BEYOND THE GREEN LABEL: EVALUATING THE PROPOSED GREEN BOND FRAMEWORK VIS-À-VIS GREENWASHING IN INDIA

Sandeep Parekh[*] and Rashmi Birmole[**]

ABSTRACT: *It is no secret that sustainable investing has long crossed the boundaries of a niche practice and is changing the face of finance as we know it. With the conversation around climate change and the transition to a low-carbon economy gaining pace, the wide financing gap in meeting India's climate targets and international commitments has become apparent. Having witnessed rapid growth in recent years, the green bond market is poised to mobilize capital for sustainable projects while generating fixed returns for investors. However, the integrity and development of the green bond market faces the risk of compromise on account of greenwashing practices, i.e., overstatement of positive environmental impact or use of proceeds towards projects with little or no environmental impact. These concerns were recently addressed by the Securities and Exchange Board of India in a Consultation Paper on Green and Blue Bonds as a mode of Sustainable Finance. Through this article, the authors attempt to critically analyze the proposals in the consultation paper from the lens of mitigating greenwashing practices in India. In doing so, the authors also put forth recommendations that may be considered regarding the proposals.*

KEYWORD: *Green Bonds, Greenwashing, Sustainable Investing, SEBI, Regulatory Framework*

[*] Managing Partner at Finsec Law Advisors, Mumbai.
[**] Associate at Finsec Law Advisors, Mumbai.

I. INTRODUCTION

Often termed the real growth story of the 21st century,[1] the transition to a low-carbon economy has been a fast-emerging priority and shared vision for countries across the globe since the Paris Agreement was adopted in 2015. Recently, in the 26th session of the Conference of Parties held in Glasgow, India submitted its Long-Term Low Emission Deployment Strategy to the United Nations Framework Convention on Climate Change, crystallizing key measures and setting out India's roadmap towards achieving the rather ambitious goal of achieving net zero emissions by 2070.[2] Like most things, the potential low-carbon transition comes at a cost and monumental investment needs.[3] The need to meet the existing financing gap and infrastructure deployment needs is considerable,[4] with the estimated expenses exceeding INR 11 lakh crores per year for India alone.[5] An innovative instrument within the sustainable finance ecosystem that rapidly bridges this gap and forms the focus of this article is the 'green bond'.

The Securities and Exchange Board of India ("**SEBI**") recently released a Consultation Paper on Green and Blue Bonds as a mode of Sustainable Finance ("**Consultation Paper**"),[6] to review the existing regulatory framework on green bonds. The Consultation Paper also focuses on the need to tackle the practice of channeling proceeds from green bonds to activities with minimal or negligible environmental impact, termed as 'greenwashing', to increase the overall accessibility of the green bond market to issuers and investors alike. Through this article, the authors attempt to analyze the proposals set out in the Paper from the perspective of mitigating greenwashing concerns and put forward recommendations that may be considered before implementation.

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[1] Srijana Mitra Das, *A clean economy is the 21st century's real growth story – India is central to this*, THE TIMES OF INDIA, (Nov 19, 2022), https://timesofindia.indiatimes.com/a-clean-economy-is-the-21st-centurys-real-growth-story-india-is-central-to-this/articleshow/95611519.cms.
[2] Press Release, Ministry of Environment, *Forest and Climate Change, India delivers National Statement at COP27* (Nov 15, 2022), https://pib.gov.in/PressReleasePage.aspx?PRID=1876119.
[3] MINISTRY OF ENVIRONMENT, FOREST AND CLIMATE CHANGE, INDIA'S LONG-TERM LOW-CARBON DEVELOPMENT STRATEGY, at 55, (2022), https://unfccc.int/sites/default/files/resource/India_LTLEDS.pdf.
[4] *Financing Climate Action*, UNITED NATIONS, https://www.un.org/en/climatechange/raising-ambition/climate-finance.
[5] Khanna N., Purkayastha D., Jain S., *Landscape of Green Finance in India*, CLIMATE POLICY INITATIVE (August 2022), https://www.climatepolicyinitiative.org/wp-content/uploads/2022/08/Landscape-of-Green-Finance-in-India-2022-Full-Report.pdf https://www.climatepolicyinitiative.org/publication/landscape-of-green-finance-in-india-2022/#:~:text=Green%20finance%20flows%20must%20increase,Net%2DZero%20emissions%20by%202070.
[6] THE SECURITIES AND EXCHANGE BOARD OF INDIA, CONSULTATION PAPER ON GREEN AND BLUE BONDS AS A MODE OF SUSTAINABLE FINANCE (Aug 2022), https://www.sebi.gov.in/reports-and-statistics/reports/aug-2022/consultation-paper-on-green-and-blue-bonds-as-a-mode-of-sustainable-finance_61636.html.

