"THE ERA OF GREEN FINANCE SOCIALLY RESPOSIBLE INVESTING"

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Earth provides enough to satisfy every man's needs, but not every man's greed."

" **Mahatma Gandhi**

stract- As per the new Companies Act 2013, corporate social responsibility is emerging as a catalyst in socio economic development of the country. Due to the provisions of corporate social responsibility, it is evolving as a new tool of social development. Green finance represents a wide-ranging challenge to the traditional constructs of financial law. New green instruments threaten to transform conventional investment practices (ethical investment), lending standards associated with project finance (environmental/social impact assessment), and accounting conventions (green/social reporting). To a large extent this process was inspired by civic forces: environmentally-socially conscious citizens, environmental groups and private financial institutions. International organisations such as the World Bank and UNEP added further impetus to this process. From a legal perspective the phenomenon of green finance reflected a highly patchy social process, constituted by segregated contractual instruments and uncoordinated organisational routines.

Keywords: Green banking, green finance, Sustainability, Green counter

I. INTRODUCTION

Green financing is a term which is trending these days. Significant evidence was traced in 2007 when business week reportedly said that a 15 fold rise was there in sustainable mutual fund investment. There is a shift from capital formation to energy efficiency investments. In 1980s and 1990 the focus of investments was mostly on economically viable projects. But this is the era when the focus has been shifted to environmentally viable projects. There are many companies which are following green finance concept so as to sustain in long run.

The major objective of this paper is to study several aspects of green financing with respect to Indian scenario and it would also verify the practicability of green financing in Indian banking Sector. Green financing is now becoming a trending concept in the Industry. Besides all the facts the public is also demanding a company to be environmentally sensitive. Due to this reason many business houses have already started green financing. But this is indeed a crucial time for the companies to cope up with the norms of green financing.

II. IMPORTANCE OF GREEN BANKING

Until recently, environmental concerns were not considered relevant to the business operation of banks and financial institutions. Traditionally, banking sector's concern for environmentally degrading activities of clients is like interfering or meddling in their business affairs. However, now it is being perceived that dealing with environment brings risks to their business. Although the banking and financial institutions are not directly affected by the environmental degradation, there are indirect costs to banks. Due to strict environmental disciplines imposed by the competent authorities across the countries, the industries would have to follow certain standards to run their business. In the case of failure, it would lead to closure of the industries leading to a likelihood of default to the bank. For example the enactment of Comprehensive Environmental Response, Compensation and Liability Act in 1980 (CERCLA) in the US in late 1980s has resulted in huge loss to the banks in the US as banks held directly responsible for the environmental pollution of their clients and made to pay the remediation cost. This is the reason for which banks in the US are ahead of other countries in integrating environmental concerns into their business operations. In the recent years several other countries (more in Europe) are seen adopting policies that have made banks responsible for the misdeeds of their clients. Therefore, the financial institutions need to engage proactively with the stakeholders on environmental and social policy issues and evaluate the impacts of their client's investment. In turn, that would force the customers to take care of their management of environmental and social policy issues relating to investment. This should cover all project financing activities across all industries. The importance of Green Banking is immense for both the banks and economy by avoiding the following risks involved in banking sector.

A) Credit Risk

It can arise indirectly where banks are lending to customers whose businesses are adversely affected by the cost of cleaning up pollution or due to changes in environmental regulations. The cost of meeting new requirements on emission levels may be sufficient to put some companies out of business5 . Credit risks may be higher due to the probability of customer default as a result of uncalculated expenses for capital investment in production facilities, loss of market share and third party liability claim. Credit risks are also associated with lending on the security of real estate whose value has diminished owing to environmental problems (additional loss in the event of default). Further, risk of loan default by debtors due to environmental liabilities because of fines and legal liabilities and due to reduced priority of repayment under bankruptcy. In few cases, banks have been held responsible6 for actions occurring in which they held a secured interest

B) Legal Risk

It can occur in different forms. Most obviously, banks like other companies are at risk if they themselves do not comply with relevant environmental legislation. But more specifically, they are at risk of direct lender liability for clean up costs or claims for damages if they have actually taken possession of contaminated or pollution causing assets. An environmental management system helps a bank to reduce risks and costs, enhance its image and take advantage of revenue opportunities.

