Environmental financing in Rwanda

Presentation to staff responsible for planning, budgeting and public investment in MINECOFIN

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Structure of Presentation

- Environmental financing and its importance
- Main findings from Rwanda's first

  Public Environmental Expenditure Review (PEER).
- Existing and potential Environmental Fiscal Reform (EFR) and their benefits
- Operationalising the National Fund for Environment(FONERWA)
- The strategic role for MINECOFIN in improving environmental financing

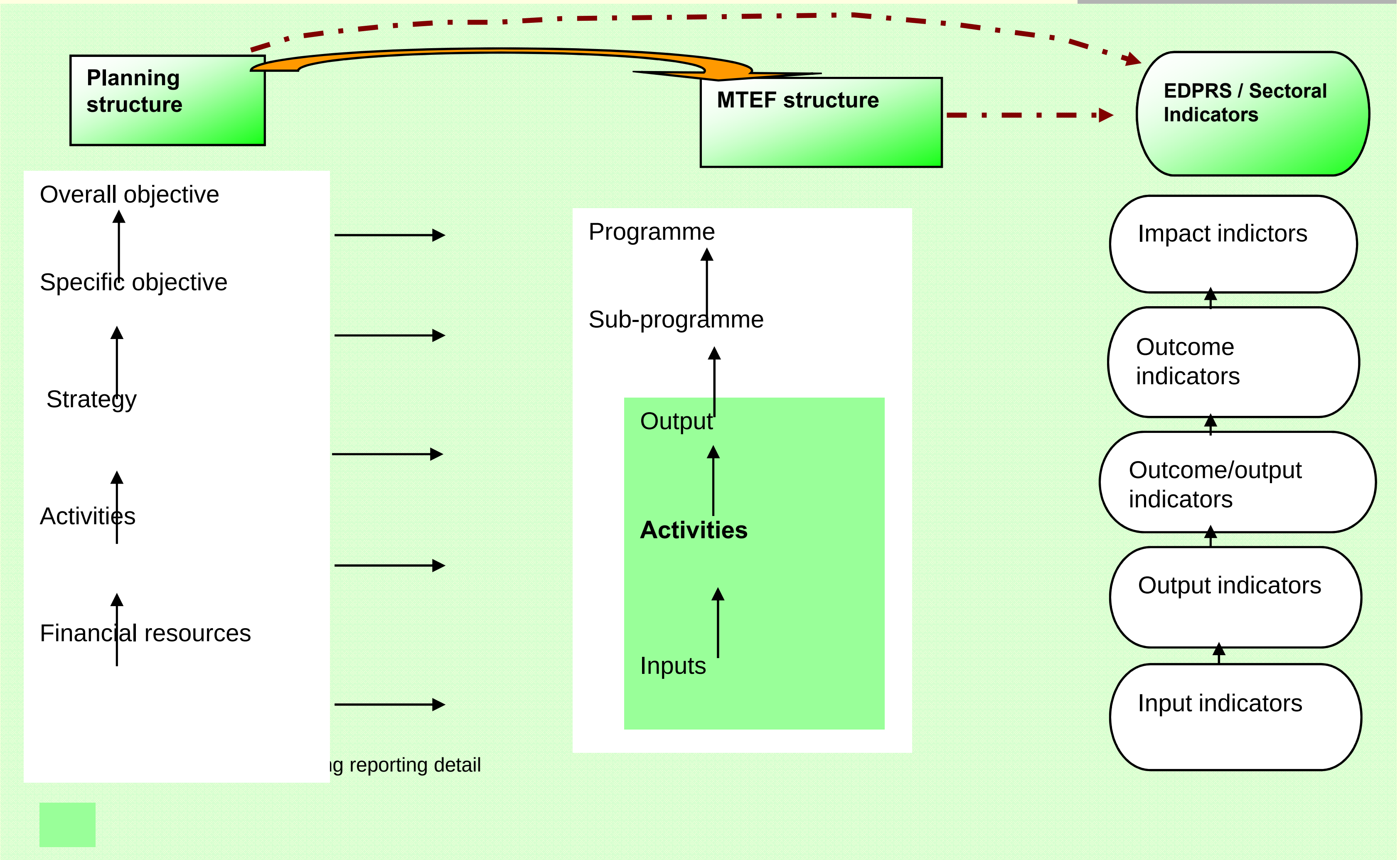
Environmental financing and its importance

- Environmental financing broadly refers to the financing provided to address environmental issues
- It is important because generally environmental issues have been marginalised in public spending and yet ENR are the mainstay of development.
- The motivation to focus on environmental financing also arose because it takes **long time** to register positive impacts on the environment, hence the need for **affirmative action** to help communities and firms shift from degrading practices to less degrading ones
- Environmental financing has also been a favourable instrument for protecting global commons e,g biodiversity through GEF.

Findings from Public Environmental Expenditure Review

- MINECOFIN has emphasised Public Expenditure Reviews in general to inform Joint Sector Reviews.
- There are many similar reporting requirements which could be rationalised to make cost effective use of time, resources and manpower.
- The existing National Planning, Budgeting and MTEF Guidelines offer entry points for improving planning and budgeting for environment and linking them to indicators.
- Despite the difficulty of disaggregating expenditure for environment, there are some few salient lessons to register

