Introduction of SWAp in environment sector

Module 3. Financial planning in practice

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Session 1

MEDIUM TERM EXPENDITURE FRAMEWORK

Public Finance Management (PFM)

- The budget and how it is converted into spending is a cornerstone of SWAps: sector policy and the associated sector budget are seen as two wheels, with public finance management as the axis in between (JLP)
- The expenditure framework makes a sector development programme operational
- It ensures that proposals in the sector action plan have been properly costed and prioritised against a realistic estimate of (government and external) resources available
- PFM underlies all government activity. It encompasses the mobilisation of revenue; the allocation of these funds to various activities; expenditure; and accounting for spent funds
- It is time to adopt a realist approach less driven by idealistic models of budget-policy links and advanced budget techniques, and more based on dialogue and initiatives for reform that are tailored to country conditions as well as the capacity and willingness to change (JLP)

Medium Term Expenditure Framework (OECD)

- There is no single, concise definition of the term „MTEF". Rather, it represents a set of broad principles for sound budgeting that are implemented in different ways in different institutional settings
- Medium Term Expenditure Framework (MTEF) may be defined as a framework that combines coherently a medium term (typically 3-5 years) fiscal framework, medium term policy programs for key sectors of the economy and medium term indicative expenditure ceilings for each policy program (sector/function/etc)
- The value added of the MTEF approach comes from integrating the top-down resource envelope – normally handled by the Ministry of Finance - with bottom-up sector programs – elaborated and promoted by line ministries

Medium-term expenditure framework

- A medium-term expenditure framework (MTEF) is a system for planning actions and programming spending over a three to five-year period. It reconciles systematically the achievement of strategic objectives with respect for aggregate resource limits.
- A sectoral MTEF must be:
  - ***Comprehensive:*** all sources of financing to the sector and all proposed spending should be included.
  - ***Realistic*** so that projections of finance are not over-estimated and projections of costs are not under-estimated.
  - ***Clear about how resources will be used*** and what the desired results to be monitored will be; it must derive from a clear action plan.
  - ***Endorsed at senior political level.***

Budget planning process

OVERALL EXPENDITURE CEILING
for the public sector: 3 one year ceilings for the three upcoming years

MTEF, Medium Term Expenditure Framework
Division of the budget in policy areas (according to e.g. Functional Classification) for the three upcoming years

MTBF, Medium Term Budget Framework

for each individual ministry/Direct Budget Beneficiary (DBB)
3 one year ceilings. All financial resources included

ANNUAL STATE BUDGET

first year of the 3 years in the MTBF for the individual DBB/SU

SECTOR MEDIUM TERM PLAN

For all sector

SECTOR MINISTRY PLAN

for the same ministry/DBB, 3 one year ceilings for each institution

OPERATIONAL PLAN

for the same ministry/DBB, 3 one year ceilings for each institution

MTEF core elements (1)

- A unified „whole-of-government" approach that encompasses all sectors
- A "top-down" hard budget constraint consistent with macroeconomic sustainability that limits overall levels of spending over the medium-term. This should involve credible, realistic resource projections that are in turn based on explicit and carefully considered macroeconomic assumptions
- A „top-down" set of strategic policy priorities that together with the hard budget constraint drive, and are reviewed during, the strategic phases of budget preparation

MTEF core elements (2)

- "Bottom-up" forward estimates of the costs of existing policies, programmes and activities over the medium-term supported by expenditure reviews
- A single nationally owned political process at the centre of government that reconciles the bottom-up and top-down components, forcing policy priorities to be established within the overall resource constraint through resource allocation decisions
- A strong and clear link between MTEF projections and the annual budget process, so that multi-annual targets (duly updated for changes in the macroeconomic situation) set in the previous years should form the basis upon which the budget is prepared. Ideally, there should be no meaningful distinction between the MTEF and the budget process: they should be one and the same thing

MTEF core elements (3)

- A focus on results (i.e. outputs and outcomes) rather than on financial inputs both in the structure of the budget and in terms of accountability:
  – Sector managers are given more predictable flow of resources coupled with more discretion over detailed budget management (on the basis that they have an informational advantage as to how best to spend public money) and are held accountable for delivery of results
  – Budgets are structured on a programme basis with strong contestability of allocations from year to year, rather than on a traditional „line item‟ basis whereby sectors are „entitled‟ to their previous year's allocation plus some small additional increment
  – Thus, "po*licy priorities drive funding and not the other way around"*
- Many of the elements of an MTEF are inseparable from good public finance management more generally

Political process

- Budget preparation phase is (and should be) fundamentally political, because it is about making real policy choices based on societal preferences and linking them to practical plans and resources
- To make real policy choices the political process must be supported by certain technical elements, which include:
  - a medium-term fiscal framework setting out the aggregates;
  - estimates of the future costs of existing policy, and
  - sector strategies setting out sector and sub-sector priorities for future spending.
- Not all of these technical elements are going to be in place at the start of an MTEF process, but making progress towards them is a critical part of early MTEF development

Role of sectoral ministries

- Setting the medium-term fiscal targets and sector ceilings is usually a responsibility of the Ministries of Finance and/or Economy
- Estimating the costs of future policies and sector strategies and programmes lies with line ministries
- This is the entry point for the sectoral ministries in the MTEF process and depending on the quality of the financing strategies and programmes prepared by these ministries, the programme cost estimates could be used as a basis for annual budget allocations

Key lessons from the OECD countries

- The potentially damaging effects of over-optimistic assumptions about future economic growth. OECD experiences point to the importance of conservative estimates for economic growth, revenue and the resource envelope
- Bottom-up budgeting alone does not fit well with a medium term approach. OECD countries have gradually moved to a more top-down approach to budget formulation, while agencies continue to prepare estimates within this framework „bottom-up"
- Political engagement is key with individual ministers engaging in decisions about allocating the top-down ceiling for their expenditure area, and much greater discipline in the parliamentary approval process
- Experience from OECD countries shows that the success of the reform process depends on the budgetary basics such as budget structure, scope and classification, accounting, information, evaluation and auditing
- In many non-OECD countries, the budget structure is too complicated, its expenditure classification too subdivided, the coverage of the budget is too limited, excluding some important fiscal activities of the government

Expenditure programming in Sweden

- As for the MTEF, there are 27 expenditure areas established in the Swedish budget system
- Previously, the appropriations were divided by responsible ministries
- The 27 expenditure areas were proposed by the Parliament, which wanted a clearer presentation of expenditures on individual policy areas than was afforded by the division by ministry
- The structure into 27 areas was also designed to reflect the committee structure in Parliament.

