

**Date: 26 July 2024**

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**Sub: Issuance of Second-Party Opinion on ESAF Small Finance Bank Ltd. (ESAF's) Policy on Green Deposit and Green Financing Framework (PGD&GFF)**

**[A] Introduction:**

CARE Analytics and Advisory Pvt. Ltd. (hereinafter mentioned as 'CareEdge Advisory') has undertaken the Second-party Opinion of the "**Policy on Green Deposit and Green Financing Framework**" (hereinafter mentioned as 'the PGD&GFF') of the **ESAF Small Finance Bank** (hereinafter mentioned as 'ESAF' or 'the Bank').

The Bank has prepared PGD&GFF in accordance with the requirement of C(6) of RBI/2023-24/14 DOR.SFG.REC. 10/30.01.021/2023-24 'Framework for acceptance of Green Deposits' issued on 11 April 2023 by the Reserve Bank of India (hereinafter referred to as the '**RBI Framework**') and Frequently Asked Questions (FAQs) on Framework for acceptance of Green Deposits dated 29 December 2023, issued by RBI (hereinafter referred to as '**RBI FAQ**').

**[B] CareEdge Advisory's Scope of Work:**

CareEdge Advisory's Scope of Work is defined above enumerated in Purchase Order No: ESFB/PO/2024-25/746, Issue Date: 14 June 2024 issued by the Bank.

**[C] Management's Responsibilities**

The Bank's Management is responsible for: (i) development of the Policy on Green Deposit & Green Financing Framework (PGD&GFF) in line with RBI Framework dt. 11 April 2023 and RBI FAQ dt. 29 December 2023, (ii) engagement with stakeholders and create awareness, (iii) ensure utilization of proceeds of green deposit as per RBI guidelines / criteria mentioned in the framework, (iv) monitor impact of the projects financed on periodic basis, (v) facilitate third-party verification of PGD&GFF, (vi) ensure periodic reporting to Bank's Board, and; (vii) ensure subsequently reporting to RBI on annual basis.

This duty entails creating, putting into practice, and maintaining internal controls pertinent to the creation of the GDP&GFF in compliance with the aforementioned RBI Circular's recommendations and requirements, which are devoid of any significant misstatement resulting from fraud or error.

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## [D] CareEdge Advisory's Responsibility

CareEdge Advisory's responsibility is to provide Second-party opinion on the Bank's PGD&GFF based on procedure described below.

## [E] Procedures:

CareEdge Advisory has performed the procedures listed below:

Modality of providing Second-party Opinion: (i) review of PGD&GFF and associated Guidelines prepared by the Bank, (ii) had discussion with key stakeholders to understand their near and mid-term plan(s) and perspective(s), (iii) benchmarked the PGD&GFF against RBI Framework/FAQ and other documents, and (iv) analysed as per industry best practice(s).

The procedure has encompassed the review of the following aspects included in the Framework:

- Overall alignment of the PGD&GFF and associated General Guidelines with the RBI's framework and/or FAQ
- Process of Identification of Use of Proceeds
- Criteria for selection of eligible projects that may be financed through green deposits proceeds in line with RBI framework and exclusions within the eligible categories
- Roles and Responsibility matrix for selection of green financing projects
- Process of management of proceeds obtained from Green Deposits incl. identification and management of asset liability mismatches;
- Process of temporary allocation of unutilized fund
- Process of third-party verification/assurance of the allocation proceeds, policies and internal controls;
- Process of reporting impacts to Bank's Board and subsequently to RBI.

## [F] Exclusions:

The Second-party Opinion on Bank's Framework (**Version 1 dt. 25 July 2024**) should be construed as a point-in-time opinion expressed basis the information made available by the Bank and not surveilled from time-to-time.

The scope of vetting the Framework excluded the following and therefore CareEdge Advisory does not express a conclusion on the same:

- Testing the operationalization of the Framework at project level and providing opinion on same;
- Review of financial data of the Bank including its operations, financial performance, usage, and allocation of the funds and end-use of funds by the borrower;
- Credit rating or testament of underlying credit quality of either Bank or its Borrower(s);
- Developing of sector specific KPIs (if any),
- Preparation of Impact Assessment framework and defining timelines for same,
- Review / provide opinion on ESAF's Environmental & Social Policies & related issues;
- Aspects either implicitly / explicitly excluded from CareEdge Advisory's scope of engagement;
- The statements (if any) that describe the expression of opinion, belief, aspiration, expectation, aim or future intentions provided by the Bank, any forward- looking assertion; and/or data.