II. GREEN BONDS - AN EXPLAINER

Akin to regular bonds, green bonds are fixed-income instruments which provide risk-adjusted returns and raise debt capital for sustainable projects with favorable climate and environmental impact. As the name suggests, the proceeds of a green bond offering are earmarked for financing green projects and are popularly known as 'use for proceeds' bonds. Unlike regular vanilla bonds issued to finance the general working capital requirements of the issuer, the proceeds from green bonds are ring-fenced for allocation to green projects or assets. Regarding credit risk, green bonds are backed by the issuer's entire balance sheet, preventing investors from being directly exposed to the project's financial risks or assets financed by the green bond.[7]

III. EXISTING REGULATORY FRAMEWORK

Green bonds were initially viewed as innovative instruments in the infrastructure financing space. They were considered to fall within the ambit of debt securities governed under the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 ("**ILDS Regulation**s") as reflected in the Concept Paper on Issuance of Green Bonds ("**Concept Paper**"), released by SEBI on December 03, 2015.[8] The Concept Paper proposed the inclusion of enhanced disclosures for green bond issuances in addition to the existing requirements under the ILDS Regulations. These enhanced disclosures largely mirrored the Green Bond Principles ("**GBP**"),[9] a globally recognized best practice for promoting transparency and disclosure in green bond issuances, published by the International Capital Markets Association.

The proposals set out in the Concept Paper aligned with the critical components of the GBP, i.e., disclosures relating to the use of proceeds, the process for project evaluation and selection, management of proceeds and reporting requirements. The framework governing green bonds was further formalized through the SEBI circular on Disclosure Requirements for the Issuance and Listing of Green Debt Securities on March 30, 2017.[10] The said Operational Circular

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[7] Aaron Maltais & Björn Nykvist, *Understanding the role of green bonds in advancing sustainability*, 11 JOURNAL OF SUSTAINABLE FINANCE & INVESTMENT 1, 1 (2021).

[8] THE SECURITIES AND EXCHANGE BOARD OF INDIA, CONCEPT PAPER FOR ISSUANCE OF GREEN BONDS, (Dec, 2015), https://www.sebi.gov.in/reports/reports/dec-2015/concept-paper-for-issuance-of-green-bonds_31167.htm

[9] INTERNATIONAL CAPITAL MARKETS ASSOCIATION, GREEN BOND PRINCIPLES, (June 2021), https://www.icmagroup.org/assets/documents/Sustainable-finance/2022-updates/Green-Bond-Principles_June-2022-280622.pdf.

[10] Securities and Exchange Board of India, Circular on Disclosure Requirements for Issuance and Listing of Green Debt Securities, CIR/IMD/DF/51/2017 (Issued on Mar 30, 2017).

subsequently superseded the Circular for the Issue and Listing of Non-Convertible Securities (NCS), Securitised Debt Instruments (SDI), Security Receipts (SR), Municipal Debt Securities and Commercial Paper (CP) ("**Operational Circular**"),[11] read with Regulation 26 of the SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 ("**NCS Regulations**"), which collectively form the existing framework governing green bonds in India.

The NCS Regulations set out the categories of projects or assets in respect of which green bonds may be issued and are supplemented by the Operational Circular, which prescribes disclosure norms in relation to offer documents for the issuance of green bonds in respect of, *among other things* the decision-making process underlying the determination of eligible projects and details of selected projects, environmental objectives of the proposed investment and internal procedures for tracking the deployment of proceeds. Additionally, issuers are also required to abide by continuous disclosure norms, which necessitate the inclusion of additional disclosure alongside the annual report and financial results in respect of, *among other things*, the utilization of the proceeds of the issue, details of unutilized proceeds, list of projects to which funds have been allocated, and performance indicators of environmental impact.

IV. GREENWASHING CONCERNS

While the size of the Indian green bond market has witnessed massive growth since the issuance of the first green bond by Yes Bank in 2015, a majority of the assignments are comprised of green bonds which target foreign investors and are listed in offshore markets on account of favorable pricing.[12] It is common knowledge that considering the magnitude of India's commitments and consequent financing requirements, the need to scale up domestic avenues to supplement international capital is evident. This knowledge raises a fundamental question - how can the domestic green bond market be made more accessible to investors? In the authors' view, the answer lies in reducing the risk perception around low-carbon investments[13] and effectively creating a sense of comfort and familiarity around green bonds within the investor community. However, what is considered seemingly the most fundamental

[11] Securities and Exchange Board of India, Operational Circular for Issue and Listing of Non-Convertible Securities (NCS), Securitised Debt Instruments (SDI), Security Receipts (SR), Municipal Debt Securities and Commercial Paper (CP), SEBI/HO/DDHS/P/CIR/2021/613 (Issued on Aug 10, 2021).

