Green Growth and Energy Transformation (GROW-GET)
Solar for Education
Event Report of Forum for Policy, Jaipur
Friday, August 25, 2017

Background:

CUTS International, in collaboration with Friedrich Ebert Stiftung had commenced a project called **Green Growth and Energy Transformation (Grow GET)** in April, 2016 in Jaipur, Rajasthan. The core idea of the project is to create an implementable strategy for energy transformation at state level by engaging all the concerned stakeholders into fostering a dialogue to identify common interests. To serve this purpose, long-term multi-stakeholder working groups or the 'Seed Communities' were set up at Rajasthan, West Bengal, National and the International (India- EU Cooperation) levels. The ultimate target of the project is in coherence with the national aim of increasing the share of renewable energy in the overall energy mix.

In the previous session, i.e. Forum for Finance, conducted on July 28, 2017, challenges of Banks with respect to providing small sized loans for solar electrification in rural areas. Key challenges are high transaction costs of small loans, apprehensions on repayment capacity of rural borrower and lack of communication between the regulator and commercial banks. Availability of a sustainable source of funds is a key concern for project developers as well. In order to address this, possible business models (possibly without the capital subsidy component) were discussed that can allow use of CSR funds for solarisation of schools in rural areas.

In order to improve the uptake of decentralised solar solutions and improve access to energy, enabling ecosystem with appropriate policies, financing mechanisms and job opportunities needs to created. Therefore, it is important to first address policy level challenges with respect to technology and finance. In order to facilitate a deliberation on the same, CUTS International organised a Policy Roundtable called **Forum for Policy** on **August 25, 2017** with representations from Bank of Baroda, Reserve Bank of India, Rajasthan Renewable energy Corporation Ltd. (State Nodal Agency), project developers, Expert on Renewable Energy and seed community members.

The key discussions of the session revolved around the concerns on mandates of Priority Sector Lending, concerns of bankers with respect to credit worthiness of rural borrowers, role of bank regulator (RBI) towards energy access, challenges associated with mechanism of channelizing capital subsidies, role of State Nodal Agency in promoting use of decentralised solar solutions, etc.

1. **Challenges faced by Banks:**

I. **Role of Reserve Bank of India towards Financial Inclusion**:

Financial Inclusion Development Department (FIDD)of Reserve Bank of India conducts financial literacy camps in schools and other educational institutions and educates people on the use and benefits of bank accounts, loan formalities for education loans and security issues.

RBI, through its Lead District Officers (LDO)discusses with the District Collectors on quarterly basis, the progress of government sponsored schemes that are implemented through banks. Under these government schemes, respective Government Officials are responsible for collecting the loan applications. The loan application is then scrutinised by a Committee comprising of the respective government officials and banks for viability. This Loan Appraisal Committee is answerable to the District Collector (DC), andin absence of the DC, to the Lead District Officer. The bank then finally approves or disapproves the loan based on the recommendations of the Appraisal Committee.

Banks are sometimes unwilling to sanction loans owing to certain constraints but it needs to be justifiedto the District Collector.

II. **Qualification of Renewable Energy for Priority Sector Lending (PSL)**:

As per Reserve bank of India,renewable energy projects qualify for Priority Sector Lending (PSL).However, renewable energy projects of households and schools are rather treated as Consumer Financing.

Issues of credit worthiness and collection faced by the banks could be acting as a deterrent in providing loans to households under PSL.Banks are apprehensive about lending to renewable energy installations for households as they are not connected to any income generating activity.

Financing solar projects in rural areas is a gainful opportunity for the bankers. Every bank needs to achieve their mandated PSL target. In case they are unable to achieve their PSL targets, Commercial banks purchase PSL certificates at premium from the RBI for unspent amount allocated for priority sectors. It is believed that sub categorising Renewable Energy for PSL further may increase the lending for Decentralised Renewable Energy (DRE), especially solar. However, RBI has refused to put a mandate exclusively on solar. Solar can be recognised as a component of renewable energy category under PSL, but an exclusive mandate on solar may not be possible.

III. **Constraints of Bankers to finance decentralised space**:

In order to lend to consumers, commercial banks need to analyse the fund position and repayment capacity of the borrower. If the borrower does not have the capacity to repay back the principle amount, then the banks may not be in a position to lend.In case of Interest Subsidy towards loans, the subsidy would take care of only the interest portion of the entire loan amount but the borrower would still have to repay the principle amount. Therefore, the analysis of the fund position shall be crucial to estimate the credit worthiness of the borrower.