List of Expenditure Areas

- The Swedish Political System
- Economy and Fiscal Administration
- Tax Administration and Collection
- Justice
- Foreign Policy Administration and International Co-Operation
- Defense
- International Development Assistance
- Immigration and Refugees
- Health Care, Medical Care, Social Services
- Sickness and Disability Benefits
- Old Age Benefits
- Family and Children’s Benefits
- Unemployment Benefits
- Labor Market
- Study Support
- Education and University Research
- Culture, the Media, Religious Organizations, Leisure
- Planning, Housing Supply, Construction
- Regional Development
- General Environment and Development
- Energy
- Communications
- Agriculture, Forestry, Fisheries
- Business Sector
- General Grants to Municipalities
- Interest on Debt
- Contribution to European Union Budget

MTEF programming in Austria

- The Austrian budget is divided into 29 chapters, including six for state bodies, independent from the Government
- This presents more flexible approach of expenditure programming, taking into account independent bodies and legislature

List of budget chapters

- Presidency of the Republic of Austria
- Parliament
- Constitutional Court
- Appellate Administrative Court
- Ombudsman
- Federal Court of Audit
- Federal Chancellery
- Interior
- Education and Culture
- Art
- Science
- Social Security
- Social Security Funds
- Health and Woman
- Family Policy, Generations and Consumer Policy
- Foreign Affairs
- Justice
- Defense
- Finance
- Cash Management
- Taxes
- Intergovernmental Fiscal Relations
- Government Property
- Pensions (for civil servants)
- Federal Debt
- Agriculture, Forestry and Water Management
- Environment
- Economy and Employment
- Transport, Innovation and Technology

Government Expenditure by Function (Serbia)

Table 6. Consolidated General Government Expenditure by Function					
As % of GDP	2005	2006	2007	2008	2009
General public services	4.2	5.3	4.2	4.3	3.8
Defence	2.4	2.4	2.5	2.3	2.3
Public order and security	2.3	2.5	2.5	2.3	2.1
Economic affairs	5.5	5.9	6.6	6.3	5.4
Environment protection	0.2	0.3	0.3	0.3	0.3
Housing and community	1.5	2.0	1.8	1.6	1.6
Health	5.7	5.9	6.6	5.9	5.9
Recreation, sports, culture and religion	1.0	1.0	1.0	1.0	0.8
Education	3.5	3.8	3.8	3.9	3.7
Social welfare	15.6	16.1	16.3	16.8	18.1

Source: Macroeconomic and Fiscal Analyses and Projections Department

Situation assessment

- *Public Expenditure and Financial Accountability Assessment, Public Financial Management Performance Report, November 2010*
- Although the MTEF in the Memorandum allows for the establishment of budget ceilings, the translation of these budgets ceilings into Line Ministry budgets that are fully reflective of a policy framework developed through sector strategies and an integration of investment and recurrent expenditures <u>have yet to be developed</u>
- The current MTEF emphasises the top down element whereas the lack of an overall policy based budget, notwithstanding pilot programme budget in five ministries, ensures it is <u>only a partial MTEF</u>

Budget Planning

- There is need to improve planning and budget formulation in line ministries to fully reflect policy priorities established through the MTEF
- **Specific attention needs to be directed at formulating costed sector strategies and improving the overall capacity to implement the investment cycle starting at the identification of project possibilities through to the selection of projects for execution linked to individual ministries‟ priorities**
- The consequence of these weaknesses are that resource allocation linked to ministerial priorities is ineffective and the centre allocates the budget as it sees fit rather than an allocation based on sectoral expertise

Preparation of multi -year fiscal forecasts and functional allocations

- Multi-year fiscal forecasts are produced as part of the MTEF process and are instrumental in the setting of MTEF sector ceilings by way of line ministry MTEF submissions
- They are also used in the setting of the (later) budget ceilings, forming a part of the Memorandum on the Budget and Economic and Fiscal Policy for the Year 2010 with Projections for the Years 2011 and 2012
- However, links between multi-year estimates and subsequent setting of annual budget ceilings are not clear

Existence of sector strategies with multi-year costing of recurrent and investment expenditure

- **Sector strategies are prepared for all key sectors but, in the absence of a functioning MTEF, they do not include costing of investments and recurrent expenditure**
- Furthermore, varying proportions of sector investments are controlled by the National Investment Programme (NIP), rendering it difficult to plan for sectoral investments
- Programme budgeting is at present a desk exercise which is not translated into the current budget process, despite the appearance of demand from the MTEF pilot ministries to move towards substantive programme budgeting
- Investment decisions are made both by line ministries under the budget ceiling but also via the National Investment Plan – a dual process, rendering any link to sector strategies tenuous. There is little evidence of any investment decisions including the recurrent cost implications after completion

Instead of summary

- Where MTEFs were adopted to translate national policy objectives into public expenditure allocations within a multi-year macroeconomic and fiscal framework, one of the main concerns in this process has been the lack of capacity of sector agencies to prepare economically-sound, medium-term expenditure programmes which achieve their objectives in an effective and efficient manner
- The effectiveness of a sector MTEF depends on the wider environment of public expenditure management. A sector ministry will not take the MTEF seriously unless there is both discipline and predictability in the formulation of government budgets and in the release of budgeted funds