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**[G] Conclusion:**

The Second-Party Opinion was carried out by a group of professionals with multiple-years of experience in areas like ESG, Banking and Finance.

CareEdge Advisory believes it has received sufficient information in the form of: (i) the PGD&GFF and associated guidelines [base & revised documents], and (ii) Clarification against queries raised from key Stakeholder(s) to provide a basis of its conclusion.

Based on the Procedures performed (see sec. [E] above) and the evidenced obtained, nothing has come to CareEdge Advisory's attention that causes it to believe that the Bank's PGD&GFF is not aligned, in all material respects, with RBI's Green Deposit Policy and RBI's FAQ.

The said Framework is attached herewith as **Annexure 1.**

**[H] Restriction of Use**

CareEdge Advisory's second party opinion including the conclusion has been prepared and addressed to the Bank's management at the request of the Bank solely to assist the Bank in reviewing its Framework.

Accordingly, CareEdge Advisory accepts no liability to anyone, other than the Bank. CareEdge Advisory's report(s) should not be used for any other purpose, other than those specified in the CareEdge Advisory's scope of work defined by the Bank.

CareEdge Advisory neither accepts nor assumes any duty of care or liability arising from any form of damage(s) arising from any third party.

Regards.

For **CARE Analytics and Advisory Pvt. Ltd.**



**Kedar Deshpande**  
Director, ESG – Advisory

CARE Analytics and Advisory Private Limited  
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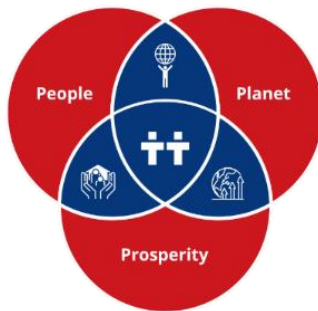
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# GREEN FINANCE FRAMEWORK

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## **1. 1 Introduction**

ESAF Small Finance Bank is committed to addressing climate change and promoting sustainable development through the implementation of its Green Deposit Policy and Framework. This strategic initiative is designed to align with global environmental initiatives and regulatory frameworks, utilizing green finance to create positive environmental impacts.

Climate change is recognized as a critical and pervasive challenge affecting numerous sectors of the economy. Consequently, sustainable finance is seen as a meaningful opportunity to manage and mitigate these risks. In line with global trends and the Reserve Bank of India's Framework, ESAF Small Finance Bank has adopted the Green Deposit Policy Framework, marking a significant step toward fostering a more sustainable financial sector in India.

This framework leverages green finance as a tool to promote positive environmental impacts, particularly in reducing carbon emissions, enhancing energy efficiency, and supporting sustainable development.

### **1.2 Objective**

The primary objective of this framework is to provide a structured system for the issuance, allocation, monitoring, and reporting of Green Deposits while ensuring transparency, accountability, and compliance with regulatory standards. This framework aims to promote environmental sustainability through targeted financial products and investments, in alignment with the United Nations' Sustainable Development Goals (SDGs).

The Green Finance Framework support the national agenda for sustainable development, fosters innovation in clean technology, and drives investment in environmentally sustainable projects. This involves directing funds towards projects that address climate change adaptation and mitigation, contributing to building a more resilient economy that is better prepared to face the impacts of climate change.

### **1.3 Scope**

The Green Finance Framework applies to all departments and business units involved in the issuance, allocation, and management of Green Deposits within the Bank. It encompasses all processes from product design to impact assessment and reporting.

## **2. Definitions**

### **2.1 Green Deposits**

Green Deposit means an interest-bearing deposit, received by the bank for a fixed period and the proceeds of which are earmarked for being allocated towards green finance.

### **2.2 Green Finance**

Green Finance means lending to and/or investing in the activities/projects meeting the requirements prescribed by RBI in the Framework for acceptance of Green Deposits that contributes to climate risk mitigation, climate adaptation and resilience, and other climate-related or environmental objectives - including biodiversity management and nature-based solutions.