C) Reputation Risk

In all likelihood, due to growing awareness about environment safety, banking institutions are more prone to loose their reputations if they are involved in big projects, which are viewed as socially and environmentally damaging. There are also few cases where environmental management system has resulted in cost savings, increase in bond value etc (Heim, G et al, 2005). In few cases the environmental management system resulted in lower risk, greater environmental stewardship and increase in operating profit. Reputation risks involved in the financing of ecologically and ethically questionable projects. The adoption of green banking strategies will help the bank to deal with these risks involved in their business operation. Green banking strategies involves two components

1) managing environment risk and

2) identifying opportunities for innovative environmentally oriented financial products (IFC, 2007).

To manage environmental risk, the banks have to design proper environmental management systems to evaluate the risks involved in the investment projects. The risks can be internalized by introducing differential interest rates and other techniques. Moreover, bank can withdraw itself from financing high-risk projects. The second component of green banking entails creating financial products and services that support commercial development with environmental benefits. These includes investment in renewable energy projects, biodiversity conservation, energy efficiency, investment in cleaner production process and technologies, bonds and mutual funds meant for environmental investments etc

The banking and finance industry influences economic growth and development, both in terms of quality and quantity, leading to a change in the nature of economic growth. Therefore, banking sector plays a crucial role in promoting environmentally sustainable and socially responsible investment. Banks may not be the polluters themselves but they usually have a banking relationship with some companies/investment projects that are polluters or could be in future.

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III. GREEN PRODUCTS AND SERVICES ON OFFER

A) Green Home Mortgages

These are special kind of mortgages for new homes which comply green energy consumption standards. The interest rate offered on these mortgages are usually 1-2% lesser than the market rate. In certain countries exemption from income tax can be claimed if an individual has opted for green mortgage product.

B) Green Commercial Building Loan:

Attractive loan designs and arrangements have emerged for “green” commercial buildings, characterized by lower energy consumption

(~15-25%), reduced waste and less pollution than traditional buildings.

C) Green Auto and Fleet loan:

With below market interest rates, green car loans aim to incentivize the uptake of cars that demonstrate low GHG intensity and/or high fuel efficiency ratings. The number of these products has increased in recent years, with the majority being offered in Australia and Europe.

D) Green credit and debit cards:

A broad family of green products includes debit and credit cards linked to environmental activities. “Green” credit cards offered by most large credit card companies, typically offer NGO donations equal to approximately half a percentage point on every purchase, balance transfer or cash advance made by the card owner. In September 2006, Rabobank launched an innovative ‘climate credit card’. The bank pledges to pay a proportionate sum to support WWF projects, depending on the energy intensity of the product or service bought with the card.

E) Green Mortgage Based Securities:

A “green” mortgage-backed security package mortgages on buildings that meet specific energy-use and environmental benchmarks. “Green” Mortgage-Backed Securities in the early stages of product design and discussion would hold energy efficient and environmentally-friendly commercial buildings. These “green” products could be rated higher and worth more than traditional mortgage-backed securities as a result of the operational savings and marketability, as well as other tangible and intangible benefits associated with “green” facilities; added value features that could result in better and cheaper access to capital for potential owners and investor in green building projects. However, like other lending scenarios related to “green” buildings, this scenario is highly dependent on the financial community being able to accurately measure and value savings and reductions associated with building “green.

F) Carbon Funds:

A carbon procurement vehicle (or carbon fund) is a collective investment scheme which receives money from investors and uses this money to buy carbon credits from, or invest into, greenhouse gas (GHG) emissions reduction projects, generally through the Kyoto.

Protocol’s CDM and Joint Implementation (JI) schemes. After a certain defined period, the carbon fund will then give investors carbon credits and/or cash in return.

G) Green Insurance:

The insurance sector can generally be divided into two categories: Life Insurance; and General (Non-Life) Insurance.“Green” insurance falls under the latter and typically encompasses two product areas:

1) Those which allow an insurance premium differentiation on the basis of environmentally relevant characteristics; and

2) Insurance products specifically tailored for clean technologies and emissions reducing activities. Mileage-based insurance is offered to vehicle owners. Discount is offered for hybrid and fuel efficient vehicles. Bank can also choose to offset vehicle’s annual emissions.