Session 2. Miroslav Buncic, General Secretariat

FINANCIAL PLANNING PROCEDURES IN SERBIA

YEARLY OPERATIONAL PLAN (GOP) METHODOLOGY

- The process of **objective-based planning** or **planning based on results** relies on **the logical methodological approach** perceived in the definition of all parameters **of the logical framework and their cause and effect relations**, including envisaged mechanisms for monitoring and reporting on the implementation of the plan as basic **instruments for decision-making and/or managing**.
- **The Yearly Operational Plan** (GOP) is neither a one-off initiative nor a managerial instrument used solely by public administration institutions, but **a comprehensive document** integrating objectives of strategies and plans of national interest, including reform initiatives. Also, GOP defines **sector programs** based on **sector policies**, and as such are recognized **in the system of programmatic budget and within the three-year long medium-term expenditure framework**.

- In this regard, the contents of a yearly operational plan should represent a document developed in detail on the basis of the three-year medium-term plan. The development of each **Yearly Operational Plan** should be preceded by **an analysis stage**, both of the execution of the previous annual plan and the situation analysis including all changes or alterations occurred in the meantime, which could significantly influence the competencies, priorities and deadlines laid before the implementing parties within the public administration system.

- **Basic parameters** defined within the Yearly Operational Plan are:
- **Long-term and medium-term (general) objectives of the sector;**
- **Programmes and projects;**
- **Short-term (specific) objectives;**
- **Expected results arising from the implementation of programme and project activities;**
- **Indicators;**
- **Sources of verification;**
- **Assumptions and risks**;
- **Budget;**
- **Deadlines and dynamics of the GOP execution process;**
- **Responsible implementing parties** (institutions, organizational units, functions);
- **System of monitoring and reporting** on GOP implementation**.**

Planning Levels

- **a) Strategic planning:**
- Process of finding those solutions-**strategies** which shall provide optimal results in regard to the achievement of objectives in the domain of resource allocation;
- Continued and complex process;
- Provides necessary orientation (perceiving basic development directions of a system) and in this way helps solve the issue of resource allocation;
- Directs development and represents a policy instrument.

Strategy:

- Strategy is a methodical document representing a means for the achievement of objectives;
- Special importance is attributed to medium-term strategies in the process of strategic planning, because they encompass the so-called development stages and programme implementation (2-5 years);
- Short-term strategies relate to the period of up to a year, and their implementation is not expected to result in more significant structural changes (systematic changes);
- Long-term strategies have a percentage of vagueness and unpredictability;
- **The main weakness of strategic planning is that it is based on long-term and questionable projections increasing the level of uncertainty in planning**.

b) **Operational planning** is an aspect of planning practice **falling within the domain** of short-term planning. **The task of operational planning is:**

- To ensure regular and balanced usage of capacities and resources;
- Monitoring the level of achievement by use of indicators;
- Development and monitoring the implementation of specific methodical tasks developed for the institution on the whole and all its units.

Types of Objectives

- In relation to time:
- **Long-term**
- **Medium-term**
- **Short-term**
- General/specific objectives
- **General** objective is an objective contributed to by the ministry itself but also in cooperation with all other actors (crosscutting/national objectives)
- **Specific** objective is an objective whose achievement depends exclusively on the ministry (sector objectives)
- In relation to the level of planning
- High priority objectives, e.g. programmatic objectives
- Low priority objectives, e.g. project objectives

S.M.A.R.T.

- During the definition of each objective, parameters that provide answers to the following questions have to be taken into account:
- Is it **Specific**?
- Is it **Measurable**?
- Is it **Adjustable**?
- Is it **Realistic**?
- Is it **Time-based**?

Stakeholders Analysis:

- Identification, classification and analysis of stakehoders.

Current State Analysis (e.g. SWOT):

- Identification of key strengths, weaknesses, opportunities and threats and establishment of cause and effect relations.

Problems Analysis:

- Identification of key problems, obstacles and opportunities and establishment of cause and effect relations, finding solutions for identified problems.

Analysis of Measures:

- Identification of possible measures for reaching solutions, selection of the most appropriate package of measures.

What is a programme?

- Programme is a group of independent yet linked activities and projects with a common objective. Programme activities are defined during the planning process as most useful per time unit with the aim of achieving the common general objective and specific objectives.
- **What are policies?**
- Policies represent <u>a set of activities and projects</u> estimated to most efficiently and effectively lead to the achievement of the medium-term programme objective;
- **Ministries should develop sets of activities and/or policies and then select by use of comparative analysis the ones they estimate will most efficiently and effectively lead to the achievement of the medium-term objective.**

What is a project?

- A project is a complex and unrepeatable business enterprise (capital, development, process-oriented, system-oriented, etc.) undertaken in order to achieve objectives within an envisaged period and with envisaged costs. It is a set of activities mutually linked and organized in such a way as to lead to the achievement of the project objective, implemented in a set timeframe and which have predefined necessary resources.

- In the context of defining a project, logical approach represents a way of thinking or cause and effect logic used in order to assess whether each project parameter is necessary and sufficient for achieving a project objective. Logical approach is an analytical process including:

- Analysis of the current state of the institution;
- Analysis of needs and capacities (own and stakeholders');
- Setting objectives;
- Analysis of alternative measures for achieving objectives;
- Formulation of a hierarchy of set objectives;
- Selection of an appropriate strategy for achieving the general objective.