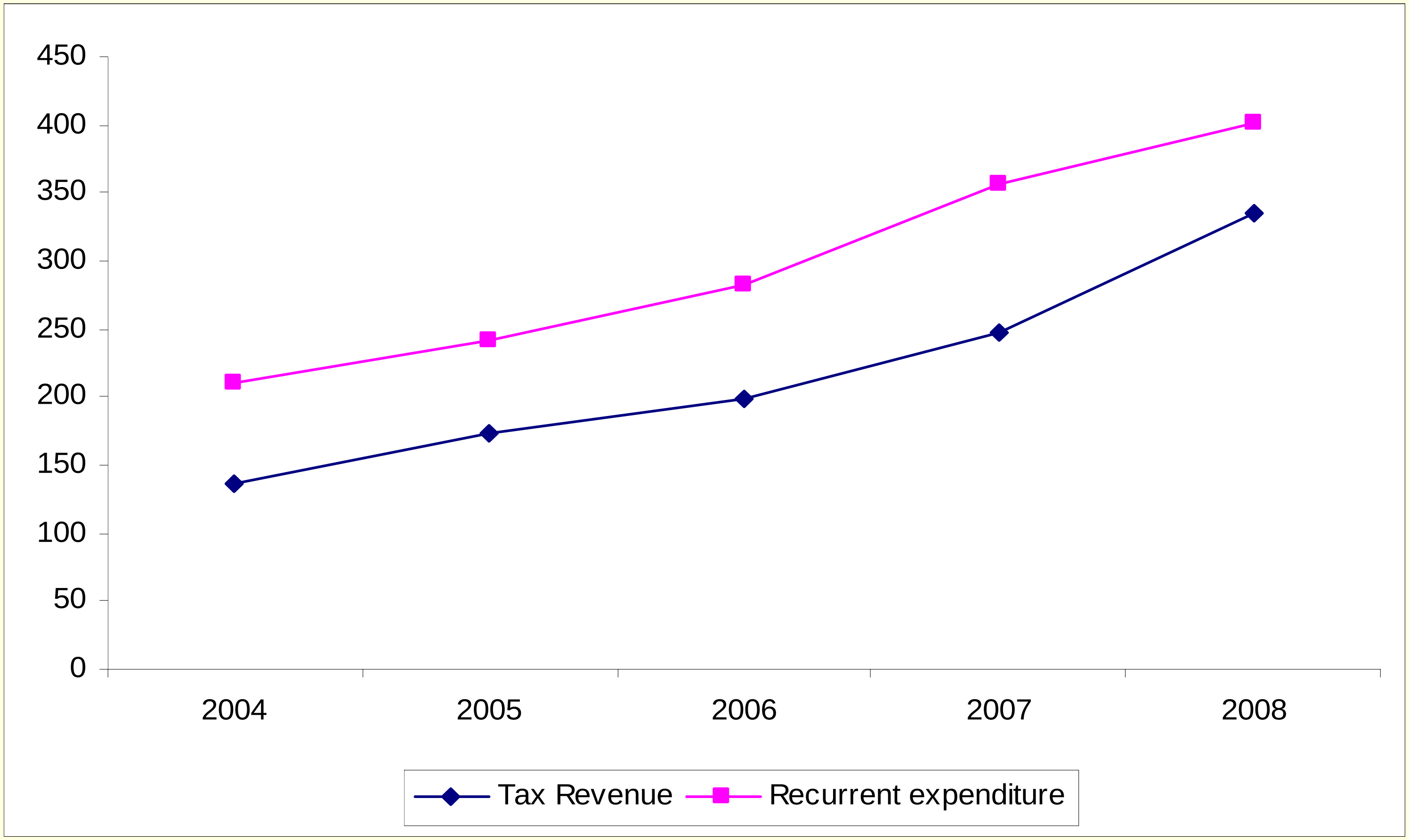
Great potential to reflect environment in planning, MTEF and indicators using existing guidelines



From the revenue side, PEER revealed that…….

- Both tax revenue and ODA has been on the rise and projected to continue
- The tax revenue as a ratio of GDP is 14.1%, making Rwanda the median country in EA, rivaled by Kenya (18.4%), Burundi (17.4%) but surpassing Tanzania (12%) and Uganda (12.6%).
- But that ratio projected to stabilise at 12.8% because RRA has exhausted its capacity for revenue collection. Additions will have to come from GDP growth, with increase in disposable income.

But tax revenue not yet able to cover recurrent expenditure, leaving the country open to vulnerability of foreign aid



Extra-budgetary funds

- Their true levels not known.
- It is government's desire to harmonise and rationalise them under one consolidated account.
- Likely funds for Climate change.

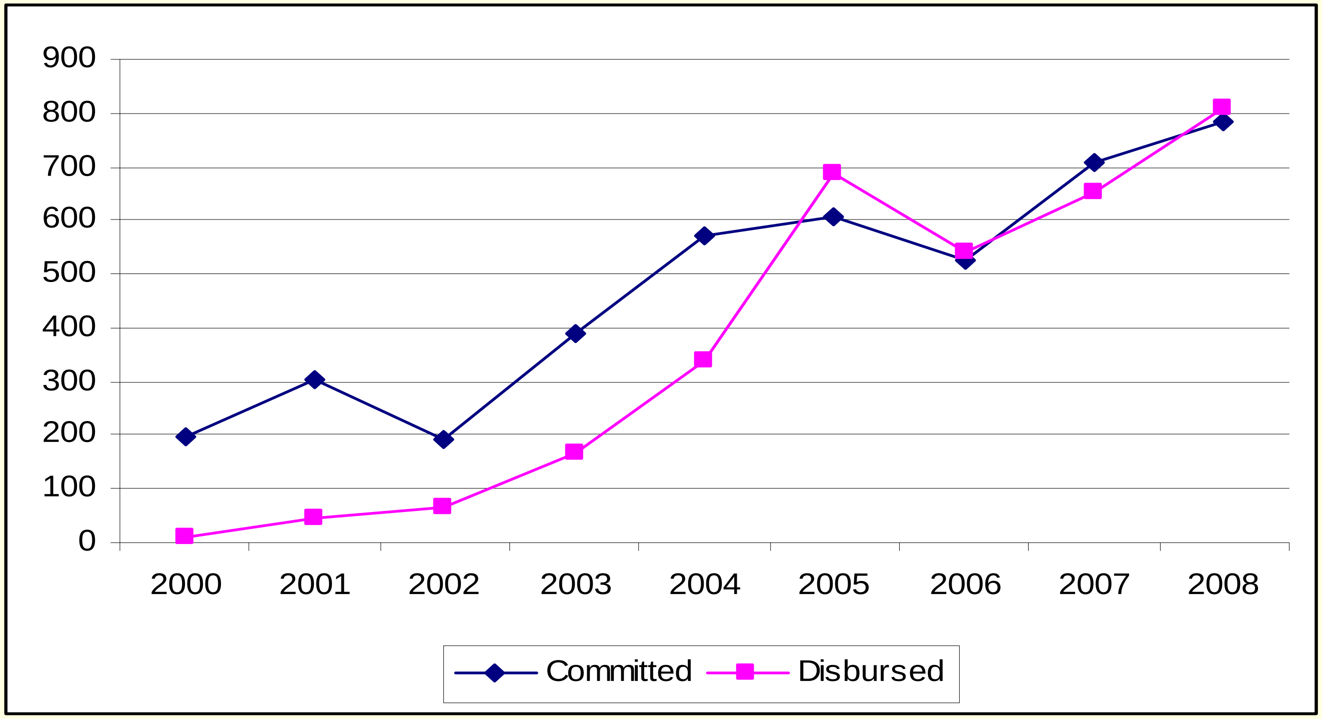
Aid context, patterns and trends

- Rwanda is a favourable recipient of ODA and it should use it as an opportunity to equally fund environment.

