Sustainable Finance

For Prelims: Carbon Market, MSME, Regulatory Sandbox

For Mains: Sustainable Finance, International Financial Services Centres Authority

Why in News?

A Committee on Sustainable Finance, constituted by **International Financial Services Centres Authority (IFSCA)** submitted its report on Sustainable Finance suggesting development of the **carbon market** among others.

What is Sustainable Finance?

- Sustainable finance is defined as **investment decisions that take into account the environmental, social, and governance (ESG) factors** of an economic activity or project.
  - **Environmental factors** include mitigation of the climate crisis or use of sustainable resources.
  - **Social factors** include human and animal rights, as well as consumer protection and diverse hiring practices.
  - **Governance factors** refer to the management, employee relations, and compensation practices of both public and private organizations.

What are the Recommendations of the Committee?

- Developing a voluntary carbon market, framework for transition bonds, enabling de-risking mechanisms, promoting **regulatory sandbox** for **green fintech** and facilitating the creation of a global climate alliance among others.
- Setting up of a **dedicated** MSME (Micro, Small and Medium Enterprises) **platform for sustainable lending.**
- Facilitating the **use of innovative instruments such as catastrophe bonds, municipal bonds, green securitisation, blended finance among others.**
- **Enabling aggregation facilities**, impact funds, green equity etc. in IFSC.
- **IFSCA has to play a vital role in capacity building** which lays the foundation for greening the financial system.

What is IFSCA?

- **Establishment:**
  - The IFSCA was established **in 2020 under the International Financial Services Centres Authority Act, 2019.**
  - It is headquartered at GIFT (Gujarat International. Finance Tec-City) **City, Gandhinagar in Gujarat.**
- **Role:**
  - The IFSCA is a unified **authority for the development and regulation of financial**

products, financial services and financial institutions in the International Financial Services Centre (IFSC) in India.
    - At present, the GIFT IFSC is the **maiden international financial services centre in India.**
    - Prior to the establishment of IFSCA, the domestic financial regulators, namely, **RBI**, **SEBI**, **Insurance Regulatory and Development Authority of India (IRDAI)**, and the **Pension Fund Regulatory and Development Authority (PFRDA)** **regulated the business in IFSC.**
- **Members**:
    - The International Financial Services Centres Authority **consists of nine members,** appointed by the central government.
    - They include **the chairperson of the authority,** a member each from the **RBI, SEBI,** the **IRDAI,** and the **PFRDA**, and two members from the Ministry of Finance. In addition, two other members are appointed on the recommendation of a Selection Committee.
- **Term:**
    - All members of the IFSCA have **a term of three years,** subject to reappointment.

What are the Carbon Markets?

- **Carbon markets** allow for buying and selling of carbon emissions with the objective of reducing global emissions.
- Carbon markets existed under the Kyoto Protocol, which is being replaced by the Paris Agreement **in 2020.**
- **Carbon Markets** can potentially **deliver emissions reductions** over and above what countries are doing on their own.
    - For example, technology upgradation and emission reduction of **a brick kiln in India can be achieved in two ways:**
        - A developed country which is unable to meet its reduction target can provide money or technology to the brick kiln in India, and thus claim the reduction of emission as its own.
        - Alternatively, the kiln can make the investment, and then offer on sale the emission reduction, called carbon credits. Another party, struggling to meet its own targets, can buy these credits and show these as their own.

What are the Related Indian Government Initiatives?

- **Perform Achieve and Trade (PAT) Scheme:** The government has undertaken the **PAT scheme**, targeting carbon emission reduction in 13 energy intensive sectors.
- **Encouraging Foreign Capital:** The Government has permitted **Foreign Direct Investment (FDI)** up to 100 percent under the automatic route in the renewable energy sector.
- **Encouraging Renewable energy:**
    - The Government has waived inter-state Transmission System (ISTS) charges for inter-State sale of solar and wind power for projects.
    - Making provisions for Renewable Purchase Obligation **(RPO)** and setting up Renewable Energy parks
- **India's Nationally Determined Contribution:** Under the Paris Agreement which was adopted by signatory countries in 2015, India had submitted **Nationally Determined Contribution (NDC)** with quantified targets
    - To reduce the emissions intensity of its **Gross Domestic Product (GDP)** by 33-35% till 2030 from the levels at 2005,
    - To achieve about 40% cumulative electric power installed capacity from non-fossil fuel-based energy resources by 2030,
    - To create an additional carbon sink of 2.5-3 billion tonnes of carbon dioxide equivalent through additional forest and tree cover by 2030.

UPSC Civil Services Examination Previous Year Question (PYQ)

Prelims

Q. The concept of carbon credit originated from which one of the following? (2009)

(a) Earth Summit, Rio de Janeiro
(b) Kyoto Protocol
(c) Montreal Protocol
(d) G-8 Summit, Heiligendamm

Ans: (b)

- Adopted in 1997, the Kyoto Protocol came into force in 2005. It is an international treaty which extends the 1992 United Nations Framework Convention on Climate Change (UNFCCC) that commits parties to reduce greenhouse gas emissions, based on the scientific consensus.
    - Emissions trading, as set out in Article 17 of the Kyoto Protocol, allows countries that have emission units to spare – emissions permitted to them, but not "used" – to sell this excess capacity to countries that are over their targets.
    - Carbon Credit is a unit of measure, the credit given to someone or an entity/company or country, if they reduce their GHG emissions (CO2 equivalents) by 1 unit. This is provided through Clean Development Mechanism (CDM) under **the Kyoto Protocol, which facilitates a "carbon market".**
- Rio de Janeiro Earth Summit, or Rio Summit, was a major United Nations conference, held in Rio de Janeiro in June 1992.
    - The summit concluded with an agreement on the Climate Change Convention, which in turn led to the **Kyoto Protocol and the Paris Agreement.**
    - Another agreement was to "not to carry out any activities on the lands of indigenous peoples that would cause environmental degradation or that would be culturally inappropriate".
    - The documents developed in the summit are, the Rio Declaration on Environment and Development, Agenda 21, Forest Principles.
- Montreal Protocol is a protocol to the Vienna Convention for the Protection of the Ozone Layer. It is an international treaty designed to protect the ozone layer by phasing out the production of numerous substances believed to be responsible for ozone depletion.
- The outcome of 33rd G8 Summit held in Heiligendamm was Heiligendamm Process. This process was to initiate a dialogue on relevant issues with the important emerging economies.
- Four Areas of Focus
    - Promoting and protecting innovation,
    - Strengthening the freedom of investment by means of an open investment climate, including strengthening the principles of corporate social responsibility,
    - Determining joint responsibilities for development, focusing specifically on Africa,
    - Joint access to know-how to improve energy efficiency and technology co-operation, with the aim of contributing to reducing CO_2 emissions.
- **Therefore, option (b) is the correct answer.**

Mains

Q. Should the pursuit of carbon credits and clean development mechanisms set up under UNFCCC be maintained even though there has been a massive slide in the value of a carbon credit? Discuss with respect to India's energy needs for economic growth. **(2014)**

Source: IE