Project Parameters

- Objectives (general and specific)
- Expected outcomes
- Activities
- Indicators
- Sources of verification
- Risks and assumptions
- Budget

Thank you for your attention

Discussion

WHAT SWAP REQUIRES DIFFERENT FROM EXISTING FINANCING PLANNING PROCEDURES

Session 3

COST ASSESSMENT OF ENVIRONMENTAL PROGRAMMES

NEAS. Costs (1)

- The cost calculations have largely focused on the "Heavy Investment Directives", which are:
  - Urban Waste Water
  - Drinking Water
  - Nitrates
  - Municipal Solid Waste which bundles the Landfill, Packaging, Waste Electrical and Electronic Equipment and Batteries Directives
  - Large Combustion Plants which includes both Thermal Power Plants and Heating Plants.

NEAS. Costs (2)

- The highest cost will be in:
  - Water sector amounting to €5.6 billion
  - Waste sector with €2.8 billion
  - Industrial pollution and noise sector with €1.3 billion
- Accumulated Total Cost 10.584 MEUR (CAPEX & OPEX)
- Total costs estimated 1400 EUR/capita (average 1150 EUR/capita in previous enlargement)
- The conservative estimate indicates that over the period to 2030, benefits would outweigh the costs by a factor of approximately 2.4

NEAS. Investment needs

Sector	Costs (MEUR)
Water	3505
Waste	555
Industrial pollution and noise	1101
Nature protection	56
Air quality and climate change	214
Chemicals and GMOs	59
TOTAL	5490

Why cost assessment

- Because policy implementation is related with use of resources
- We have to know, what kind of resources we need and how we obtain them
- Resources have their price
- By assessing costs, we are “pricing” environmental policy implementation
- We need it in order to ensure, that we are realistic about establishing policy goals and implementation timetables

Identification of investment projects

- Most countries have experienced period, when, from one side, country faced a lot of environmental problems, from another side – donors hardly have any projects for financing
- Identification and development of investment projects can be taken as special effort
- Results would be achieved but costs of this process in terms of time required and resources spent would be rather high
- In such case investment planning process will need to overcome all gaps environmental policy might have

Policy framework

- The EU accession process is providing clear policy frame – the environmental *acquis*
- And the approximation process requires development of implementation plans
- These plans become major source of information for investment planning

Few costs categories

Feature	Category of cost
Baseline vs. incremental	1. Baseline cost 2. Incremental cost
Approximation stages	1. Transposition cost 2. Implementation cost 3. Enforcement cost
Purpose	1. Administrative (institutional cost) 2. Investment 3. Operational & maintenance 4. Technical assistance
On whom cost are imposed	1. Public costs 2. Private costs
Versus time	1. Annualised cost 2. Cumulative cost 3. Yearly expenditure

Common approaches for cost assessment

- Very rough and quick
- Unit cost approach
- Specific detailed models

- Surveys / Questionnaires

Rough and quick cost estimate

	BG	SK	CZ	EE	H	LV	LT	PL	RO
EDC (1997) estimate	15	5.4	13.4	1.5	13.7	1.7	2.4	35.2	22
Ministries' estimate, ~2000	8.6	4.8	6.6-9.4	4.4	4.1-10.0	1.5-2.4	1.6	22.1-42.9	22
Population, million	7.7	5.3	10	1.3	10	2.3	3.4	38	21.6

- Estimated environmental financing needs in some candidate countries, billion EUR
- ≈1000 EUR/capita

Unit cost approach

Construction costs for covering	EUR/m2
Duboko feasibility study	**11,4 MEUR**
Construction costs for covering small dumpsites	15
Construction costs for medium and large dumpsites	24 (23)
Subotica feasibility study	**7,6 MEUR**
Small	14,7
Medium	18,20
Large	21,70
Valjevo feasibility study	
Small	9,90
Medium	14,7
Large	???
Excludes investigation, design and tendering	

Specific detailed models

- Usually require quite a lot of technical and financial input data
- For example, FEASIBLE was used during previous accession in several countries
- Usually black box, difficult to understand and maintain afterwards
- Good for aggregated level
- Not that useful for project level cost assessment

Surveys / Questionnaires

- When entities, for which cost assessment is needed, are very different
- Difficult to establish unit costs
- For example, for IPPC cost assessment

Investment needs (Lithuania)

- It was assessed, that Lithuania will need about 1.5 billion Euro for environmental investment to implement EU requirements
- Two thirds of this amount would be public sector costs (mainly water and waste management)
- It would mean that public sector has to increase environmental financing by some 3 - 4 times
  - Was 350 million Euro during 1990 - 2000 (1.2 billion Litas)
  - Required 1.2 billion Euro during 2000 – 2010
- In fact, for period 2000 – 2010 even more is being allocated – 1.5 billion Euro (5,2 billion Litas) and implementation will continue to some 2015
- This is not only considerable increase of spending. It also brings issue of affordability for people and institutional capacity to manage investment projects (each municipality for this period had 3 – 8 projects to prepare and implement)

Essential elements of Environmental Investment Plan

- Clearly defined objectives (specific, measurable, realistic and time-bound) and priorities.
- Clearly defined timeframe.
- State of related infrastructure.
- Needed investment actions to develop new or upgrade existing infrastructure complying with environmental requirements.
- Cost estimates of achieving the objectives (preferably, at project level).
- Criteria for projects selection and priority setting.
- Ranked list of projects.