Country	Per Capita ($)	ODA as a % of GDP	ODA as a % of gross capital formation
Burundi	48	48	400
Kenya	22	3.8	22.3
Rwanda	64	25.6	121.9
Tanzania	39	11.1	58.6
Uganda	42	14	56

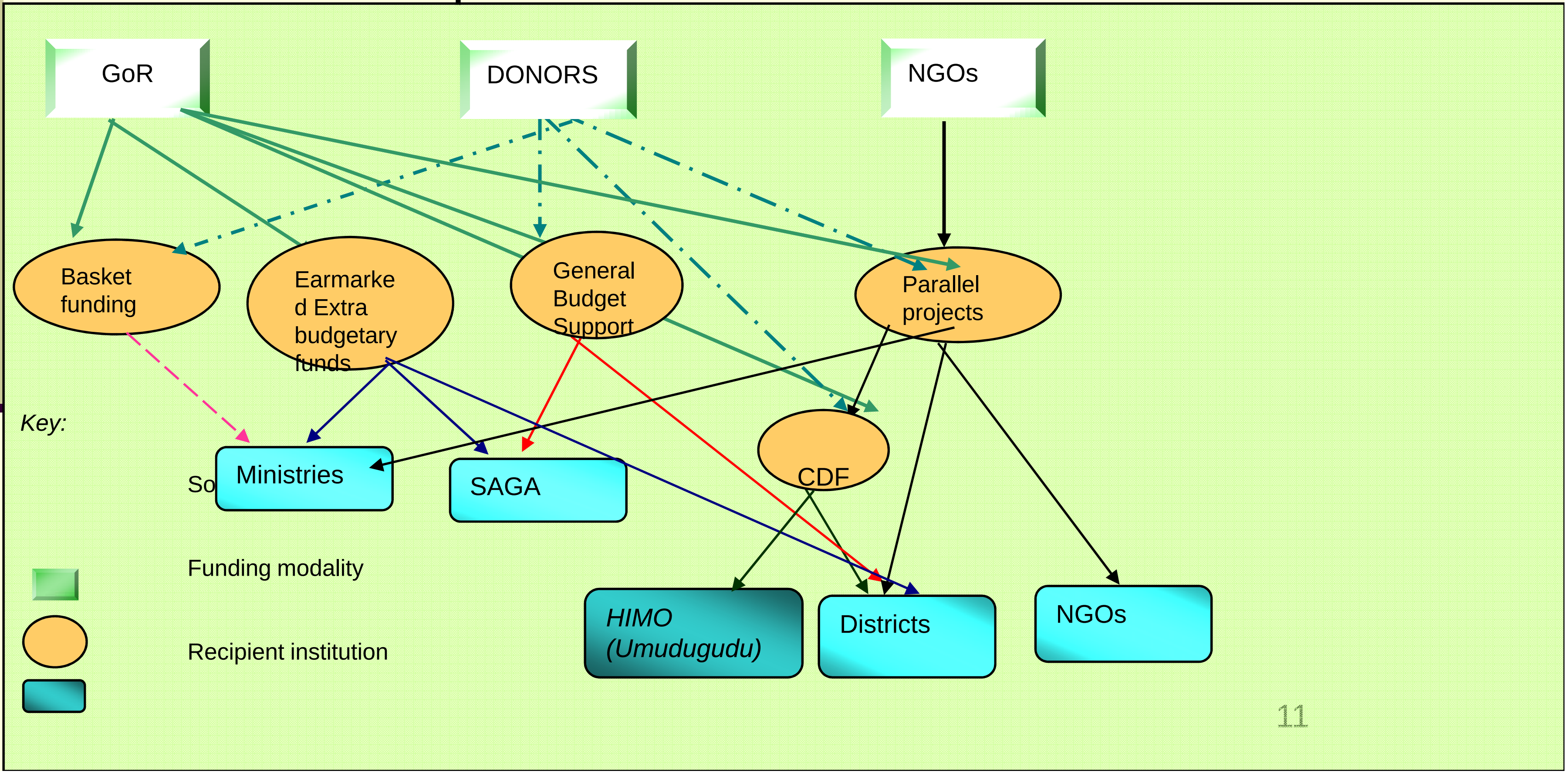
Aid context, patterns and trends

- Predictability is also improving and that builds confidence in programming



Aid context, patterns and trends

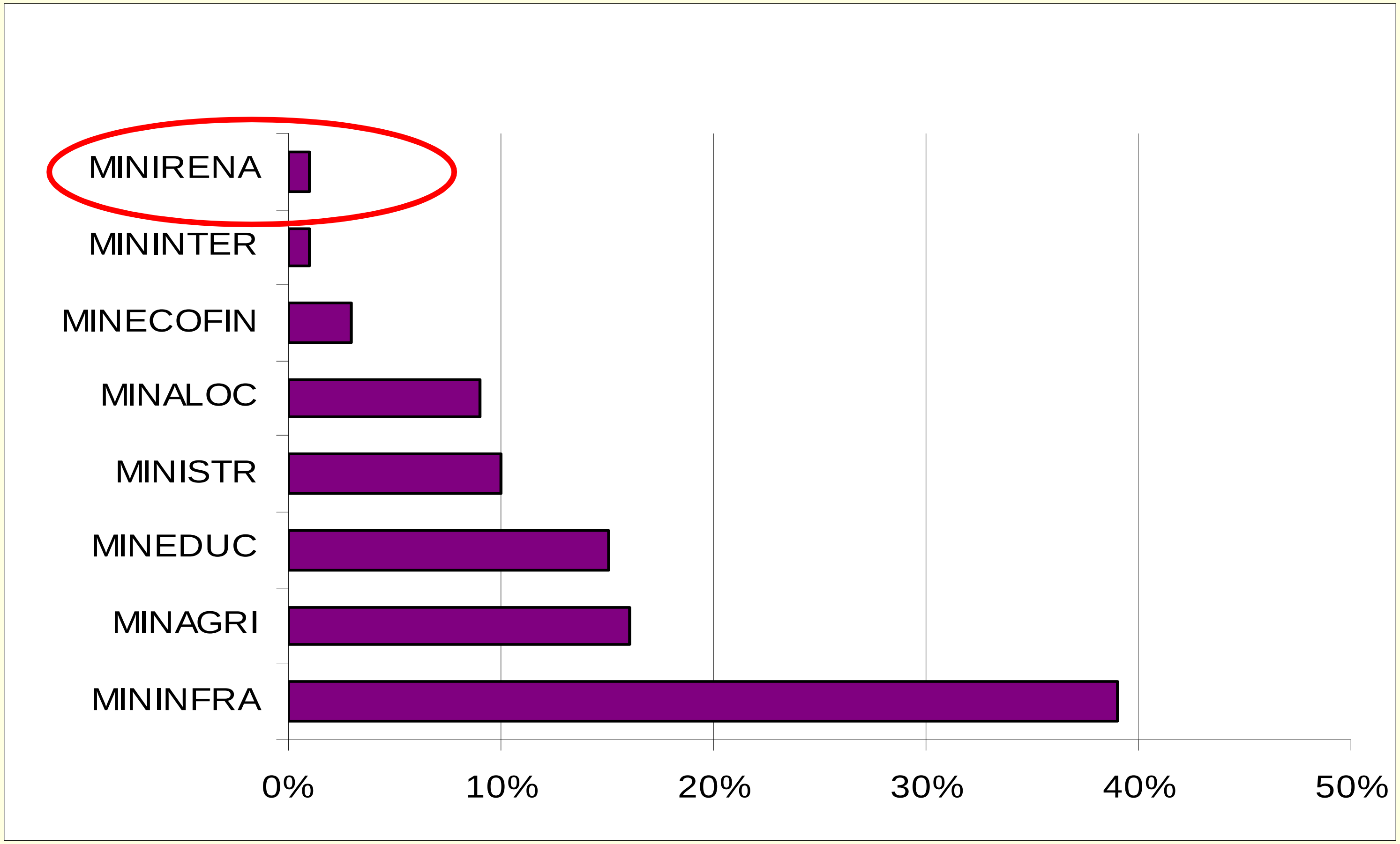
- Multitude funding modalities exist, complicating tracking of environmental expenditure