[12] Bhattacharya S., Kumar N., Lonikar P., *India Sustainable Debt State of the Market Report*, CLIMATE BONDS INITIATIVE (May, 2022), https://www.climatebonds.net/files/reports/cbi_india_sotm_2021_final.pdf.

[13] Kumar N., Vaze P., Kidney S., *Moving from growth to development: Financing green investment in India*, OBSERVER RESEARCH FOUNDATION (April, 2019), https://www.orfonline.org/research/moving-from-growth-to-development-financing-green-investment-in-india-49420/.

risk of investing in green bonds is the possibility of overstating environmental impact[14] or making false or misleading claims regarding the 'greenness' of the project and its projected impact on climate change and the environment.[15]

Greenwashing can lead to reputational risks for issuers seeking to raise capital to fund sustainable projects and information asymmetry for investors seeking to diversify their portfolios by investing in environmentally-linked financial instruments. The diversion of the proceeds of green bonds to projects with minuscule or questionable environmental impact also directly influences the perception of green bonds as 'safe' instruments and is, in turn, viewed as one of the biggest challenges to the development of the green bond market by regulators across the world.

V. ANALYSIS OF PROPOSED CHANGES

Through the proposals in the Consultation Paper, SEBI has attempted to tackle the challenge of greenwashing by seeking to equip investors with the information necessary to evaluate the sustainability and environmental impact of their investments in green bonds on a holistic basis. While the Consultation Paper deals with a slew of proposals in respect of the existing framework on green bonds, the analysis in the subsequent paragraphs has been limited to recommendations concerned with monitoring requirements for tracking the utilisation of proceeds, disclosures in connection to the refinancing of projects and use of standards, certifications, or taxonomies for identification of eligible projects and impact reporting.

A. TRACKING THE UTILISATION OF PROCEEDS

Monitoring the utilization of proceeds from a green bond issuance is the foundational principle of the green bond market. It serves as a strong signalling tool to investors regarding aligning their investment with environmental objectives.[16] The Operational Circular spells out material requirements concerning monitoring the utilization of proceeds in a twofold manner, i.e. *firstly*, the pre-issuance disclosure of internal processes to be employed for tracking the deployment of profits in the offer document, and *secondly*, the post-issuance ongoing reporting of the actual utilization of proceeds as per internal tracking carried out by the issuer, along with the

[14] Suk Hyun, Donghyun Park, Shu Tian, *The price of frequent issuance: the value of information in the green bond market*, ECONOMIC CHANGE AND RESTRUCTURING (2022).
[15] Patrick Henry, *What are green bonds and why is this market growing so fast?*, WORLD ECONOMIC FORUM, (Oct 26, 2021), https://www.weforum.org/agenda/2021/10/what-are-green-bonds-climate-change/.
[16] *Supra* note 6.

submission of the annual report and financial results. The latter is also required to be verified by an external auditor. Moreover, the issuer must disclose any unutilized proceeds from the issuance. Through the Consultation Paper, SEBI has also proposed to include disclosures on the intended types of temporary placement for the balance of unallocated net proceeds.

Investment in green bonds is motivated mainly by the investors' knowledge that their investment shall be used for financing projects which will contribute to the green agenda. Thus, reporting on the processes to be put in place for internal tracking of the funds and utilization of proceeds from the green bond issuance, right from the stage of the offer document and as a continuous disclosure measure, is instrumental in providing clear assurance to investors regarding the deployment of funds to appropriate projects and critical from the standpoint of mitigating greenwashing concerns.

Once fundraising is complete, it is equally important to have clear visibility on the availability of any unallocated proceeds to a specific project, on allocation. This ready availability can be ensured by disclosing the intended types of temporary placement of unallocated proceeds, as proposed in the Consultation Paper. The said disclosure is a standard practice followed across the globe and can be viewed as a step forward towards attuning the domestic green bond framework with international conventions. To ensure that the funds raised are not deployed towards non-green projects pending allocation to suitable environmental objectives, the proposed framework may incorporate indicative guidelines on the nature of assets or instruments into which the unallocated proceeds can be parked. These instruments may be highly liquid, well-rated, short-term instruments such as cash, government bonds, commercial paper, and other money market instruments.

