



## Energy Savings Insurance

### Mobilizing private investment in energy efficiency



The Inter-American Development Bank has partnered with the Danish Government to replicate and scale up an innovative risk management package aimed at catalyzing increasing levels of EE investments in the Latin America and Caribbean region.

Building on IDB experience and work by the Global Innovation Lab for Climate Finance, the facility will replicate and scale-up an innovative risk management package aimed at encouraging private sector investment in energy efficiency

projects. This will support countries in exploiting energy efficiency investment opportunities through the development of local markets.

The facility is built on the strong reputation and experience of the IDB in the region, including experience from piloting energy efficiency financing programs in Mexico (FIRA) and Colombia (Bancoldex), where the energy efficiency market is being catalyzed with the support of international climate funding.

#### *Why Energy Efficiency?*

The use of high efficiency technologies and retrofit strategies can play an important role in reducing the energy intensity of economic activities and avoiding the need for new energy supply. At the same time, it can enhance firm productivity, potentially reduce emissions, and support climate change mitigation in a cost-effective manner. As highlighted by the International Energy Agency (IEA), energy efficiency is the most important element in keeping the door open to the globally agreed 2°C target through to 2020 at no net economic cost.

economic growth and support energy security and competitiveness, while also improving general health and the environment.

However, much of this vast energy efficiency potential remains untapped, particularly in emerging economies where market barriers prevent investors from prioritizing these investment opportunities. These barriers include: lack of trust between clients, technology solution providers and financial institutions; financial barriers; and lack of information and awareness of business opportunities.

The ESI Facility offers an innovative business model consisting in a “package” of standardized interventions that together help build energy efficiency markets by addressing technical and financial risks and building confidence among key market actors including: End users/investors; energy service and technology providers; commercial financial institutions; and insurance providers.

A key innovation of the business model is an insurance product covering projected energy savings for specifically defined and verifiable energy efficiency measures that are agreed upon under a standard contract between firms and technology solution providers.

The suite of measures will be tailored to country and/or sector specific conditions and is designed to be scalable. It overcomes barriers that firms and technology solution providers encounter when seeking to finance energy efficiency measures from monetized expected future energy savings. An innovative business model is introduced consisting of a structured set of interventions promoted by a national “champion” and coordinator (in Latin America typically a National Development Bank). The “package” reduces the risks that companies encounter when seeking bankable finance for energy efficiency projects.

This gives assurance to both the end-user/investor and the bank that energy savings will be sufficient to pay back the financing, while also building capacity and credibility of technology solution and energy service providers.

With the development and implementation of a pipeline of projects, capacity and credibility of technology solution/energy service providers will be enhanced. In parallel, banks become increasingly familiar with energy efficiency investments. In a subsequent stage, the elements of standardization of contracts, project validation and savings verification may mobilize the interest of institutional investors such as pension funds, e.g. through securitization and green bonds.

The model emphasizes the use of standardized approaches that minimize transaction costs. This is enabled by focusing on sectors and technologies where relatively standard energy efficiency solutions are available. The sector focus is mainly on commercial buildings, SMEs and light industry. Technologies covered to date include: Air-conditioning, electric motors, industrial boilers, refrigeration, compressed air systems, cogeneration, refrigeration systems, solar water heating, and LED lighting (under development).



**The key elements of the intervention package include:**

**Financing.** A credit line from IDB channeled through a national development bank will enable the local financial institution to provide competitive financing at longer terms to support enterprises in the implementation of energy efficiency measures.

**Standardized performance contract.** The energy efficiency market in emerging economies is still in its early stages, and there are not very clear rules on how to deal with, sell and allocate risk related to energy savings. The facility introduces a contractual arrangement between a potential client and a technology supplier, which establishes a transparent

and equitable risk sharing arrangement. The contract extends beyond merely supplying energy efficient equipment to cover the performance of the installation and the associated savings. The contract will be adapted to the local legal framework and market practices.

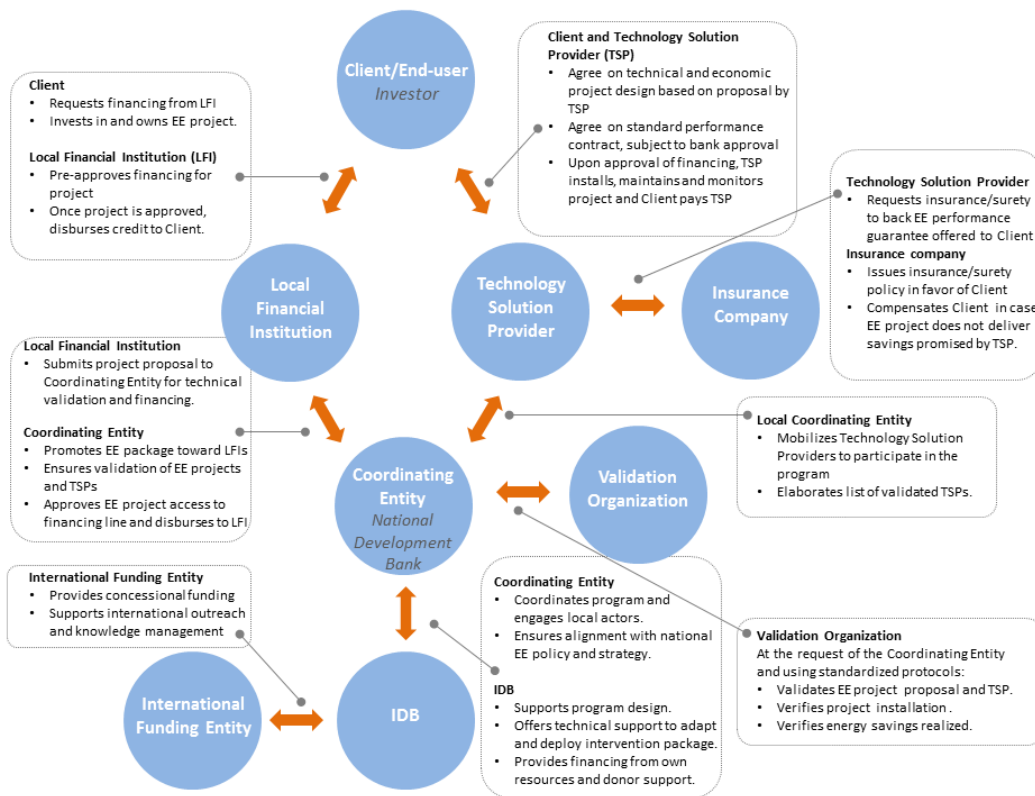
**Energy savings insurance.** An insurance (e.g. in the form a surety) that is covers the performance commitment made by the technology solution provider and thus minimizes risk to the investor. Local insurance companies are mobilized in collaboration with international re-insurance companies.