Proportion of ENR expenditure under MINIRENA

	2005	2006	2007	2008
Total government expenditure	241,382	313,192	419,701	521,135
Recurrent	241,382	281,531	356,022	401,922
Development	_	34,963	63,679	119,217
MINIRENA's total	**2,666**	**7,478**	**12,210**	**4,210**
Recurrent	2,666	3,280	2,556	2,986
Development		4,198	9,654	1,244
MINIRENA's % share	1.1	2.4	2.9	0.8
Recurrent %	1.1	1.2	0.7	0.7
Development	_	12.0	15.2	1.0

Where did the highest dev. budget go in 2008, and with what implications?



Intra-sectoral expenditure, 2008, shows that conservation and protection of environment took 40% while IWRM lost out

	2007	2008	2007	2008
1.Land planning and management	1,026.75	1,052.94	8%	25%
2. Conservation and protection of the environment	556.25	1,682.42	5%	40%
3. Forestry resources	412.60	472.78	3%	11%
4. Water and sanitation	9,171.88	178.97	75%	4%
5. Mining and geology	445.41	376.97	4%	9%
6. Service and management support	597.21	446.53	5%	11%
MINIRENA	**12,210.09**	**4,210.61**	**100%**	**100%**

Source: MINECOFIN Budget execution report, 2004-2009

Other sector's budgets addressing some environmental aspects

- MINAGRI promoting sustainable agriculture
- But it needs to study the extent to which fertilisers are absolutely necessary.
- Cancellation of pesticide subsidies in Indonesia saved the government $100 million. At the same time it did not result in a fall in output of rice – in fact output increased by 3 million tons. Complementing the subsidy was a program of Integrated Pest Management which cost about $5 million a year and reduced the growing problem of pest resistance.

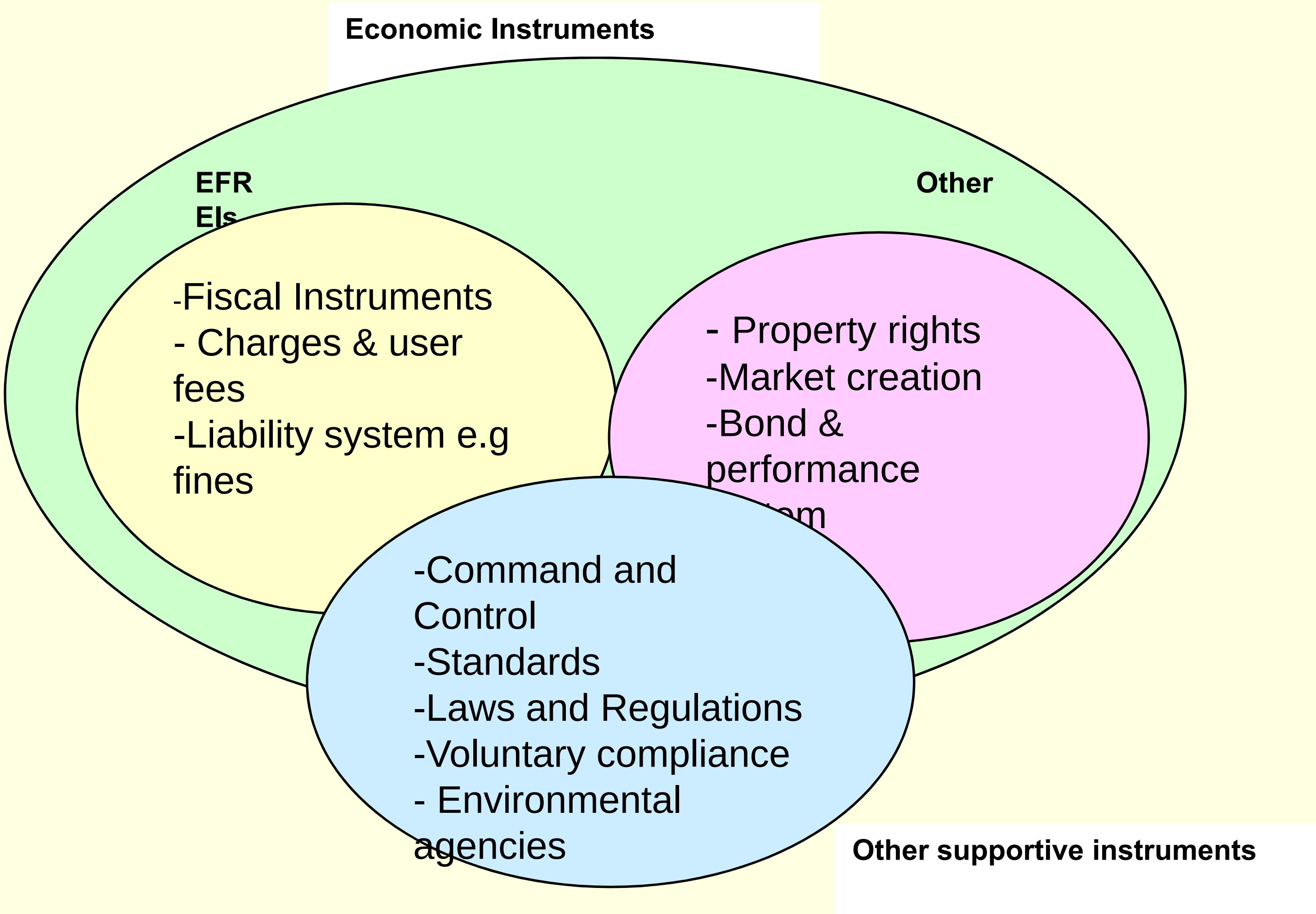
Other sector's budgets addressing some environmental aspects