B. REFINANCING OF PROJECTS

It is generally used to use the proceeds from green bond issuance to refinance assets or projects with a longer operating life than the bond's tenure.[17] Refinancing existing projects through the proceeds of a green bond issuance comes to the aid of issuers who cannot identify a significant pipeline of new eligible green projects in the given financial year and is a key enabler of green investment.[18] While doing so, it is crucial to provide a potential investor with necessary

[17] Igor Shishlov, Romain Morel, Ian Cochran, *Beyond transparency: unlocking the full potential of green bonds*, INSTITUTE FOR CLIMATE ECONOMICS (June, 2016), https://www.cbd.int/financial/greenbonds/i4ce-greenbond2016.pdf.
[18] Ghosh A., Chawla K., Jaiswal A., Kwarta S., Connolly M., Kaur N., Deol B., Mance A., Smis D., Dougherty S., Schub J., & Youngs R., *Greening India's Financial Market: How Green Bonds Can Drive Clean Energy*

information regarding the existing projects which may be refinanced. An attempt to enhance the disclosure requirements for refinancing projects through green bonds has been made under the Consultation Paper. It is proposed to include additional disclosures on the project details in which the proceeds will be utilized for refinancing purposes, the per cent share of financing and refinancing, and the look-back period for determining the eligibility of such refinanced projects. A look-back period essentially refers to the time frame used to determine the eligible existing projects which may be refinanced from the proceeds of green bond issuance.

Regarding refinancing of projects, it is also pertinent to discuss the 'additionality' factor, which assumes relevance while directing the proceeds of green bond issuance to exist projects or assets. While the term additionality is yet to be circumscribed by a clear definition, it can be broadly understood to mean the flow of capital to green assets or projects which would not otherwise be financed.[19] It is widely believed that for a green bond to demonstrate additionality, it must contribute to scaling up activities which, in the absence of financing conditions offered by the green bond proceeds, would otherwise not occur.[20] From the standpoint of existing projects which have originated several years before the refinancing, it has been observed that the additionality of an investment is low or downright questionable,[21] and issuers may market their green credentials under an existing project without further contributing to sustainable operations,[22] leading to an overall impression of greenwashing. Moreover, when a portion of the proceeds is used for refinancing, a lower additionality is generally assigned to existing projects selected through a more extended look-back period.[23]

The framework proposed in the Consultation Paper notes that while the issuer's disclosure of a look-back period has been proposed, the maximum permissible extent of such period has not

Deployment, COUNCIL ON ENERGY, ENVIRONMENT & WATER (April, 2016), https://www.ceew.in/sites/default/files/ceew-research-how-green-bonds-can-drive-renewable-energy-deployment-india.pdf.

19 Sean Kidney, *Green Bond Additionality: The Big Picture*, BONDS & LOANS, (Dec 24, 2018), https://bondsloans.com/news/green-bond-additionality-the-big-picture.

20 UNITED NATIONS ENVIRONMENT PROGRAMME FINANCE INITIATIVE, ALIGNING FINANCE FOR THE NET-ZERO ECONOMY: NEW IDEAS FROM LEADING THINKERS, (April, 2021), https://www.unepfi.org/wordpress/wp-content/uploads/2021/03/5-Green-Bonds.pdf.

21 Dion Bongaerts & Dirk Schoenmaker, *Working paper: The next step in green bond financing* (Rotterdam School of Management, April 2020), https://www.rsm.nl/fileadmin/Faculty-Research/Centres/EPSVC/WP-Green_Bond_Financing.pdf.

22 Manual Adamini and Krista Tukiainen, *the Impact Bond Market*, *in* RESPONSIBLE INVESTMENT IN FIXED INCOME MARKETS (Joshua Kendall & Rory Sullivan ed., October 2022).

23 Eugenia Jackson & John Ploeg, *Filtering Shades of Green Through our Green Bond Framework*, PGIM FIXED INCOME (June, 2021), https://cdn.pficdn.com/cms/pgim-fixed-income/sites/default/files/Filtering%20Shades%20of%20Green%20Through%20our%20Green%20Bond%20Framework.pdf.

been defined. The absence of a precise look-back period in the regulatory framework gives rise to the possibility of issuers using green bonds as a refinancing tool for older projects that may have existed for as long as ten years.[24] To avoid the risk of such green bonds from being construed as an attempt at greenwashing, it may be prudent to specify an upper limit for the look-back period in the regulatory framework for determining the eligibility of projects which may be refinanced through proceeds from green bonds. While setting the upper limit, it is equally important to retain the issuer's discretion to determine the exact look-back period. It is also recommended that the time elapsed since the project was last financed be included in the disclosures to enable informed decision-making by the investors.