There are some issues which impede the growth of Green financial products. Green products have still not been able to position themselves as an economically viable option as many lower cost products exist in the market. Unlike of what is happening today in Europe, where the market of "green" financial products & services is growing substantially, globally, even though the market appears to grow, it is in an early stage, with indefinite boundaries and without having gained unified characteristics, differentiating it from the traditional industries.

IV. SMALL SCALE SECTOR IN INDIA AND GREEN BANKING

Industries irrespective of their size (large, medium or small) emit pollutants to the environment in which we all inhabit. Though the large-scale industries are more capable of degrading the environment, they have adequate financial resources to install pollution control equipment or waste treatment plants to control pollution. Moreover, these large-scale industries are always in the eyes of the government or the pollution control board, these industries strives hard to adhere to set emission standards. On the other hand, the small-scale industries (SSIs), on account of their financial constraints may not be able to unable to install the necessary equipment to meet the emission standards prescribed by the competent authorities. Also because of their small scale of operation, the SSIs escape from the eyes of the concerned authorities. SSI constitute major portion of Indian industry. These industries account for about 40 per cent of industrial production and 30% of total manufacturing exports. Use of western technological systems in small scale industries produce enormous gaseous, liquid and solid wastes. However, they may not be in a position to bear additional expenditures on account of environment audit and pollution control equipments. Therefore, banks need to apply different procedures to promote pollution controls like

(1) environmental pollution status of SSI

(2) environmental Clearance from the appropriate authorities and

(3) steps undertaken or proposed for disposal of solid, liquid and gaseous wastes before lending to SSI in India.

This is where the banks and financial institutions can extend the necessary financial support.where pollution is on account of inadequate financial capabilities. Realizing the difficulties faced II. by SSIs in maintaining environmental standards and its huge impact on economy and society, different state governments provide schemes to encourage small scale industries to adopt better environmental management practices such as:

• In order to improve the quality of raw materials and also finished products, the SSI units are allowed for testing facilities for products / raw materials and also to obtain the BIS Certificate etc.

• Grants and subsidies are given to an extent of 50% of the total for obtaining the ISO 9000 Series (equivalent Indian Standard IS 14000 Series) in many states.

However, SSIs are small but large in number. And most of the industries are in the unorganized sector. Therefore government and financial institutions must come forward to help these units financially to adopt expensive pollution control technologies developed in the other developed countries. However, the most practical solution to these large number of SSI enterprises would be developing low cost pollution abatement technologies, adopt mechanism from pollution control to pollution prevention activities and international cooperation. Government can further provide tax incentives and other financial help to SSIs to meet requirements.

V. ENFORCEMENT OF ENVIRONMENTAL MANAGEMENT AND ROLE OF THE GOVERNMENT

The financial institutions also should make sure that the customer is ready to comply with environment management plan during the construction and operation of the project and provides regular reports, prepared by in house staff and third party experts. There should be a direct communication between the lenders and monitoring group. However, much less attention is given for the environmental risk management after the post transaction period. Recently, western financial institutions use environmental criteria with credit risk management activities than with formulating overall lending or investment strategy. With the introduction of ISO 14000 and development of information network, it is easier now to the credit officers to compare firms and plants regarding their environmental management and measure the relative environmental liabilities and risks. Though commercial banking has been more attentive to the investment banking than the environmental problems, the environmental liabilities would play a larger role in their investment decision in the near future (Schmidheiny and Zorraquin, 1996). Further, the environmental audits are required to determine the environmental status of a facility, property, and operation and to identify regulatory compliance status, past present problems and potential environmental risks and liabilities associated with the project. These should be done by an independent body or by any environment investigation team. But to ensure all these work,, there should be legislation, which will enforce the standards along with training and demonstration skills. Government should enact legislation to force banks to consider producing a formal environmental policy statement and making this publicly available. Though Schmidheiny and Zorraquin (1996) conclude from their primary study that banks are not hindering the achievement of sustainability, banks can also play a hindering role for sustainable development because (1) they prefer short-terms payback periods where as sustainable development needs long-term investment (2) investment which take into account of environmental side-effects usually have lower rate of return in short-term (Jeucken and Bouma, 1999). Therefore, sustainable investments are unlikely to find sufficient funding within current financial markets. Thus, government must design proper legislation of environmental rules for banks and ensure enforcement