IV. Potential to consider lending to DRE as a Social Scheme:

The challenges faced by Decentralised Renewable Energy sector are far more different from the grid connected large rooftop projects. Issues pertaining to credit worthiness and repayments are far more crucial for this sector. Moreover, the transaction cost of sanctioning loans in DRE space is higher than other sectors. Therefore, there is a major resentment among commercial

banks to lend to DRE space. There might be a potential to consider lending to DRE space as a social sector scheme.The Government may launch a scheme exclusively targeting bank financing for decentralised solar projects, supporting banks through a back-end subsidy.

V. **Lack of Awareness among Bankers:**

Banks have varied understanding regarding different schemes under which DRE solar solutions can be financed. State Level Banker's Committee (SLBC) can be a platform to address the issue. An 'All-Bank Meeting' along with representation from NABARD and RBI can be organised to deliberate on the crucial solar schemes in the respective state and 'guidelines' could also be issued to all corporate head offices of all banks to facilitate clarity on operational aspects of the schemes to its branches.

VI. **Understaffing in Banks for Repayment**:

Banks face a challenge of understaffing in order to provide loans to the borrower in the remotest areas. Houses in remote areas being extremely scattered, it is challenging for bank staff to visit the borrower's house for collection of loan amount.

2. **Role of Self-Help groups in rural credit**:

The credit need of the rural consumers is extremely basic and small. Therefore, Self-Help Groups (SHG) can be essential in access to credit in rural areas. SHGs have a well-established channel of credit in the rural areas of Rajasthan which will ensure timely repayment of loan amount effectively. The loan to SHG need not necessarily be linked to a livelihood activity, except under NRLM.

SHGs function under the aegis of the Rural Development Department of the state and are provided support by local NGOs. In case of default in payment by any SHG, **the Department takes initiatives by sending its own team to enable collection from the SHGs.**

Since the transaction cost for providing a loan is the same irrespective of the loan size, therefore, **in order to reduce the transaction cost, loans of small amounts can be bundled together and considered as single portfolio of bigger ticket size which can be facilitated through** SHGs. The SHG then becomes the point of contact between the borrower(s) and the bank. The credibility of the SHG becomes the collateral and also helps in reducing the transaction cost and hence ensuring efficiency.

However, there would be need for an independent agency for a bundled bank loan for **a region or a block** (with households, primary health care centres and educational institutions), to take up the responsibility to coordinate with all of the stakeholders and disburse loans. This is because, institutions like the primary health care centres and educational institutions are run by government.

A consortium for two different kinds of funds is challenging to be facilitated. A non-state actor creating liability on government buildings will be a problem from legal perspective as well. A consortium exclusively for grants can be created and used for development of a region.

Therefore, a special purpose vehicle (SPV) or an independent agency can facilitate the entire loan process.

3. **Tripartite Agreement**

Bank financing is quite relation-centric and recovery of loans from such households can depend on the relation of the borrower with the banks. Since the Indian legal system is not that

efficient to enable recovery of loans, the relational aspect with the banks becomes even more important.
The issue of understaffing of banks could be addressed if a local person who knows the area well is hired by banks as their collection agents. As there are no roads and proper addresses or landmarks in such remote areas, such an arrangement will help identify the houses.

Such a tripartite arrangement between a technology provider, bank and the local partner can help simplify the process of loan disbursement. In such a situation, **the technology provider (or the project developer) becomes the point of contact between the villager and the bank and they establish a relationship with the banker on behalf of the borrower. They facilitate the whole loan process for the villager.**

However, there are few challenges associated with the Tripartite Agreement, i.e. **Credibility of Third Party (giving bank guarantee)** and **Limited list of channel partners with MNRE** as banks will only go with empanelled Channel Partners). The banks may be willing to enter into such arrangement only with technology providers who are empanelled with the Ministry.