Feedback to implementation policies

- Environmental policy is background for investment projects, but investment project design can equally impact way environmental policy is implemented
- You have alternative if to construct landfill for each municipality or develop and implement regional landfill
- How centralised or decentralised waste water treatment you want to have?
- Design of project will have implication on costs, both investment and operational, on legal framework and institutional arrangements

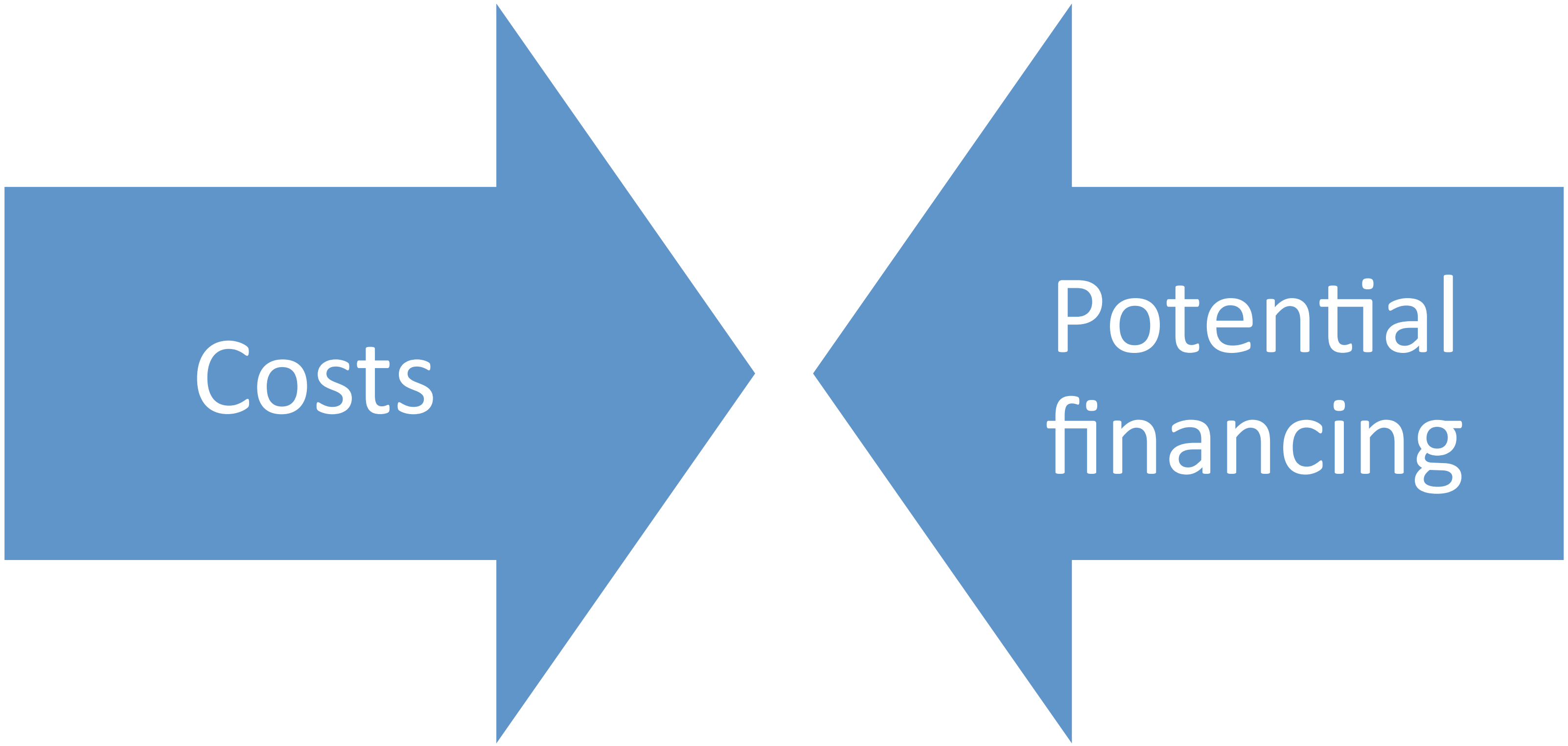
Some conclusions

- Investment planning is good instrument to check if proper environmental policies are in place
- Investment project design may influence implementation process considerably
- Negotiations require project level information
- Clear priority setting criteria are necessary to provide background for your plans
- Financing assumptions must be realistic and established at adequate level
- Institutions role shall not be underestimated
- Ministries tend to overestimate budgets knowing, that the Ministry of Finance will cut it down. This is nothing to do with real cost assessment. Better to avoid this “traditional” behaviour if possible on both sides

Good Budget Formulation & management Guide

- For grant projects, co-financed by the European Union in Serbia
- “ The project budget is always an estimate. How many pages will the project final report have? How much will heating prices increase over the project lifetime? These types of questions are impossible to answer at the start of the project. Good planning can only mean that the estimate is more accurate”

Matching costs and financing



Discussion

ASSESSING EXPENDITURE DEMANDS FOR SECTOR. PROGRAMMING

Session 4

FINANCING SOURCES FOR SECTOR PROGRAMMES

Sector resource programming mechanisms

- Even if adequate funds to meet the total costs of a SDP are available "in principle", this does not guarantee its smooth implementation
- Therefore, a key concept is **programming,** that is: linking projects and activities clearly to assured sources of funds, and to detailed work programmes based on agreed schedules for implementation
- In practice, planned activities are always likely to exceed available budgets; hence, the allocation of funds requires a further prioritisation of planned activities
- The whole process is made much more complex by the need to combine funding from many different sources.

Challenges

- The role of public versus private investment
- Fragmentation of the ‘sector’ budget
- Earmarking of the revenue streams
- Importance of Non-State Actors (Risk of too great a focus on government and the national level)
- Choosing the ‘right’ financial support modalities

Few good practice principles (1)

- **Start from a comprehensive view of resource flows to the sector**
  - An important task will be to get a comprehensive view of sector expenditures, taking into account national and donor expenditures that may be off-budget, and the contributions made by clients, NGOs and the private sector
- **Build up the sector expenditure framework systematically**
  - Improved costing of existing public expenditures will be a starting point (public expenditure reviews [PERs] may play a useful role) together with costing of proposed targets, such as those implied by the MDGs – the affordability of desirable targets will have implications for the quality/cost structure to be adopted. The development and use of expenditure analysis and planning tools is an iterative process

Few good practice principles (2)

