The World Bank

India: Partial Risk Sharing Facility for Energy Efficiency (PRSF)
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Matrix of CTF Independent Reviewer Comments and World Bank Task Team Responses
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CTF Independent Reviewer Comments	World Bank Task Team's Response	CTF Independent Reviewer's Comments to World Bank Task Team's Response
Developmental partners have supported several programs and projects over the past two decades to stimulate the ESCO market in India. While this has led to the establishment of 128 ESCOs and to the EESL, commercial FIs in India continue to be apprehensive of lending to ESCOs and balance sheet lending prevails over project finance in India. The proposal would be strengthened if it were to address how this program will help overcome this barrier where other efforts have not been quite as successful as envisaged.	The team agrees that the ESCO development in India has not taken off even though efforts, including those funded by donors, have been made in last two decades. As explained in the proposal, one of the lessons learned from experiences in India, and limited successes outside India, has been to integrate TA with financial incentives and this project design has been developed based on that premise. EE market has a complex ecosystem with many barriers. Of the 130 ESCOs, most are small and do not have the financial credibility to access finance (ability to borrow from FIs) and FIs too perceive these investments through ESCOs as riskier because these are not only complex, non-asset based transactions but also involve EE measures and technologies	The WB team is correct in stating that the integration of TA and financial incentives, coupled with the stronger policy and regulatory initiatives in India would help alleviate barriers to ESCO operations. TA to PFIs could emphasize development of mechanisms to mitigate risks of project finance for ESCO projects to overcome PFI resistance to financing ESCOs. The project monitoring framework could include indicators to monitor this aspect of the effectiveness of the TA in educating PFIs.

	which FIs do not always clearly understand. The combination of TA, which will help develop capacity of FIs, ESCOs, end users, and standardize the transaction tools and templates, and financial risk sharing through PRSF is aimed at addressing these barriers and demonstrate to the FIs and EE market that there is in reality, very little risk in ESPC based energy savings implementation through ESCOs. We also feel that with NMEEE in place, there is a stronger mandate and willingness amongst all stakeholders now to move forward to large scale EE market transformation.	
The report states that "ICICI currently has a US$836 million portfolio in energy efficiency and renewable energy lending. Some banks have even developed financial products specifically for EE projects. SBI, for example, had facilitated 60 energy audits and sanctioned 20 energy efficiency loans as of 2009. SIDBI has worked extensively with the MSMEs in promoting EE". Given this vast experience of commercial banks (at least some major banks) in India with EE, why do FI's continue to perceive ESCO financing as risky? Is it more because banks in India lend primarily on balance sheet and are averse to project financing? The report would be strengthened if it were to address	FIs in India do limited financing of EE projects, but almost negligible ESCO financing as they perceive ESCO based ESPC transactions as riskier in general with relatively high transaction costs arising out of the complex ESPCs and M&V arrangements involved, and ESCOs which are mostly small companies, as not financially credible enough to lend to. Many EE investments tend to be small providing insufficient return to cover the associated transaction costs. Many ESCOs also have few assets that could be pledged as collateral for EE sector loans, requiring greater reliance on the cash flows generated by the EE projects. The uncertainties involved in the cash flow estimation and monitoring also increase the banks' risk perception of EE projects. Larger ESCos (like Schneider, Honeywell, Johnson Controls, etc) and vendor ESCos are either able to user their own finance or are able to easily borrow for ESPC based EE projects. Much of the	The WB should ensure that part of the TA should focus on developing mechanisms to lower transaction costs and mitigate risks for FIs to help broaden the market for ESCO financing and operations.

how the proposed program would be different and would sustainably engender additional financing for continued ESCO operations.	FIs current EE portfolio is with large and regular clients who anyway do business with them (relationship banking) and also many EE loans are embedded within other larger loans.	
The proposed project will develop standardized procedures, contract documents and M&V protocols for ESCO operations, which is expected to support the sustainability of ESCO operations in India. The proposal would be strengthened if it were to address how these documents will differ for past efforts, which have also developed similar documents and contracts and have yet not been adopted as a standard by stakeholders. The proposal could also address how these standardized documents are to be made legally enforceable under Indian contract law and business practices, which would be essential if the outcome of the technical assistance is to lead to sustainable ESCO operations.	This is an important observation. The objective of the TA and the PRSF facility operations is to "market test" and demonstrate what would work best in practical terms in terms of ESPC templates, M&V protocols and other EE transaction documents. As the TA evolves over the first 2-3 years and some early experience from PRSF supported investments start coming in, and these templates are standardized as market and business best practices for various sectors (SMEs, industries, municipalities, buildings) these would need to be vetted under India contract laws. The team will discuss this aspect during appraisal and incorporate elements into the TA if necessary.	Ensuring that project appraisal considers the need for standardized contracts and protocols developed under the TA are applicable and enforceable under Indian laws and business practice would improve project outcomes.
The proposed project will make the risk facility available to implementing projects in large industries and to entities notified under PAT in India, in addition to other qualifying MSMEs and public entities. Large industries are generally capable of financing cost effective EE projects and	The team agrees with this comment. Most large PAT industries do not want to work with ESCOs (as ESCOs may not add much value in terms of bringing technical solutions and innovation in specialized process industries for instance). Many PAT industries are financially strong enough to either fund themselves or borrow from FIs to implement EE projects. Even though they are included,	A project pipeline focused on SMEs and municipalities would be better targets for the PRSF. The approach to project identification for PRSF support could include this parameter.