4. **Housing projects and Rooftop solar for houses**:
Loans for solar rooftop could also be linked to government schemes like Awas Yojana. **Under the Awas Yojana, loans for installing solar rooftop could also be added as a component of the housing loan, which could be provided at a preferential rate of interest and the system can be an off-grid system as well.**

5. **Issues with NABARD Scheme on Solar Home Lighting System (SHLS):**

MNRE (GOI) has signed an MOU with NABARD to promote SOLAR HOME LIGHTING SYSTEMS to rural areas. This program is to be implemented under the Jawaharlal Nehru National Solar Mission (JNNSM). The Ministry provided a subsidy of 40% of the capital cost which was channelized through NABARD, Regional Rural Banks and other Commercial Banks. For balance of the cost, the banks could extend credit facility to the beneficiary at usual commercial rates.
The RRBs and other Commercial Banks extended the loan for balance cost of the systems at normal interest rates. Regional Rural Banks and Commercial Banks extends loans to the consumers and directly disburses subsidy for solar home lighting systems and small Capacity PV systems under the financing of Off-grid Solar Applications Programme.

The NABARD scheme for Solar Home Lighting System has been discontinued. There were several challenges in implementing the scheme and channelizing the subsidies. Most of the northern states have been on the bottom of the list regarding sanctioning loans under this scheme.
Therefore, **the NABARD Scheme could be redesigned to involve all the banks as partners for directly channelizing the subsidies. The scheme can be facilitated through the State Nodal Agencies for renewable energy and this could potentially eliminate NABARD in the channel.**
The scheme could also propose to enable direct participation of commercial banks in the scheme to disburse subsidies and a stronger mechanism for monitoring of (bank) loan amount and its deployment and repayment. This could allow the banks to identify the right reasons for a

loan turning bad and will lead to providing a better ecosystem in place for bank financing for DRE.

6. **List of Channel Partners prepared by State Nodal Agencies to be recognised for subsidy schemes:**
   State Nodal Agencies (SNAs) also empanel Channel partners for their own schemes and maintain a list which is frequently updated. However, banks cannot use the list maintained by the SNA (RRECL) unless recognised by RBI or NABARD (MNRE) or corporate head office of the respective commercial bank.

   It is suggested that the SNA list of Channel partners, which is much more relevant to the bankers as it is state-specific, gets notified to the banks so that the scope of providing loans increases and it may also enable banks to enter into tripartite agreements.

7. **Need for an Empowered State Nodal Agency**:

   There is need to establish clear responsibilities for every agency regarding every aspect of scrutiny of loan. **There has to be an agency exclusively responsible for sanctioning the design of the module.**

   - **Scrutinising and Approving Newer Modules:**
     Providing stringent technical specifications for a module can restrict the scope of innovation. There are newer technologies that can making products (or modules) more efficient. **The procedure to be followed to get every newer and better model recognised with MNRE** (for capital subsidy) may delay the process of making newer and better version already available in the market. **State Nodal Agency, if empowered to recognise and scrutinise the newer models, can speed up the process. This may also promote innovation in the sector which will ultimately have an impact on the efficiency of the entire system.**

   - **Providing technical support to banks for loan appraisal**:
     There is a need for a technical expert to be associated with the banks as an external consultant. State Nodal Agency can potentially become an external expert for the banks to scrutinise loans.
     The circular on the MNRE scheme also puts technical criteria (with respect to modules to be accepted for the scheme) while sanctioning the loan. Since, the bankers may not be technical experts of the scheme, they may rely blindly on the certifications shown to them by the project developers.
     The SNAs can then further inform the SLBC about the newer technologies and the SLBCs can further inform the banks to recognise the newer modules while appraising the loans. The SNAs could be made the point of contact for the SLBC on technical advancements.

   - **Evaluation of performance of channel partners:**
     Renewable energy sector, being an upcoming sector where there are new players coming into the market and who are working in the rural areas. Such players may not be able to match the financial criteria (sales turnover mandates) specified by MNRE. Therefore,

criteria for empanelment of channel partners could be based on performance (qualitative criteria). Also, the MNRE or the credit rating agencies recognised by MNRE should not be the only agencies to evaluate the channel partners. **This also creates a case for a much more powerful SNA that can evaluate the performance of the channel partners as per the state-specific criteria. There are certain channel partners who are catering to only certain specific geographies and do not have operations nation-wide.**

- **Avoid Duplication of Infrastructure:**
  There is also a **need for coordination between the energy department of a state and the state nodal agency to avoid duplication of infrastructure**. SNAs need to take the responsibility of creating such an ecosystem where DISCOM and off-grid technology providers can work together towards a common goal of 100% rural electrification and not as rivals.