- MININFRA now spending to shift population from more polluting energy technologies to less polluting ones
- Among others, MINICOM is also spending to put in place environmental standards
- CDF is spending for erosion control
- Districts are investing in erosion control and afforestation
- The main lesson is that with increased awareness, sectors could do much more and much better

The role of environmental fiscal reform (EFR) in sustainable development

- Environmental Fiscal Reform (EFR) refers to a range of taxation and pricing measures which support environmental management, and can raise **fiscal revenue**. e,g landfill charges by Kigali City Council.
- EFR are a sub-set of economic instruments
- Economic instruments (EIs) are policy instruments which influence investment and consumption decisions in a way that alternatives chosen lead to an environmentally more desirable situation than in their absence. This is because they affect **costs** and **benefits.** e.g tax exemption on cars that carry more than 14 passengers in Rwanda
- EFRs/EIs are complemented by other instruments

Environmental Fiscal Reform



Functions of EFR/EIs

- To act as **incentives** to stimulate, reward, and motivate environmentally good practices. e.g GoR exempts solar equipment and accessories from customs duty.
- To act as **disincentives** to discourage environmentally bad practices in accordance with the **polluter- pays-principle** e.g the more the pollution, the higher the pollution charge on effluents.
- To ensure that those who harvest natural resources or get environmental service pay real values in accordance with the **beneficiary –pays- principle** e.g mining royalties
- To raise some revenue e.g levy on fuel

Benefits of Environmental Fiscal Reform

Poverty reduction

-Addressing environmental problems that affect the poor

-Improved access to environmental Infrastructure (e.g water access)

-Finances for pro-poor investments (e.g education, road maintenance)

EFR

Environmental Benefits

-Incentives for sustainable NR management

-Incentives for curbing deforestation

-Funds for environmental agencies and Investments e,g FONERWA

Fiscal benefits

-Revenue mobilization

-Reduced distortions

-Reduced drains on public finances

-Allowing private sector paricipation

Examples from Rwanda and elsewhere

- Providing secure **property rights** promotes mobilisation of private capital, and Pubic-Private Partnerships (PPPs) e.g giving permits for collecting waste in Kigali to private companies like COPED, Cooperatives and associations

Examples from Rwanda and elsewhere

- In turn, the "bads" (waste) are turned into "goods" (manure, recycled products) in addition to creating employment
- More property rights to allow communities sustainably use marshlands are proposed under Marshlands Draft Law
- Additional property rights are proposed for water use for irrigation .

- *Turning waste into goods*

Scope exists to further privatize and modernise waste management through long term concessions

Examples for Rwanda and elsewhere

- RECO **subsidises** waste, allowing access by the poor
- Smart **subsidies** stimulate private sector resources in ENR investments that give returns after long time e.g commercial forestry
- Subsidies and grants could be proposed to promote land consolidation