entities mandated to implement EE under PAT will have to find financing mechanisms to implement EE and comply with the mandate. Should these entities be excluded under the proposed PRSF and risk guarantees provided only to eligible entities, which may otherwise not undertake EE measures? Equally, should the FIs, which already have large EE portfolios (such as ICICI, SBI, etc.) be excluded from benefiting from the PRSF since they already have adequate experience with mitigating risks of EE financing?	our pipeline analysis as shown in the document and our preparation discussion with FIs, industries, SMEs, ESCOs and other stakeholders have led to the conclusion that it will be the SMEs and municipalities (for street lighting) pipeline that will be most attractive for ESCO interventions and therefore for PRSF. FIs with large EE portfolios do not necessarily have large ESCO borrower base or end-user base which works with ESCOs. Hence the team, in consultation with SIDBI and BEE, have decided to keep all FIs for participating in PRSF as long as they can meet the eligibility criteria for PFIs. We also feel that those FIs that already deal with EE projects will be quicker to move to deal with ESCO based transactions.	The Team's reasoning to provide the benefit of PRSF to all eligible FIs to ensure deal flow is reasonable.
The proposal states that the GoI is establishing a Partial Risk Guarantee Fund for Energy Efficiency (PRGFEE), and would play largely the same role as the PRSF. How does the GoI intend to fund the PRGFEE? The report would be strengthened if it were to address why the PRSF with CTF financing is essential to GoI to undertake the proposed project when it itself plans to implement a similar program.	PRGFEE, funded with US$20 million from GOI, will play largely the same role as the PRSF, but its support will be limited to Government Buildings and Municipalities in the first phase. PRGFEE has not started its operation yet. PRSF will cover those same sectors but also large industries, MSMEs, municipal street lighting and buildings. The two programs will cross-leverage the technical assistance and capacity building each delivers. The proposed US$25 million of CTF contingent finance through PRSF would provide important additional resources to mobilize commercial funding for ESCO-implemented EE projects. It would also allow market	The Team's contention that the PRSF would help broaden the market to more end-use sectors and PFIs is reasonable. Project implementation could ensure that the PRSF and PRGFEE are complementary and broaden capacity building.

	development to take root in more sectors and with more commercial banks than would be possible only with PRGFEE. The Bureau of Energy Efficiency (BEE) plays the role of guarantor with PRGFEE. With PRSF, that role is performed the Small Industries Development Bank of India (SIDBI) which during project implementation aims to build its own capacity to issue guarantees for EE projects. This way it could act as a guarantor in the future, independently of IFI or CTF funding, to support commercial lending for EE projects, as long as the market would require such risk sharing support. PRGFEE alone does not include a component to develop the capacity of a local financial institution to act as a guarantor after program expiration PRSF will also assist SIDBI in its market development efforts by allowing it great flexibility on setting the guarantee terms and conditions in response to market needs, including coverage and pricing levels. On the contrary, PRGFEE guarantee rules are well-defined up-front and do not aim to improve the guarantee product based on market feedback.	
The proposal intends to put in place a TRA mechanism whereby "the cash flows of the EE Project is insulated by shifting the control over future cash flows from the Beneficiary industry to an	To the extent possible, all EE loans covered by PRSF will be extended on a project finance basis, which insulates the EE project cash flows from the reach of other creditors. All EE project cash flows will be required to flow to the TRA and can only be used for the	Ensuring that FIs finance ESCOs on the basis of project finance would enable the TRA mechanism to be operable and effective.

independent agent, called Trustee Bank, duly mandated by the PFI." The proposal could address how the savings from EE projects can be ring fenced. Would other creditors to project beneficiaries not have a first lien on all cash flows? Would the TRA be subordinate to such liens?	purposes agreed in a TRA Agreement to be signed between the PFI, the ESCO, the Host and the Trustee Bank in a format to be attached in the PRSF Operations Manual. The TRA will bind the Host to make timely payments and legal action can be taken in case the Host does not pay the required amount into the TRA. The TRA and the Reserve Account will be regularly monitored by the PFI and reported to the PRSF Facility Manager (SIDBI) on a quarterly basis in the form and manner to be specified by the PRSF Facility Manager (SIDBI)	

Final Comments by the CTF Independent Reviewer

The proposed project document was reviewed again in view of the response provided by the WB team to the initial comments made by this reviewer. The response from the team adequately addresses the principal comments. Based on a revised review of the project document, the proposed project meets the eligibility criteria for CTF co-financing.