funds is perceived to be the principal roadblock in achievement of the said target. The Green Bonds offer an ideal solution by emerging as a major source of funding for the renewable sector.

UNDERSTANDING 'GREEN BONDS' IN INDIAN ECONOMY

A green bond cannot be defined in specific terms. In common parlance, a Green Bond is a type of bond instrument where the proceeds are applied exclusively to finance or refinance new and/ or existing eligible green projects such as renewable and sustained energy, sustainable water management, clean transportation etc. However, functionally a Green Bond is like any other conventional bond issued by an issuer for raising funds from the prospective investors. In other words, a Green Bond is a conventional bond with green features.

RELEVANCE OF GREEN BONDS IN INDIAN ECONOMY

Along with India's ambition of renewable energy production and investment by the year 2022, India's Intended Nationally Determined Contribution (INDC) has set targets for India's contribution towards climate improvement and following a low carbon path to progress. Lack of sufficient funds is hindering the growth trajectory. Traditionally, similar to any other infrastructure sector projects, banks and non-banking finance companies have been the primary source of funding for renewable energy. However, the banks will have limited appetite for a major role as providers of long-term debt for renewable energy projects as they are weighed down by the risk of an asset-liability mismatch. The long-term funds available with insurance and pension funds in India are not being adequately channelized to meet the debt requirement of the renewable energy sector due to the regulatory restrictions.

Thus, the existing traditional financing sources may not be sufficient to support

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capacity addition, and given the huge financial requirement of the renewable energy sector, there is a dire need to identify alternate sources to supplement and widen the channels of renewable sector funding.

Green Bond, as a part of corporate bonds is a fast emerging source for clean energy capital. Green Bonds enable the issuers to tap into a global and domestic pool of fixed income capital, and attract investor groups who have focussed interests in sustainability and responsible investment and whose investment guidelines allow them to invest in different qualities of Green Bonds.

The key benefits of issuing the Green Bonds are:

i. Investor diversification: Green bonds help the issuer to expand funding sources and limiting the dependency on specific markets by such issuers. In particular, Green Bonds have attracted investors from the growing segment focused on sustainable and responsible investing (SRI), investors that fall under the ESG (Environmental, Social, and Governance) criteria and other investors, whose investment guidelines may allow investing in different qualities of Green Bonds.

ii. Positive public relations: Green bonds also helps raise awareness about issuers' environmental programs and thereby, improves the reputation of the issuer offering the Green Bonds.

iii. Potential for pricing advantage: The green label to these bonds, can bring in pricing advantage. The Green Bonds have a high potential to mobilise domestic and foreign capital for renewable energy on better financing terms, including lower interest rates and longer repayment schedules, while meeting the environmental targets of the investors.

THE LINEAGE OF GREEN BONDS

In 2007, European Investment Bank issued first climate- focused bond in the form of a structured product. In 2008, the World Bank issued the first bond labeled "Green" for mainstream investors with a fixed coupon. By 2010, they were joined by various other multilateral agencies such as the IFC and by public entities (governments, agencies and municipalities) in issuing a total of about US$4 Billion worth of climate-focused bonds. The annual global issuance of Green Bonds havegrown by more than 35 times to US$ 37 Billion within first seven years since its first launch. [1]Moody's reported in February 2016 that Green Bond issuance for 2016 could exceed US$ 50 Billion[2].

Overall, Europe hosts the highest number of Green Bonds, with nearly US$ 18.4 Billion issued in 2015. About US$ 10.5 Billion came from the U.S, where the market was mainly driven by municipal green bonds. U.S surpassed supranational institutions and is the largest Green bond issuing country in 2015. Sevennew countries including India joined the Green Bond market in 2015 jointly raising Green Bonds worth US$ 3.2 Billion.[3]