8. **Business model of Regional Rural Banks**:
   There are huge differences between a **large scale project** and a project for a **rural household** in terms of costing, design, availability of finance, etc. However, there are similar challenges faced in rural financial outreach in terms of solar and other sectors. However, Solar is the safest system for rural lending and financial inclusion as well (i.e. to connect rural households to institutional financing system).
   The expertise and business models of bank financing in other rural lending spaces can be utilised for extending loans for off-grid energy as well.

   Rural Financing as a business model:
   Rural financing activity of the banks also has to be acknowledged as a business activity. Banks need to ensure that the loans that they provide do not turn bad and therefore are bound to follow rules framed by the higher authorities. Therefore, rural lending must not be considered as a social obligation of the banks. However, if there are government schemes which would ensure that bankers do not incur losses and repayment of money is guaranteed.

   One criteria of providing credit in rural areas is also presence of project developer in the area where the systems have been installed. There is huge transaction cost to scrutinise a loan. It is not the job of the banks to be technical experts for solar projects.

9. **Awareness Creation among Bankers about Decentralised Solar Space**:
   A major challenge in providing loans for solar is **lack of awareness among the bankers about the nitty-gritties of decentralised solar**. Therefore, there are apprehensions among bankers to provide loans for solar. There is a need to conduct Banker's workshop to create awareness among the banking community regarding technical aspects of solar financing. Such an initiative is taken by private entities voluntarily at the grassroots. There is need to promote such initiatives at institutional level as a mandatory feature. **It is to be understood whether SLBC platform can be used for conducting more of such workshops at regional levels**. Banker's workshops have been conducted by many organisations and despite that the lending for solar is not picking up. This indicates that there can be other structural problems within the system that are restricting the uptake which need to be addressed.

10. **Need for improvement in inter-organisational communication**:

There is poor communication flow within the layers of banking from its corporate office to its branch managers. Therefore, **there a need to device mechanism to improve communication flow from ministry to regulator, from regulator to bank corporate offices and from corporate office to branches.**

Bank branches often do not have clarity on the operational aspects of the solar schemes and other policy guidelines. There is a need to improve inter-departmental communication (within a bank) and communication between regulators to bring more clarity on the application (or operational criteria) of the schemes. Policy guidelines must also be simplified for the banks.

11. **Over-burdening Existing Institutions**:
    Banks as financial institutions are under tremendous pressure for serving at the grassroots. Being an institution with vast network of branches, banking infrastructure is being used for several other activities (like running of government schemes, insurance linkages, Adhaar) apart from banking. Overburdening existing institutions with ancillary activities creates tremendous pressure on them.

12. **Improvement in the MNRE Capital Subsidy Scheme**:

- **Compulsory O&M by project developer**: The confidence of the bankers with respect to solar financing is weak. **There is a need to put a mandate on the project developer to look after the operations and maintenance of the project for at least 5 years. Remuneration under the scheme can be linked to this condition.** This may also improve the confidence of the banks about the quality of the products used by the project developer in the system. This can also act as a performance guarantee for the banks.
- **Bank Guarantee by project developer**: Another important addition to the scheme could also be to make it mandatory for the project developers to **provide bank guarantee for the project**. Also, the criterion for having a service centre in proximity to the region where the projects have been installed can be made mandatory. Both of these criteria can ensure product quality and maintenance.
- **Bank Guarantee backed by Product Quality Mandates**: Bank guarantee is the part of solution but not a complete solution. Typical bank guarantee norm is 5-10%of the project cost. If the project developer gives bank guarantee, he may also compromise on the quality of the product and increase his profit margin by 5-10%such that the additional cost in terms of a bank guarantee gets off-set. **Bank guarantee must be backed by stricter product quality mandates.**

- **Repayment Mechanisms**: The scheme should also be clear about the repayment mechanism for consumers.

13. **Potential of Solar Off-Grid systems to contribute to RPOs**:
    There is a need to look at off-grid solar beyond just household and towards a more integrated solution that includes community health care centres and schools also in off-grid. This can potentially contribute to the RPO targets of the Discoms.

14. **Interest Subsidy vs. Capital Subsidy:**

Bankers may prefer having Interest Subsidy to Capital Subsidy as Interest subsidy provides a direct back-end support from the government to the bank regarding payment of the interest portion of the loan.This may reduce the chances of NPAs in the sector and can also reduce the transactional cost of the loan.

- **List of Participants:**

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