## 2.3 Greenwashing



















Greenwashing means the practice of marketing products/services as green, when in fact they do not meet requirements to be defined as green activities/projects.





## 3. Use of Proceeds

### 3.1 Segments for Green Financing

The allocation of proceeds raised from Green Deposits shall be based on the official Indian green taxonomy.

The Bank will allocate the proceeds raised through Green Deposits towards the following list of green activities/projects which encourage energy efficiency in resource utilisation, reduce carbon emissions and greenhouse gases, promote climate resilience and/or adaptation and value and improve natural ecosystems and biodiversity, Energy Efficiency Measures; Projects that improve energy efficiency in industrial processes, buildings, and transportation.

Sector	Description	SDG Linkage
Renewable Energy	<ul style="list-style-type: none"> <li>Solar/wind/biomass/hydropower energy projects that integrate energy generation and storage.</li> <li>Incentivizing adoption of renewable energy.</li> </ul>	  
Energy Efficiency	<ul style="list-style-type: none"> <li>Design and construction of energy-efficient and energy-saving systems and installations in buildings and properties.</li> <li>Supporting lighting improvements (e.g., replacement with LEDs).</li> <li>Supporting construction of new low-carbon buildings as well as energy-efficiency retrofits to existing buildings.</li> <li>Projects to reduce electricity grid losses.</li> </ul>	   
Clean Transportation	<ul style="list-style-type: none"> <li>Projects promoting electrification of transportation.</li> <li>Adoption of clean fuels like electric vehicles including building charging infrastructure.</li> </ul>	  
Climate Change Adaptation	<ul style="list-style-type: none"> <li>Projects aimed at making infrastructure more resilient to impacts of climate change</li> </ul>	  
Sustainable Water and Waste Management	<ul style="list-style-type: none"> <li>Promoting water efficient irrigation systems.</li> <li>Installation / upgradation of wastewater infrastructure including transport, treatment and disposal systems.</li> <li>Water resources conservation.</li> <li>Flood defence systems.</li> </ul>	    

Pollution Prevention and Control	<ul style="list-style-type: none"> <li>Projects targeting reduction of air emissions, greenhouse gas control, soil remediation, waste management, waste prevention, waste recycling, waste reduction and energy/emission-efficient waste-to-energy.</li> </ul>	
Green Buildings	<ul style="list-style-type: none"> <li>Projects related to buildings that meet regional, national or internationally recognized standards or certifications for environmental performance including green building projects and energy efficiency projects.</li> </ul>	
Sustainable Management of Living Natural Resources and Land Use	<ul style="list-style-type: none"> <li>Environmentally sustainable management of agriculture, animal husbandry, fishery and aquaculture.</li> <li>Sustainable forestry management including afforestation/reforestation.</li> <li>Support to certified organic farming.</li> <li>Research on living resources and biodiversity protection.</li> </ul>	
Terrestrial and Aquatic Biodiversity Conservation	<ul style="list-style-type: none"> <li>Projects relating to coastal and marine environments.</li> <li>Projects related to biodiversity preservation, including conservation of endangered species, habitats and ecosystems.</li> </ul>	
Investment in Sovereign Green Bonds		
<p><b>Exclusions</b></p> <ul style="list-style-type: none"> <li>Projects involving new or existing extraction, production and distribution of fossil fuels, including improvements and upgrades; or where the core energy source is fossil-fuel based.</li> <li>Nuclear Power generation.</li> <li>Direct waste incineration.</li> <li>Alcohol, weapons, tobacco, gaming, or palm oil industries.</li> <li>Renewable energy projects generating energy from biomass using feedstock originating from protected areas.</li> <li>Landfill projects.</li> <li>Hydropower plants larger than 25 MW.</li> </ul>		

The taxonomy and sectors will be reviewed periodically in alignment with RBI guidelines to ensure compliance and relevance.

### **3.2 Asset Products for Green Financing**

The bank will periodically create different products that can be financed using the proceeds from Green deposits. Alternatively, current loan products that are eligible to be categorized as Green finance can be funded using Green deposits and accounted for as such. The business teams will ensure its sole intended use for the green segment.