- **Ensure that the sector expenditure framework is comprehensive**
  - A comprehensive sector development programme will embrace all public sector funding (recurrent and capital financing by both government and donors)
  - It will set public expenditures in the context of other resources going to the sector, e.g. through private sector activities and community contributions, but must demonstrate that agreed government responsibilities can be funded and implemented
  - These will be financed from a variety of sources: government itself will usually be the main financier, and will dominate the funding of recurrent expenditures
  - Government resources are supplemented by aid provided in a variety of ways – through general budget support or sector budget support; through pooled funds earmarked to the sector; and through individual projects. Technical assistance and other in-kind resources are also relevant

Few good practice principles (3)

- **Donors shall support and use of government expenditure management systems**
  - Donors should support the close involvement of the Ministry of Finance and the articulation of sector development programmes into a national MTEF system, ensuring a consistent medium-term approach to planning and budgeting across all sectors
  - Not least, they should themselves recognise the importance of making their own aid commitments more predictable and reliable, with specific allocations fully programmed before the start of the partner country's fiscal year. Ideally, all government- to-government aid funds should be fully incorporated in the partner government's budget
  - Even if it is not possible for some donors' funds to be disbursed through standard government procedures, they should be: i) "on-plan" – i.e. their availability should be notified in advance so that they can be fully taken into account when the government decides the overall pattern of resource allocation for the sector, and donors should not seek to apply them to activities that are not prioritised by the government; and ii) recorded in budget and expenditure documents both ex ante and ex post. Donors should also support the integrity of the sector MTEF by providing full information on their disbursements, using the same broad categories as in the budget classification

Few good practice principles (4)

- **Review the impact of all aid instruments on resource programming and on PFM in general**
  - The main obligations on donors supporting the sector are to: i) ensure that their support is focused on the priorities identified by the sector development programme; and ii) deliver their aid efficiently and in ways that promote government ownership and capacity
  - Budget support, where funds are entirely allocated using the government's own budgeting and disbursement procedures, is the modality that is most fully integrated into government systems.

Earmarking

- *Earmarking* of funds reduces budgetary discretion and may make it difficult for government to achieve the desired balance in actual funding of the sector
- The underlying principle of a SWAp is to achieve consensus on an overall level and pattern of funding for the sector, as an alternative to ring-fencing the activities
- Project/programme documentation should explain why earmarking is necessary or appropriate and how the project/programme is designed to support and integrate with the SDP

Budget programmes

- Do programme approach works in environment sector?

NEAS. Economic challenge of environmental approximation

- Total cost of meeting EU environmental requirements will be EURO 10.6 billion (between 2011 and 2030)
- Important part is operational costs, which cannot be covered by international sources and will have to be financed from public budgets, private sources or charges
- Need of additional financing from Serbian public budgets is estimated to peak at in 2018 at MEUR 360 in 2018

Strategy for financing of approximation costs

- To define the funding mechanisms required to meet the multi-annual stream of costs the following steps have been taken:
  - Calculation of the cost recovery component, i.e. the amount of the costs that can be recovered from the end users. This requires prior calculation of the affordability constraints
  - Estimate of reasonable transition periods for full compliance of the Acquis;
  - Definition of the financing sources
  - Calculation of the funding gap
  - Formulation of a plan to finance the gap

Affordability

- The requirement for charges to be affordable on average
- In the case of domestic consumers a limit of 4% of average household income is taken as the upper limit of expenditure on total combined services (water and wastewater, including taxes and fees)
- In waste household expenditure is assumed at the 1.5% threshold

Supply of environmental financing

- Total burden could reach about 3% of GDP going to environment (from current 0.4%)
- In NPV terms cost recovery will amount to € 5.7 billion. Total costs are estimated at € 10.6 billion. The cost recovery component amounts to 54.4% of the approximation effort
- It is estimated that the annual total costs (i.e. administration, capital expenditure, and operation and maintenance) will exceed the funding that can be raised from user tariffs until 2024
- Until full cost recovery is achieved, cost recovery should at least cover OPEX costs (only for OPEX until 2017)

FINANCIAL GAP COVER

€ million	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025	2030
TOTAL COST	**98**	**385**	**540**	**713**	**851**	**884**	**944**	**1.037**	**1.135**	**1.286**	**958**	**876**
COST RECOVERY (INCREMENTAL)	0	16	43	83	150	228	318	421	511	612	958	876
EFFECTIVE EU GRANTS RECEIVED	12	20	28	33	41	50	50	50	117	185	252	630
NET FINANCING (NO GOVT. RECOURSE)	19	75	98	127	137	123	109	105	102	114	-48	-73
OTHER DONORS	7	27	36	47	53	50	49	52	54	62	18	3
COMMERCIAL & PRIVATE SECTOR	11	44	57	75	85	81	79	83	88	100	29	4
REQUIRED FROM PUBLIC SECTOR	**-50**	**-204**	**-278**	**-348**	**-385**	**-352**	**-338**	**-326**	**-264**	**-213**	**250**	**564**

PUBLIC SECTOR SUPPORT

€ million	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2025	2030
REQUIRED FROM PUBLIC	**-50**	**-204**	**-278**	**-348**	**-385**	**-352**	**-338**	**-326**	**-264**	**-213**	**250**	**564**
DOMESTIC FUNDING SOURCES												
MEMSP	10	10	11	12	12	13	13	14	15	15	20	25
SEPA	0	0	0	0	0	0	0	0	0	0	0	0
SEPF *	63	80	97	114	120	126	132	139	146	153	195	249
LSG	45	47	50	52	55	57	60	63	66	70	89	114
NIP (OR EQUIVALENT)	4	4	4	4	5	5	5	5	6	6	8	10
WATER DIRECTORATE**	52	55	57	60	63	66	70	73	77	81	103	131
PUBLIC SECTOR RESOURCES	174	197	219	242	255	267	281	295	309	325	415	529
PUBLIC SECTOR FINANCING NEEDS	**0**	**0**	**0**	**-48**	**-179**	**-264**	**-322**	**-354**	**-308**	**-196**	**0**	**0**
EXCESS FUNDS CARRIED FORWARD	**124**	**117**	**57**	**0**	**0**	**0**	**0**	**0**	**0**	**0**	**2.199**	**6.201**