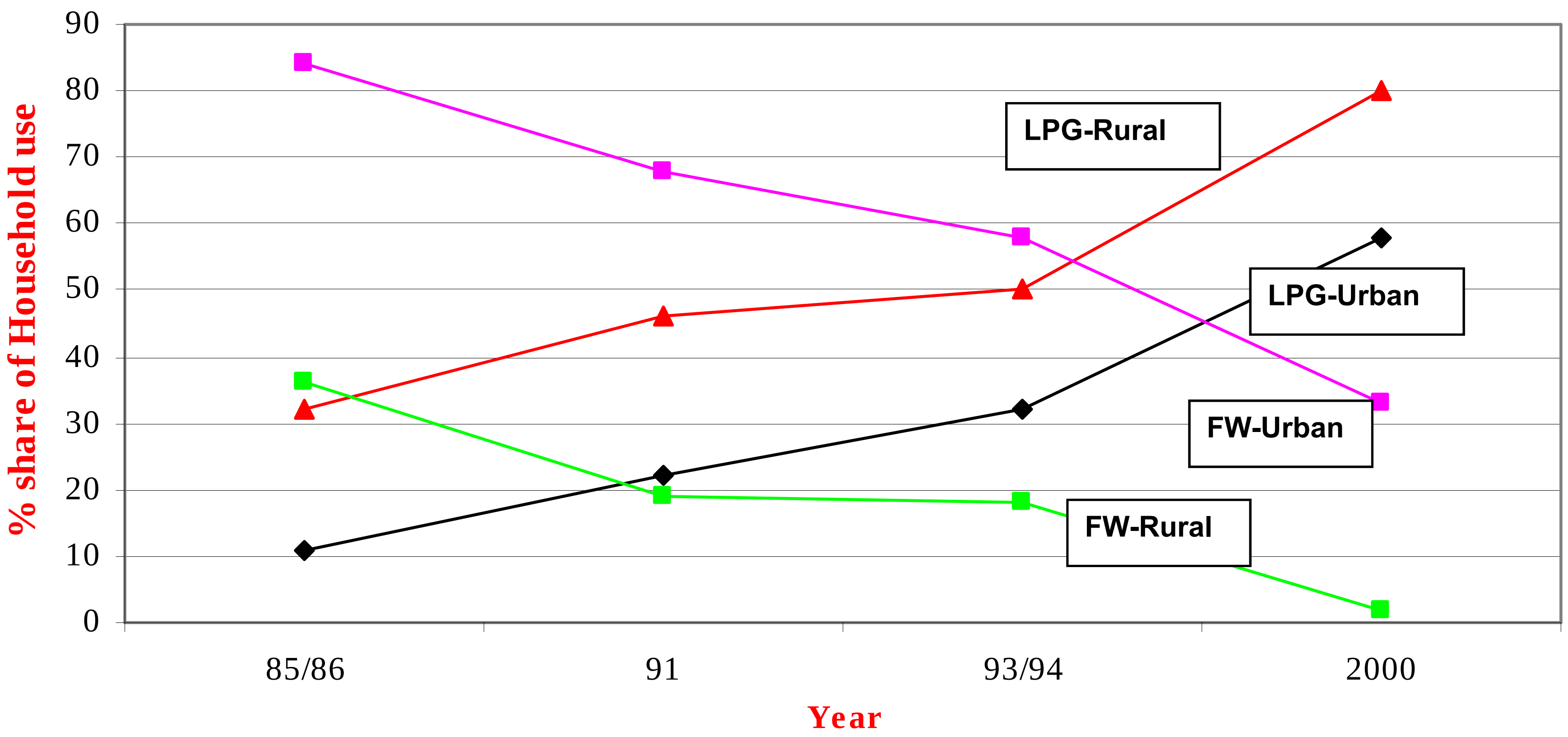
Examples for Rwanda and elsewhere

- **Tax exemptions** generally and those for environment are attracting investment in Rwanda
- Under VAT Law, government exempts water supply for non-profit organisation
- Tax exemption could also apply to garbage trucks, as was the case in Kenya, Tanzania, Uganda in 2008 budgets

Examples for Rwanda and elsewhere

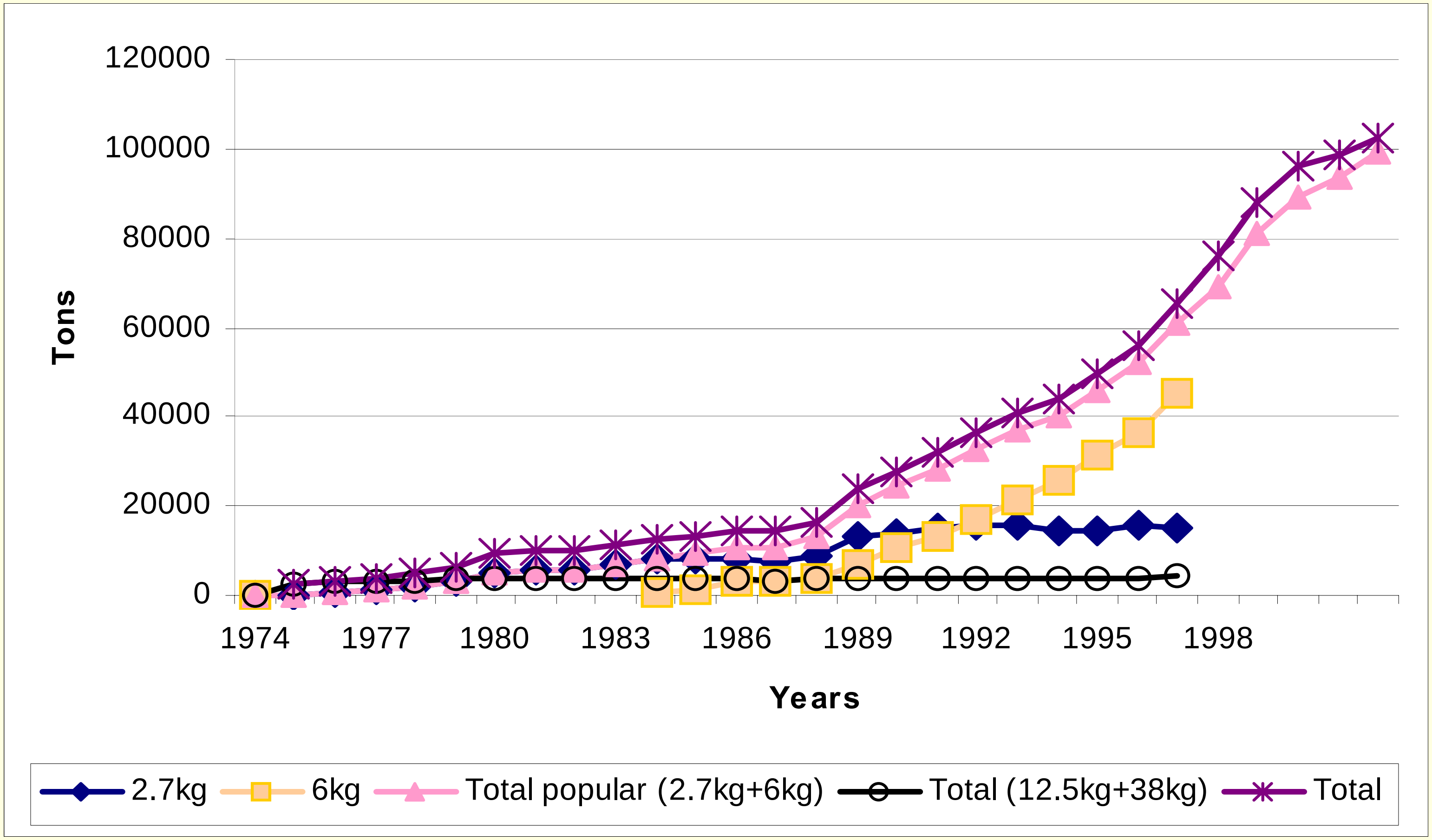
- **Substitution** from more polluting to less polluting products now promoted
  - Tax exemption on cars that cars that carry more than 14 passengers
  - Tax exemption on solar equipment
  - Tax exemption or subsidies could also be given for LPG

LPG displaces firewood in urban and rural Botswana



Source: Ogunlade R. Davidson [2007]