### **4. ESAF Green Deposit- Product Details**

4.1 Green deposits can be issued as cumulative or non-cumulative deposits and denominated in Indian Rupees only.

4.2 The tenure, size, interest rate, and other terms and conditions applicable to green deposits shall be in compliance with RBI's Master Directions on Interest rate on deposits.

4.3 Retail Liability department shall design and set up Green deposit products in the system, for augmenting the resources of Green finance initiatives. Alternatively, deposits collected, positioning and offering it as Green deposits to the depositors, during a pre-fixed period, declared in advance may be classified as Green Deposits and earmarked for Green financing.

4.4 Green deposits may be offered to the following type of customers:

- Individuals
- Individuals with other individuals for a joint account
- Minors under guardians
- Firms
- Companies
- HUF
- NRI
- OCI's
- Trust/Associations/Societies
- Any other organization not prohibited by RBI

4.5 Awareness on the green deposits shall be created by introducing special Account opening forms and such other promotional activities by the Retail Liability Department with the assistance of Sustainable Banking Department.

### **5. Green Finance Credit Appraisal Process**

5.1 The allocation of funds to projects outlined in Point # 3 will be undertaken by the Bank through its credit appraisal sanction process as per the approval matrix based on their approval limits as set by the Bank for the products deployed for the Green Financing.

5.2 The sanction process will follow the Bank's Credit Policy with its green emphasis as approved by the Board.

### **6. Project Evaluation and Selection Criteria**

6.1 The Bank shall ensure lending to or investing in activities or projects that contribute to climate risk mitigation, climate adaptation, resilience, or other climate-related or environmental objectives. The bank's policy ensures that lending and investment activities support climate risk mitigation, adaptation, resilience, and other environmental objectives. This

is outlined in the Environmental, Social & Governance Policy and the Green deposit policy aligns with this strategy.

6.2 In addition to the process for evaluation and selection of eligible climate-related projects or projects with environmental objectives, the following components will be included:

a. The development of a comprehensive training program for relationship managers and credit risk management, focusing on identifying eligible projects, sustainable lending/investing practices, and the assessment of sustainability information provided by borrowers.

b. The creation of Standard Operating Procedures (SOPs) that clearly outline the criteria, guidelines, and steps for evaluating and selecting eligible climate-related projects or projects with environmental objectives. These SOPs will serve as a reference for relationship managers and credit risk management when identifying eligible projects for lending/investing within the eligible categories.

c. Collaboration with the Sustainable Banking Department to ensure that the training program and SOPs align with sustainable banking practices and principles, and that they receive the necessary approvals before implementation.

d. The evaluation of Green Projects will follow the standard procedures, aligning with the Bank’s Credit Policy, Credit Risk Management Policy, Delegation of Powers, and other relevant lending policies.

## 7. Roles & Responsibilities Matrix

<b>Roles</b>	<b>Responsibility</b>
Directors and Board	<ol style="list-style-type: none"> <li>1. Establishing and overseeing the bank’s green deposit strategy and ensuring its alignment with the broader corporate sustainability strategy and Regulatory guidelines.</li> <li>2. Ensuring transparent reporting and communication with stakeholders about the bank’s green deposit initiatives and their outcomes.</li> </ol>
MD & CEO	<ol style="list-style-type: none"> <li>1. Supervision of Green Deposit Scheme for Green &amp; Sustainable finance in a comprehensive manner.</li> </ol>
ALCO	<ol style="list-style-type: none"> <li>1. Responsible for monitoring for the matching between the liability raised and fund deployed on a quarterly basis.</li> <li>2. Address any potential mis-match of Green Deposit and Green Finance on a quarterly basis.</li> </ol>
ESG Management Committee (ESGMC)	<ol style="list-style-type: none"> <li>1. To receive the Green Assets Portfolio listing from Retail Assets and approve the same for the Green Deposit Deployment avenues.</li> <li>2. To review the Green Deposit – Green Finance promotional activities for maximising the ESG impacts.</li> <li>3. To review the matching of Green Deposit and Green Finance and suggest actions to ALCO for addressing potential mismatch (if any).</li> </ol>
Retail Assets, MSME, Agri and FIBD	<ol style="list-style-type: none"> <li>1. Classification of Retail Asset Products that qualify Green Deposit Deployment criteria as defined by RBI. List to be provided to ESGMC for approval.</li> <li>2. Development of New Products that will open new avenues in the market (especially the green finance market), that will qualify Green Deposit Deployment Criteria as defined by RBI.</li> </ol>