Closing funding gap

- The funding gap after cost recovery must be covered by a mix of instruments, including:
  - EU grants. IPA funds during the candidate phase and structural funds after membership
  - Financing Institutions (KfW, European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB) and others)
  - Direct support from project donors including technical assistance
  - Industry/Commercial direct investments and private investors
  - Public Sector including Central Budget;
  - Local Self-Government Budgets
  - Economic instruments, e.g. Serbian Environmental Protection Fund (SEPF), Budgetary Fund of the Republic of Serbia for Water and Budgetary Fund of the Autonomous Province of Vojvodina for Water

Financing from Serbian public sector institutions

- Central budget
- Local Self-Government budgets
- Other public sector institutions (SEPA, National Investment Plan (NIP))
- SEPF
- Budgetary Fund of the Republic of Serbia for Water and Budgetary Fund of the Autonomous Province of Vojvodina for Water

Need for external support

- The balance of funding that will need to be provided annually by the public sector is high, between €200 and €400 Million per annum until 2024
- Serbia will require external support for capital expenditure until 2024, when affordability will be able to generate sufficient funds to offset all costs and to commence repayment of the non-grant support required until that date
- It is estimated that Serbia would need to obtain credit line of finance for approximately €360 million

Importance of environmental financing planning

- Financial resources are limited
  - Resources have to be targeted to priority areas
- Project financing takes time
  - Institutions have to know which projects and when to prepare for financing
  - Sources of financing have to be made available (for example, loan preparation takes time)
  - Implementation of programmes shall be assessed in time terms
  - Funds have different rules for project financing and coordination takes time and effort
- Financing process involves substantial institutional resources which have to correspond planned financing levels

Essential elements of Environmental Financing Plan

- Sources of financing and expected allocations by year
- Distribution of financial resources among sectors
- Matching investment needs and available or potential financial resources
- Policy to close the gap if any
- Clearly defined terms of financing, co-financing requirements, maximum/minimum level of support
- Affordability criteria to "accept" investments
- Eligible project types
- Eligible beneficiaries
- Well-documented principles, rules and operating procedures for project cycle management

Sources of financing and expected allocations by year

	2005	2010	2012	2013	2014	….	2030
State budget							
Environmental fund							
Municipal budget							
Beneficiary's own resources							
EU funds							
Other donors funds (grants)							
Loans							
……………………..							
TOTAL							

Sources of financing and expected allocations by year (2)

- Description of sources and involved assumptions shall be made
  - E.g. as regards expected amounts from international sources of financing
- Some sources might be sector specific
  - E.g. only for waste or only for water
- Some sources might be reform sensitive
  - E.g. Environmental funds might require revision of environmental charges if resources are not sufficient
- Loans
  - Who is recipient? State, municipalities, regional waste management centers, WWTP?

Distribution of financial resources among sectors

Sector	% of funds
Drinking water	20
Waste water	30
Waste management	30
Air protection	15
Clean up of polluted areas	5
???????	

Distribution of financial resources among sectors (2)

- Requires all sectors (environment) wide approach
- Additional complications, when responsibilities are divided among several institutions
- Lithuania's case:
  - 70% for water and waste water
  - 30% waste management

Matching investment needs and financial resources

- Global matching
  - Approximation strategy (GDP or other level)
- Sector matching
  - Sectoral programmes
- Directive level matching
  - DSIPs
- Project level matching
- Aggregated matching
  - Investment and financing plan