C. USE OF COMMON STANDARDS

There is a growing consensus over the need to adopt common globally accepted standards, certifications, or taxonomies in selecting projects financed through green bonds and post-issuance impact reporting. Under the existing framework as set out in the Operational Circular, an issuer is required to, *among other things,* disclose the process followed for the determination of eligible projects, performance indicators of the environmental impact of the project, and any globally accepted standards used for identification of eligible projects and impact reporting. Under the Consultation Paper, it is proposed that, in addition to the existing disclosure requirements, an issuer shall disclose any taxonomies, standards or certifications (from now on collectively to as "**standards**") and information regarding the alignment of the selected projects with the said standards or taxonomies, if referenced during project selection. Similarly, issuers shall disclose the project's environmental impact in the offer document and as a continuous disclosure. Further, any standards or taxonomies used during such impact reporting may also be disclosed optional.

Let us first consider the upside of the proposals set out in the preceding paragraph. The proposed disclosure of standards used when identifying eligible projects and impact reporting is a step ahead in supporting investors to make environmentally conscious investment decisions. The disclosure of such measures is also integral to demonstrating the 'greenness' of a selected project and minimizing instances of greenwashing. Moreover, reporting information pertaining to project-specific impact in the offer document and as a continuous disclosure measure is also instrumental in demonstrating the 'additionality' of investment and enabling

[24] Rosl Veltmeijer, *Stimulating Change or Just Cheap Financing*, TRIDOS INVESTMENT MANAGEMENT (Oct 10, 2019), https://www.triodos-im.com/articles/2019/green-and-social-bonds.

investors to assess their assets in a timely fashion regularly. In light of the same, it would be prudent to mandate the use of such standards by issuers during project selection and impact reporting to ensure the legitimacy of the green label.

However, without the introduction of harmonized standards in the Indian green bond market, the purpose that the proposed disclosures intend to serve would be precluded. Given the variety of standards available, merely requiring issuers to disclose their bar of choice can lead to possible overlap, divergence and uncertainty in the market.[25] Moreover, given investors' lack of familiarity with green bonds, and the scarcity of tools required to distinguish between a green and a non-green asset, the presence of multiple taxonomies may cause further confusion. Thus, it is crucial to harmonize the standards used to identify eligible projects and impact reporting to rule out plural interpretations. Conflicting practices and, in turn, reduce the risk of investing in non-green projects under the green bond label.[26] Developing a list of reasonable and commonly accepted standards tailored to suit the nuances of the Indian green bond market is the need of the hour to address investors' concerns about greenwashing and deepen market penetration. Further, it is recommended that the issuer may be permitted to choose from the specified list of standards while identifying eligible projects and reporting on impact to maintain flexibility.

VI. CONCLUDING REMARKS

At a time when environmental, social and governance themes are gradually taking centre stage in the investor landscape, the domestic green bond market is at a crossroads. Taking note of the scale of capital required to achieve India's nationally determined contributions and net zero emission commitments, the steps taken hereon to address critical market challenges, such as greenwashing, shall dictate the growth trajectory of the domestic green bond market in the time ahead. Dispelling the risks associated with greenwashing is pivotal to increasing accessibility and facilitating a low-risk perception, and in turn, fueling greater participation by issuers and investors in the domestic green bond market. Regulation, at this juncture, needs to be market-driven and must consider the introduction of harmonized standards and taxonomies for

[25]Jun M., Kaminker C., Kidney S., Pfaff N., *Green Bonds: Country Experiences, Barriers and Options*, ORGANISATION FOR ECONOMIC CO-OPERATIONS AND DEVELOPMENT, INTERNATIONAL CAPITAL MARKETS ASSOCIATION, CLIMATE BONDS INTIATIVE AND GREEN FINANCE COMMITTEE OF CHINA SOCIETY FOR FINANCE AND BANKING (2017), https://www.oecd.org/environment/cc/Green_Bonds_Country_Experiences_Barriers_and_Options.pdf.

[26] Renita D'Souza, *Perspectives on a green taxonomy for India*, OBSERVER RESEARCH FOUNDATION (Nov 11, 2021), https://www.orfonline.org/expert-speak/perspectives-on-a-green-taxonomy-for-india/.

evaluation of eligible projects and impact reporting, detailed monitoring requirements for utilization of proceeds, clear definitions and a cohesive market ecosystem, all the while striking a balance between regulation and high compliance cost for issuers. While the proposals set out in the Consultation Paper appear to make some headway in this regard, the ability of the framework to cater to the nuances of the green bond market shall determine its course in the time ahead.