	<ol style="list-style-type: none"> <li>3. Green Loan Disbursement: Ensure the disbursement of green loans aligns with the "Use of Proceeds" section of the framework.</li> <li>4. Third-Party Assurance: Conduct third-party assurance of the "Use of Proceeds" in compliance with RBI regulations.</li> </ol>
Retail Liability, Branch Banking, BC Channel	<ol style="list-style-type: none"> <li>1. Green Deposits – Product Development in line with RBI norms, such as offerings, interest rates, maturity tenures.</li> <li>2. Green Deposits- Product Promotion, developing funding appetite, and fundraising methods, as well customer relations for Green Deposits.</li> <li>3. Customer Education: Promote customer education and awareness regarding green finance and its environmental and financial impacts.</li> </ol>
Treasury	<ol style="list-style-type: none"> <li>1. Executing a plan to allocate and distribute funds for green finance.</li> <li>2. Placing unallocated green funds into easily accessible financial instruments.</li> <li>3. Investing in Green instruments like sovereign green bonds.</li> </ol>
Risk Management	<ol style="list-style-type: none"> <li>1. Risk Mitigation Strategy: Develop and implement strategies to identify, assess, and mitigate various risks associated with green finance, ensuring the sustainability and resilience of green deposits.</li> </ol>
Credit Sanctions and Credit Monitoring	<ol style="list-style-type: none"> <li>1. Ensuring Green finance classification is done only from available green deposits.</li> <li>2. Monitoring of Deployment Disbursements and loan sanctioning using green proceeds.</li> </ol>
Compliance	<ol style="list-style-type: none"> <li>1. Regulatory Compliance for the Deposit and Financing Framework as defined by RBI.</li> <li>2. Monitor and ensure compliance with regulatory requirements and standards related to green finance, including the management of environmental, social, and governance (ESG) risks.</li> </ol>
Marketing & PR	<ol style="list-style-type: none"> <li>1. Developing Marketing Strategies for Green Deposits and Green Finance Opportunities through the same.</li> <li>2. Customer Awareness: Raise awareness among customers about green finance and its environmental and financial impacts.</li> <li>3. Communication Strategy: Effectively communicate information about green deposits through various channels, including branches, social media platforms, and the company's website.</li> <li>4. Developing a differentiation in communicating and marketing our green businesses.</li> <li>5. Creation of a Green brand for the Bank which can be communicated and marketed.</li> </ol>
IT	<ol style="list-style-type: none"> <li>1. The preparedness of the infrastructure to integrate a range of sustainable finance products (including lending and deposits) across various digital platforms such as apps and ERPs.</li> <li>2. Associating transactions with the appropriate 'Green' lending or deposit categories.</li> </ol>
Internal Audit	<ol style="list-style-type: none"> <li>1. Verify the fund collection and utilization as per use of proceeds session.</li> <li>2. Verify the reports are submitted to board/management on a quarterly basis.</li> <li>3. To assist the external auditors in conducting audits as per RBI guidelines.</li> </ol>
Sustainable Banking	<ol style="list-style-type: none"> <li>1. Overall Responsibility of Green Deposit Policy, Green Finance Framework, to synergise business growth and social &amp; environmental impact.</li> <li>2. Periodic Reviews and Renewals of the Green Deposit Policy &amp; Framework:</li> <li>3. Capability Building on ESG: for different departments to act in synergy for triple bottom line impacts.</li> </ol>

	4. Facilitating the Impact Assessment of the use of proceeds as mandated by : Conduct impact assessments in collaboration with the Asset and Liability Team.
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## 8. Management of Proceeds

The Bank will implement a system to monitor both (a) liability raised through green deposit and (b) the use of proceeds from green deposit. Funds raised through green deposits will be tagged, categorized, and allocated to projects that meet the criteria outlined in Sec.3 Use of Proceeds.

8.1. ALCO will be responsible for monitoring the mismatch between the liability raised and fund deployed on monthly/quarterly basis. The same will be reported to Bank's Board.