VI. GREEN BANKING IN INDIA

India is on a higher growth trajectory for last one and half decade and the industrial sector plays the most important role in India’s growth story. However, Indian industry faces the challenges of controlling environmental impact of their business i.e. reducing pollution and emission of their clients. Though government has been trying to address the issue by framing environmental legislations and encouraging industry to follow environmental technologies and 11 practices, they would not be enough given the poor track records of enforcement, public awareness and inability to derive competitive advantage by producing eco-friendly products. Incidentally, India's is the world's sixth largest and second fastest growing country in terms of producing green house gases. Delhi, Mumbai and Chennai are the three of the world's ten most polluted cities. The major polluting industries in India are

(a) primary metallurgical industries namely zinc, copper, steel etc.

(b) paper & pulp

(c) pesticides/insecticides

(d) refines (e) fertilizers

(f) tanneries

(g) sugar

(h) textiles

(i) chemicals/pharmaceuticals etc.

The banking operation and investment by financial institutions should take care of environmental management of these polluting industries by improving the overall environment, the quality and conversation of life, level of efficiency in using materials and energy, quality of services and products. In this context, the role of banking sector, which is on major financing sources to the Industries, assumes high importance. The environmental regulations in India can be broadly classified into two broad categories i.e. command and control regulations and liability law. The command and control regulations are ex ante regulations that are designed to dissuade environmentally damaging projects. This regulation is implemented by setting industry specific pollution standards, scrutinizing the projects and granting/denying permissions by the concerned authorities like Ministry of Environment and Forest. The liability laws are ex post in nature and are implemented by enforcing authorities through imposing fines, closing down the defaulting industries etc. However there is no law and rule in India that can hold banks responsible for scrutinizing investment projects before financing and for the environmental damage created by its client. Once legal framework for the environmental pollution standards are formulated in India, the polluting industries either have to close down or have to make necessary investment to comply with the standard. In this process these industries will loose their competitiveness in the international market, which would directly affect Indian economy and the banking sector. Thus in the present context, it is equally important for banks to guard themselves against the conversion of the now performing assets into non-performing one in the future. Realization of these facts by banks will certainty make them fast adopt the concept of Green Banking. The 12 industries, which are ill equipped to control pollution now, are the possible polluters of future. A day may come, when legislation may take a hard stance against these environmental culprits and may order the closer of these units. Almost 150 SSI units around Agra and Delhi were forced to close down for their non-compliance to the mandated environmental standards12. In such an eventuality, the industries cannot be rescued from becoming the non-performing ones, as the banking institutions continue to overlook these aspects.

Besides, the public is gaining consciousness of the multifarious problems associated with pollution. So, the public will resort to protest, strike, and agitation to stop the misuse of the environment or in a simple fashion consumers may reject the products produced by the polluting units. Before 1986, there was no provision for public to file a suit against the polluting units but now the citizens are also permitted to file suits. The present green consumerism is more concerned with the quality of the products more than the quantity. In future, market will reward those industries or the companies, which emerge as the efficient users of the energy and raw materials and will penalize the less efficient one. Further, the investors in the stock market are equally aware of environmental pollution and would take a stand against those

VII. CONCLUSION

In a rapidly changing market economy where globalization of markets has intensified the competition, the industries and firms are vulnerable to stringent public policies, severe law suits or consumer boycotts. This would affect the banks and financial institutions to recover their return from investment. Thus, the banks should play a pro-active role to take environmental and ecological aspects as part of their lending principle which would force industries to go for mandated investment for environmental management, use of appropriate technologies and management systems. Green Banking if implemented sincerely will act as an effective ex ante deterrent for the polluting industries that give a pass by to the other institutional regulatory mechanisms. There has not been much initiative in this regard by the banks and other financial institutions in India though they play an active role in India's emerging economy. The banking and financial sector should be made to work for sustainable development. As far as green banking in concerned, India's banks and financial institutions are running behind time. None of our banks or financial institutions haves adopted equator principle even for the sake of records. None of them are signatory to the UNEP Financial Initiative statement. It is time now that India takes some major steps to gradually adhere to the equator principles-guidelines that use environment-sensitive parameters, apart from financial, to fund projects.

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