INDIA'S TEMPERAMENT OF GREEN BOND

India is poised to attain greater heights in this emerging market. We have witnessed a steady rise in the last eighteen months. According to Natural Resources Defense Council (NRDC), India's Green Bond investments raised US$ 1.1 Billion in 2015, showing great prospects in its first year. Yes Bank issued India's first euro denominated "Green Bond" of INR 10 Billion in February 2015, and followed up with another issue of INR 3.15 Billion Green Bond in August, 2015. Yes Bank's second issue was entirely subscribed by the International Finance Corporation (IFC). IFC then financed the said investment by issuing a "Green Masala Bond" (an Indian Rupee denominated bond sold overseas) which was also a first. In March 2015, the EXIM Bank issued India's first dollar denominated "Green Bond" of US$ 500 Million. In September 2015, CLP Wind Farms (India) issued India's first "Corporate Green Bond" of US$ 90.3 Million to fund 150 MW of wind power. Further, IDBI Bank Limited raised Green Bonds of US$ 350 Million for renewable energy projects. In February 2016, Hero Future Energies issued India's first certified climate bond and raised US$ 44 Million to finance the

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development of wind energy projects in India.[4]

Recently, NPTC Limited became the first Indian corporate to offer Green Masala Bonds with certification from Climate Bonds Initiative and raised INR 20 Billion through Rupee denominated bonds from the offshore market.

THE REGULATORY RHYMES

The SEBI (Issue and Listing of Debt Securities) Regulations, 2008 ("SEBI Debt Regulations") governs the public issue of debt securities and listing of debt securities issued through public or private placement route, on a recognised stock exchange in India.

While, on-shore Green Bonds could have been issued and listed under the SEBI Debt Regulations, however, in the absence of clear directions or provisions in the SEBI Debt Regulations there was an ambiguity as to what would constitute a Green Bond and what is the process required to be followed. With the object to bring about uniformity regarding the Green Bonds and to remove future confusion around the subject matter, the SEBI in its meeting held on January 11, 2016 approved the new norms for issuing and listing of 'Green Bonds'.

Although the process of issuing Green Bonds is generally the same as issuing other corporate bonds, there are few additional disclosures pertaining to the periodic reporting of fund allocation. The issuer would have to make disclosures including use of proceeds, list of projects to which Green Bond proceeds have been allocated in the annual report and periodical filings made to the stock exchanges. The other salient features are as under:

i. The issuance and listing of Green Bonds shall be governed by the existing SEBI regulations for issuance of Corporate Bonds i.e. SEBI (Issue and Listing of Debt Securities) Regulations, 2008. However, the issuers of the Green Bonds will have to make incremental disclosures/ follow procedures.

ii. The definition of Green Bonds may be prescribed by SEBI from time to time. However, caution must be exercised in defining the green label for such bonds and should be in line with the international guidelines and investors expectations.

iii. Requirement of independent third party reviewer/ certifier/ validator, for reviewing/ certifying/ validating the pre-issuance and post-issuance process including project evaluation and selection criteria, to lend credibility to the issuance of Green Bonds. However, given the fact that the availability of such third party reviewer/ certifier/ validator in India is not adequate and globally such review is not mandatory, the same has been kept optional by SEBI.

iv. Escrow account for tracking the proceeds of the Green Bond is not made mandatory by SEBI. However, issuer is required to provide the details of the systems/ procedures to be employed for tracking the proceeds of the issue, including the investments made and/or investments earmarked for eligible projects and the same shall be verified by the external auditors.

The above measures are expected to facilitate investment decisions of the investors who have a mandate to focus on green investments and will also provide uniformity in disclosure sConclusion

The global Green Bond market is growing rapidly and India is garnering international attention in the form of foreign investment to finance various ongoing projects.

These bonds can not only be raised off-shore but on-shore as well by financial institutions, private sector or public sector organisations. The Government of India has ambitious plans to promote the renewable energy and achieve 175 GWof renewable energy by 2022, for which an estimated investment of US$200 Billion is required. The green bonds are likely to play an important role in realising the same.

[1] World Bank, World bank Green Bonds, June 2015
[2] https://www.moodys.com/research/Moodys-Green-bond-issuance-could-exceed-50-billion-in-2016--PR_343234
[3] http://www.climatebonds.net/files/files/2015%20GB%20Market%20Roundup%2003A.pdf
[4] Interim Report: Greening India's Financial Market by Natural Resources Defense Council and Council on Energy, Environment and Water