8.2. Unallocated proceeds of green deposits, can be temporarily parked in Level 1 High Quality Liquid Assets with maturity up to one year only. ESAF's Treasury Department will oversee their allocation to the eligible projects.

8.3. Fund approval for financing projects under Green finance should be obtained from Credit Sanctions Department. Inflow funds by way of Green deposits shall be monitored by Retail Liabilities department and outflow by way of Investment and lending as Green finance shall be monitored by the Credit Sanctions.

## 9. Third-Party Verification, Assurance, And Impact Assessment:

The bank shall ensure that the funds raised through green deposits are allocated appropriately by subjecting them to annual independent third-party verification or assurance. This process will be carried out as follows:

9.1. The Retail Asset Business Verticals shall review the Green Finance portfolios every quarter and present the findings to the ESG Management Committee, through the Sustainable Banking Department.

9.2. The Sustainable Banking Department shall identify qualified independent individuals or entities to conduct the impact verification and assurance.

9.3. The bank shall publish the Impact Assessment Report of its green finance portfolio and projects on its website as per the below table of Illustrative list of impact indicators.

Eligible Category	Project	Impact Indicators – Examples
Renewable Energy		Total renewable capacity (in MWh)
		Energy generated per year (MWh)
		GHG emissions avoided per year (measured in tonnes CO <sub>2</sub> equivalent, tCO <sub>2</sub> e)
Waste Management		Waste diverted from landfill per year (tonnes)
Clean Transportation		GHG emissions avoided per year (tCO <sub>2</sub> e)

	New clean transportation infrastructure built (km)
	Number of electric or low emission vehicles produced
Energy Efficiency	Energy savings per year (MWh)
	GHG emissions avoided per year (tCO <sub>2</sub> e)
Afforestation/ Reforestation	GHG emissions reduced/Carbon Sequestration achieved (measured in tCO <sub>2</sub> e)

## 10. Reporting and Disclosures:

10.1 A review report shall be placed by the Sustainable Banking Department before Board of Directors through the ESG Management Committee, within three months of the end of the financial year which shall, inter-alia, cover the following details:

- (a) amount raised under green deposits during the previous financial year Framework for acceptance of Green Deposits.
- (b) list of green activities/projects to which proceeds have been allocated, along with a brief description of the projects.
- (c) the amounts allocated to the eligible green activities/projects.
- (d) a copy of the Third-Party Verification/Assurance Report and the Impact Assessment Report.

10.2 The Bank shall also disclose this information in the Annual Financial Statements in the prescribed format by RBI.

Particulars	Current Financial Year	Previous Financial Year	Cumulative
<b>Total green deposits raised (A)</b>			
<b>Use of green deposit funds</b>			
(1) Renewable Energy			
(2) Energy Efficiency			
(3) Clean Transportation			
(4) Climate Change Adaptation			
(5) Sustainable Water and Waste Management			
(6) Pollution Prevention and Control			
(7) Green Buildings			
(8) Sustainable Management of Living Natural Resources and Land Use			
(9) Terrestrial and Aquatic Biodiversity Conservation			
<b>Total Green Deposit funds allocated (B = Sum of 1 to 9)</b>			
<b>Amount of Green Deposit funds not allocated (C = A – B)</b>			

<b>Details of the temporary allocation of green deposit proceeds pending their allocation to the eligible green activities/projects</b>			
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### **11. Stakeholder Engagement**

The bank shall take an active role in engaging with its customers, employees, shareholders, regulators, and other stakeholders to increase awareness of its Green Deposit policy. The bank shall encourage its customers and employees to participate in green initiatives and adopt environmentally responsible practices.

Furthermore, the bank shall collaborate with external stakeholders such as government agencies, non-governmental organizations, and industry bodies to promote environmental sustainability and green financing.

### **12. Reviews and Renewals**

The bank shall tirelessly improve its processes, systems, and controls related to Green Deposits and Green financing to ensure complete alignment with industry best practices and global standards. The Bank shall proactively review and assess the effectiveness of its green deposit policy and promptly make necessary upgrades based on evolving regulatory requirements, market conditions, and stakeholder feedback, at least once annually.