**Validation and verification mechanisms:** A set of technology-specific independent validation procedures will be performed by a third party with strong credentials.

Includes a) validation of the ability of the EE project to deliver the energy savings; b) validation of the capacity of the technology supplier to deliver the project; c) verification that the equipment has been installed according to the proposal; d) verification that the substituted equipment has been properly disposed of; e) verification of reported energy savings; and f) arbitration in case of disagreement between the client and the technology solution provider about the achieved energy savings.

**Awareness raising, partnerships, and pilot projects.** A key aspect of making EE markets take off is to raise awareness and engage key actors in energy efficiency opportunities. Potential investors (clients), financial institutions and technology solution providers are targeted and connected. Support is provided to build an initial pipeline of “bankable” energy efficiency projects to demonstrate the viability of the mechanism and attract the interest of key players in the market.

*Stakeholders and their roles*



There is increasing focus on how the public sector, including national development banks (NDBs) can develop and implement targeted measures that mobilize private investors and increase investments in energy efficiency. This intervention package establishes a public-private program to do just that, with targeted international support.

In each country and sector, a strong local entity is identified that is willing to act as a “champion” and coordinator and which has the capacity to operate the

program based on a mandate to support economic development. The program relies heavily on the outreach and credibility of this entity with local commercial banks and companies.

Key roles in implementation will be played by local financial institutions; private companies as energy end-users and investors; energy service and technology providers; insurance companies; and third party validators/verifiers.

### *IDB support for introducing the program in a country/sector*

With the support of the Government of Denmark and other donors and sources, the IDB is able to support the introduction of the intervention package in a number of countries and sectors in the LAC region.

Each intervention in a given country and sector will comprise a number of steps that use the standardized package of interventions as a point of departure to develop a tailored package:

- Analyze the energy efficiency potential and market opportunities in order to select sector and technology focus. Assess EE service providers and value chain.
- Identify a suitable “champion” in the country with a relevant mandate and capacity to structure and implement a program.
- Engage key ministries and ensure alignment with government’s development and energy priorities. Assess the regulatory/policy framework in order to identify enablers and barriers.
- Identify and engage technology solution and energy service providers and other key market actors, including end-users, commercial financial institutions, insurers, and validators/verifiers.
- Engage the insurance industry in developing/adjusting appropriate insurance products; adapt standard contract and other elements of the package to local market and regulatory conditions.
- Provide training and technical support to the coordinating entity, to the independent verifier, local FIs, and energy service/technology providers.
- Raise awareness, link market participants and support project pipeline development.
- Assess available financing options and where relevant introduce additional financing opportunities such as a credit line with IDB. Analyze the need for additional

financial risk mitigation, e.g. in the form of a credit guarantee.

Once an agreement has been reached to introduce the program in a country and sector with a given national counterpart

institution, the technical elements of the intervention can be carried out within a year. Development of a new financing line with IDB is likely to require more time. However, often existing financing can be leveraged.

### *International elements*

The Energy Savings Insurance Package has generated significant international interest, and has been recognized by the Global Innovation Lab for Climate Finance (<http://climatefinancelab.org/>) as one of the most promising instruments to mobilize private climate-friendly investment.

International cooperation and outreach is a cornerstone principle of this initiative, and discussions are maintained with governments, national development banks, and international institutions and initiatives.

With a view to further developing the interventions, consultations are also being undertaken with institutional investors, international reinsurers, technology providers and certification organizations.

A regional knowledge management platform is envisioned to disseminate knowledge and experience that can be used by interested actors at country and sector level. The IDB is also engaged in sharing experience with regions outside Latin America and the Caribbean.

*For more information, please contact*

#### **Maria Netto Schneider**

Capital Markets and Financial Institutions

Inter-American Development Bank

mnetto@iadb.org

Tel. +1 202 623 2009

#### **Jose Juan Gomes**

Capital Markets and Financial Institutions

Inter-American Development Bank

joseg@iadb.org

Tel. +1 202 623 3634