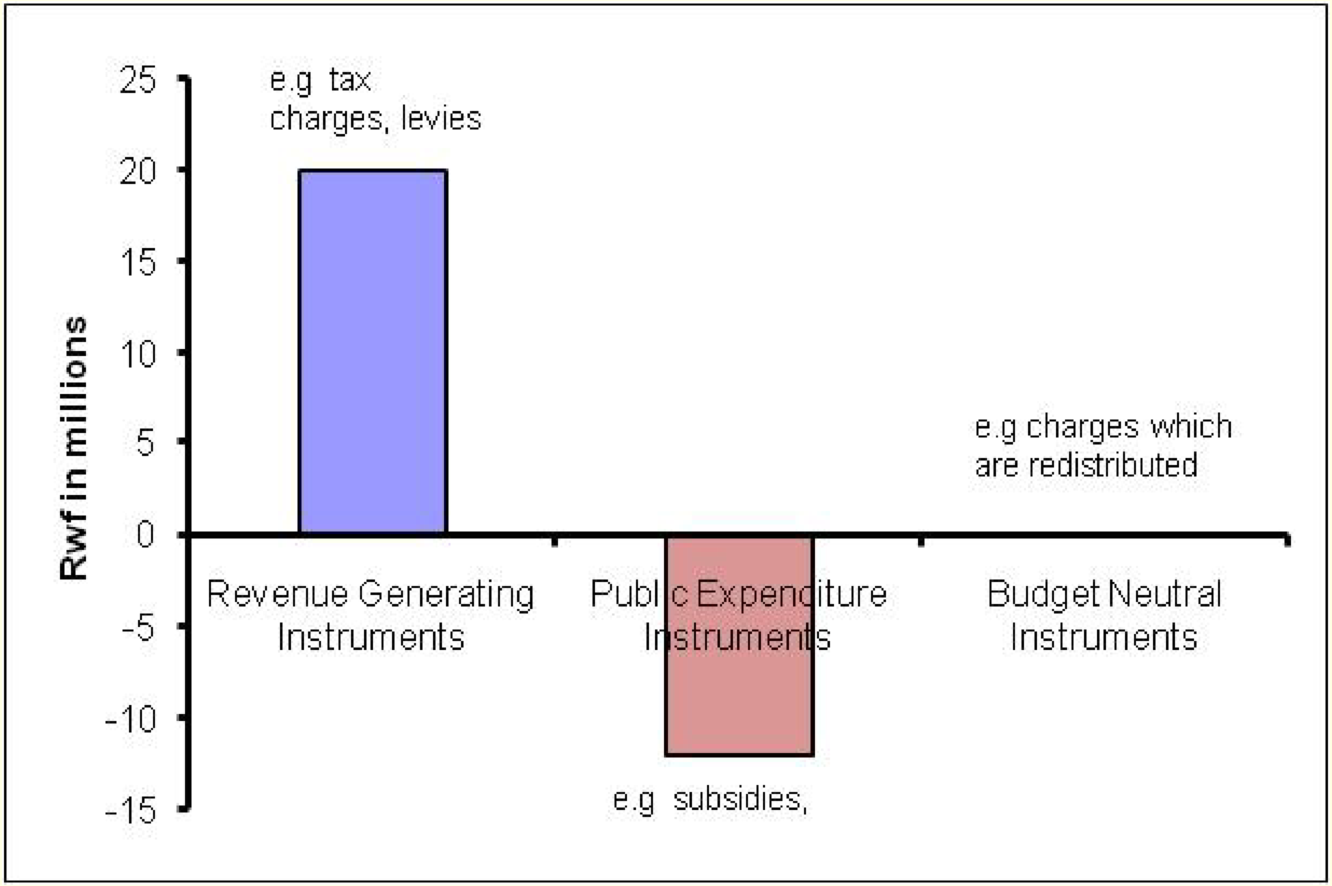
In Senegal LPG cylinders were tailored for the poor to allow the incentive benefit them



Examples for Rwanda and elsewhere

- Revenue is being raised and partly reinvested in the sector e.g
  - 25% of Forestry Fund to local governments, 75% to NAFA
  - User charges raised for electricity and water
  - Dumping fees to KCC
- There is scope for more environmental tax revenue

Financial impact of EFR/EIs on Government Revenue



Conditions favouring EFR/Eis

- Supportive policy and legal framework e.g the polluter-pays- principle, investment laws, sectoral laws,
  - Organic Law No 4/2005
  - Investment Code
  - Fiscal laws e.g VAT, Customs, Income and Consumption.
- An efficient operating market with many actors e.g many cooperatives, associations, private firms in solid waste management in Kigali
- Standards e.g for industrial effluents before introducing pollution charges

Conditions favouring EFR/EIs

- Institutional mechanisms for resolving conflict between the polluters and the polluted e.g RURA
- Macroeconomic stability e.g maintaining general price level through the control of inflation.
- Administrative feasibility e.g for collecting the taxes, fees, charges, fines and reporting on them
- Political feasibility e.g demonstrating equity, pro-poor sensitivity, gender sensitivity, supportive of growth and investment and alignment with national priorities.

When NOT not to use EFR/EIs

- In case of monopolies, monopsony
- In case of Government institutions receiving soft budgets with no incentive to be efficient
- When capacities are still weak e.g to monitor compliance to standards among informal enterprises

What to avoid in EFR programme

- Hurting the poor (so, put in place mitigation or flanking measures)
- Getting over-interested in revenue and ignoring whether environmental objectives are also being met
- Creating distortions or perverse incentives

Operationalisation of National Fund for Environment (FONERWA)

- In 2005, the GoR enacted Organic Law No 4/2005 determining the modalities of protection, conservation and promotion on environment in Rwanda.
- In order to give effect for its implementation, the government proposed the establishment of two institutions under specific laws, namely Rwanda Environment Management Authority(REMA) and National Fund for Environment, in French abbreviated as FONERWA.

Progress in establishing the institutions

- The Organic Law No. 04/2005 for environment called for establishment of 2 institutions under specific laws.

REMA	✓	**Law No. 16/2006**
FONERWA	**x**	**Bill to be passed**

- A Bill for FONERWA was made in 2008

Recent developments

- Steps towards improving the generation of internal and external revenue
- Progress towards an integrated financial management system
- The existence and proposal of other specialized non-budgetary funds with similar objectives e.g National Forestry Fund, the National Water Fund
- The emerging opportunities of international environmental funds like Climate Adaptation Fund
- A new commitment to sustainability by “greening” the performance of the Rwandan economy through low carbon growth path in search of competitiveness
- Rationalisation of donor funding under the “division of labour”

Way forward for operationalisation of FONERWA

- With all the above a concept note is being drafted by REMA and it will serve as basis for drafting the law establishing FONERWA:
  - the rationale and value-addition of FONERWA
  - the scope and financial structure of FONERWA
  - capitalisation and financial sustainability of FONERWA
  - Eligibility criteria for FONERWA funding
  - Standards for performance, transparency and accountability
  - the institutional and management aspects
  - the laws that would need to be harmonized with establishment of FONERWA

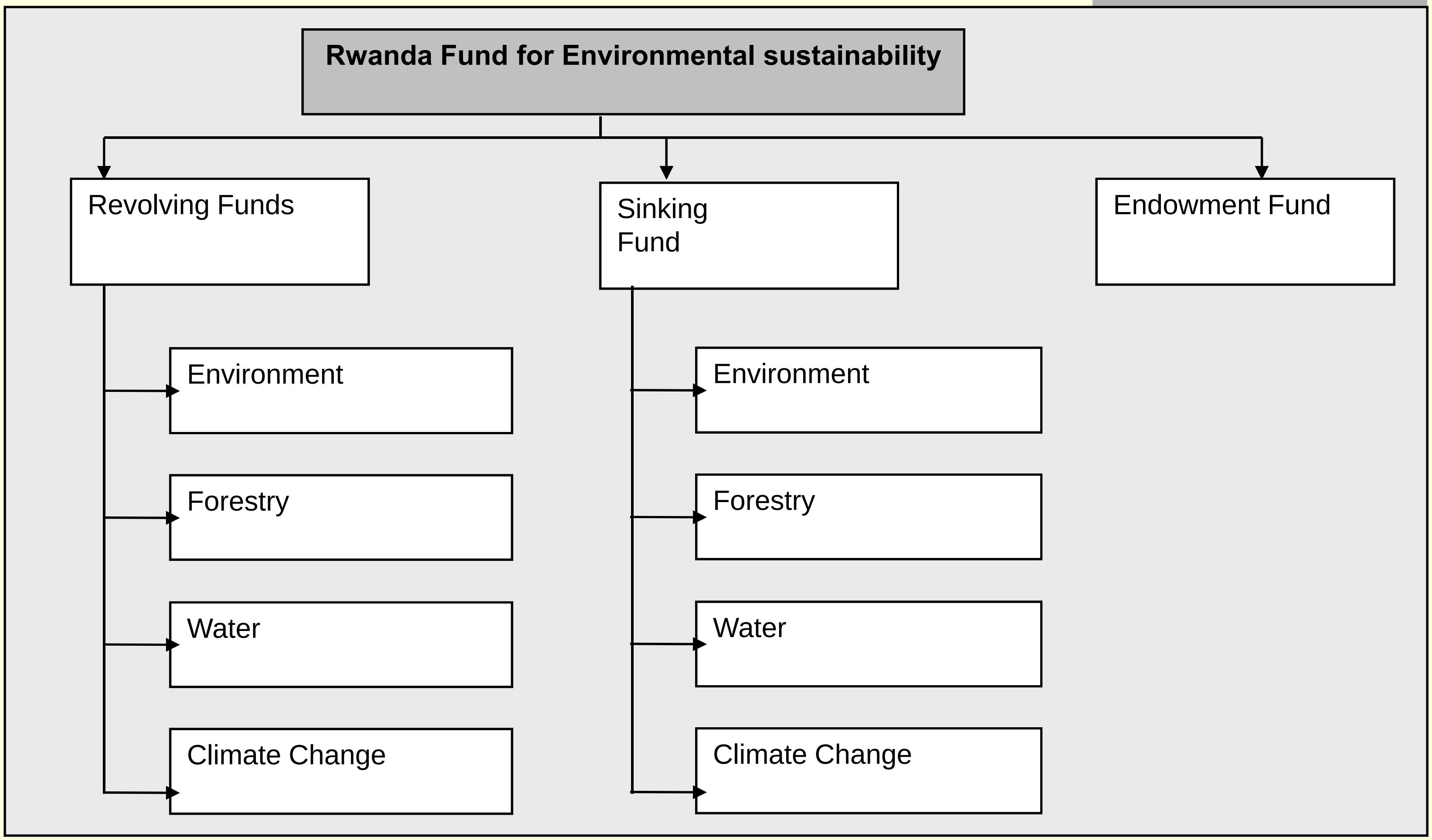
Key features given to FONERWA by Organic Law No.04/2005

- National character
- Responsibility for soliciting and managing funds in the name of environment
- Diverse beneficiaries to serve, including government services, private sector, coomunities and individuals
- Basis for charging levies,e.g for EIA
- Subsumes some activities under the National Forestry Fund and National Water Fund

Organic Law 04/2005 created high capitalisation demands for FONERWA

- Give incentives for environmental activities by individuals, associations, and public services
- Training, research and awareness creation
- Awards of excellence in environmental management
- Grants for conservation and environmental management
- Rehabilitate degraded ecosystems

Government could consider merging the Funds



Lessons from other countries on capitalisation

- EFs have been capitalised from diverse sources

Bwindi	1992	US $ 4m, GEF
Mexico	1994	US $ 20m, USAID US $10m Government
PERU	1992	US $17 debt for nature swap
Romania	2002	US $ 6m, Environmental taxes
Trinidad and Tobago	2002	US $ 7m, Green levy on all enterprises
POLAND	1998	US $540m pollution tax

Environmental Funds have grown-1

Bwindi	1992, US $ 4m	2008, US $ 10m	-interest earnings
Romania	2002, US $ 6m	2006, US $ 54m	Env. Taxes
Slovenia	1998 є 22m	2003, є 28m	•Loan repayment •Interest on loan
Lithuania	1998, є 1m	2002, є 4m	•Pollution charges •Loan repayment with charges

- Environmental funds can also be vulnerable to global and market changes e.g Bwindi during financial crunch,2008

Environmental Funds have grown-2

- National Environment Fund, Ghana

Billion cedis	2002	2003	2004	2005
Consolidated Fund	4.66	6.20	6.07	6.47
National Environment Fund(NEF)	1.78	5.03	8.73	10.38
Total	6.44	11.23	14.80	16.85
NEF as % of consolidated fund	38	81	144	161

Environmental Funds have grown-3

- Internally generated funds, NEMA Kenya, million shillings

	Recurrent grant	Development grant	Internally generated funds	Donor funds	Total
2004	220	7	11	2	240
2005	287	9	45	17	358
2006	274	15	78	14	381
2007	267	4	106	11	398

The strategic role of MINECOFIN in PEER

- Build the capacity of sectors to periodically carry out public expenditure reviews, including PEER
- Support the generation of key **outcome** indicators for environment to serve as basis for measuring effectiveness of expenditure
- Continue to bring all expenditure on budget
- Provide clear guidelines on how some sectors can shift some of their expenditure to the private sector e.g expenditure for cooking stoves

The strategic role of MINECOFIN for EFR

- Assign responsibility for closely monitoring the impact of existing EFR and/or identifying new ones among some of its staff (e.g Treasury in South Africa)
- Build strategic alliances with REMA, RRA, RDB, RBS, Private Sector Federation so as to reach decisions on EFR cost-effectively and to mitigate against resistance
- Continue to invest in reporting on extra-budgetary funds including revenue generated by ENR

The strategic role of MINECOFIN for EFR

- Support processes that can trigger additional external incentives and resources
  - GEF funds
  - Funds in the name of climate change e.g REDD
  - Funds under Clean Development Mechanisms and payment for ecosystem services

The strategic role of MINECOFIN with regard to FONERWA

- Guide the establishment of FONERWA by committing some reasonable start-up government subvention as FONERWA is challenged to broaden its capitalisation using internally and externally mobilised funds.

MWAKOZE