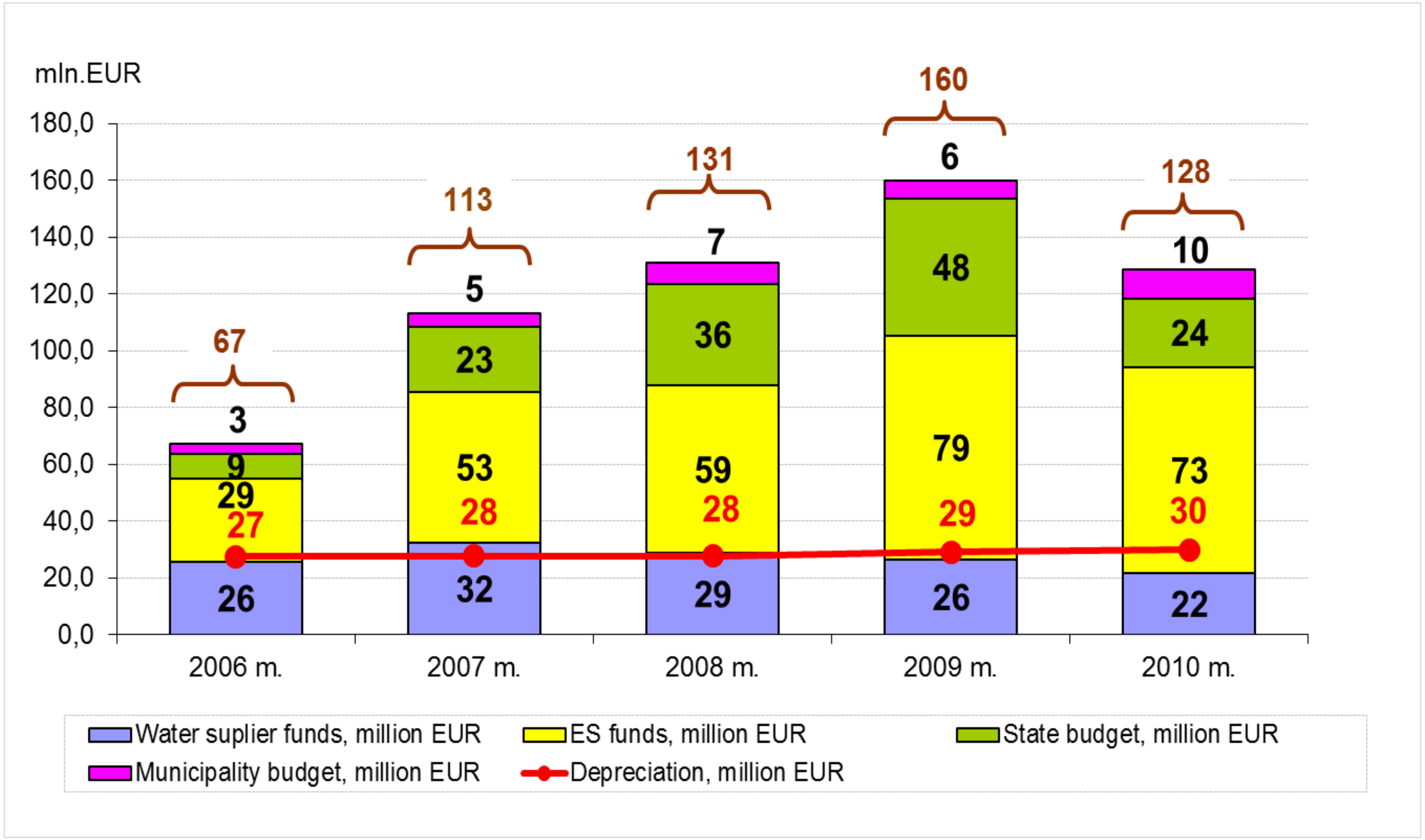
Policy to close financing gap

- Extended timing for implementation
- Better prioritisation
- Additional efforts to raise resources

Terms of financing

- Co-financing requirements
  - How much beneficiary will need to add to the financing package
- Maximum level of support
  - Grant rate based on revenues generated by project
- Minimum size of project
  - 5 MEUR ISPA
  - 10 MEUR Cohesion fund

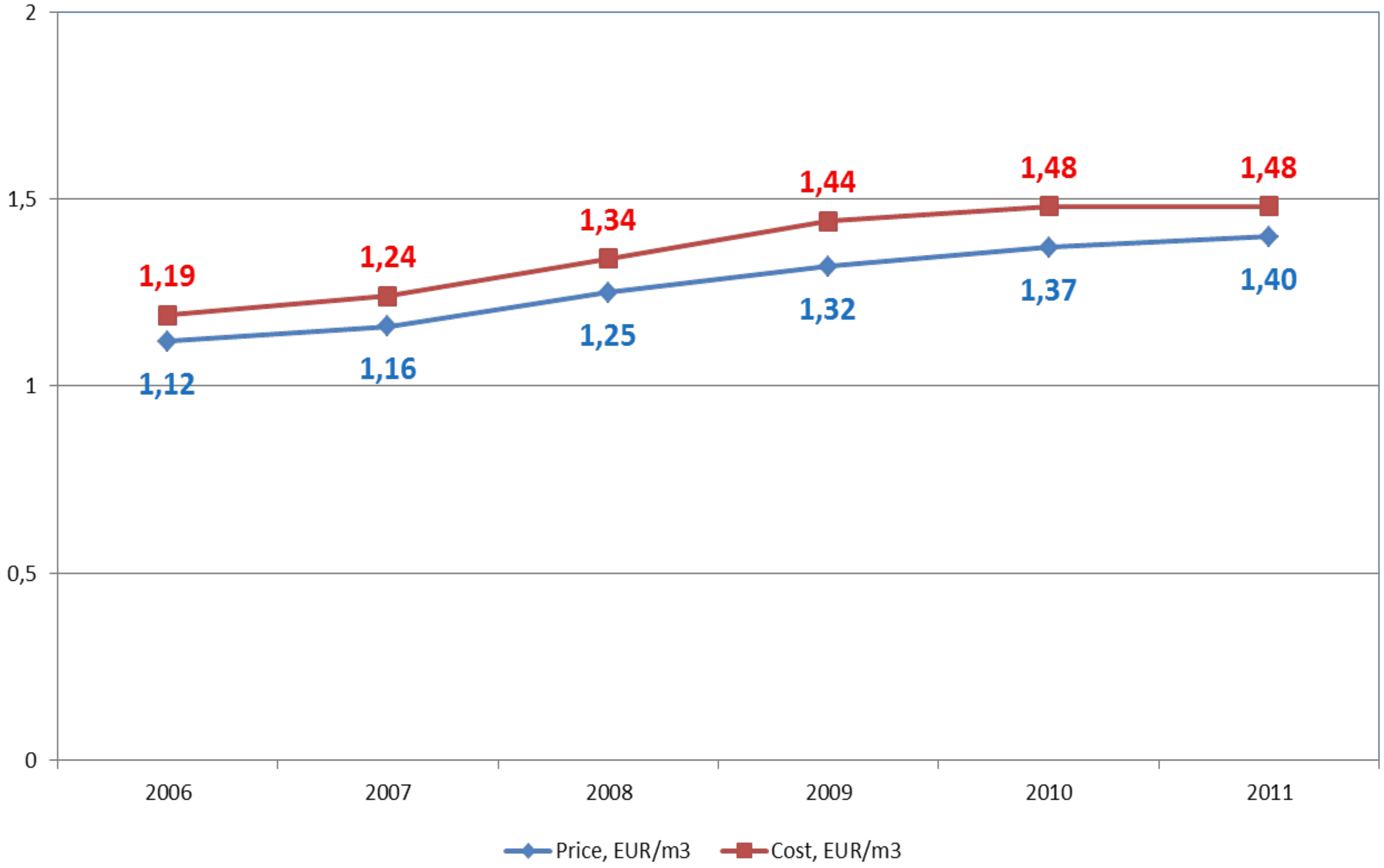
Investment structure in water sector



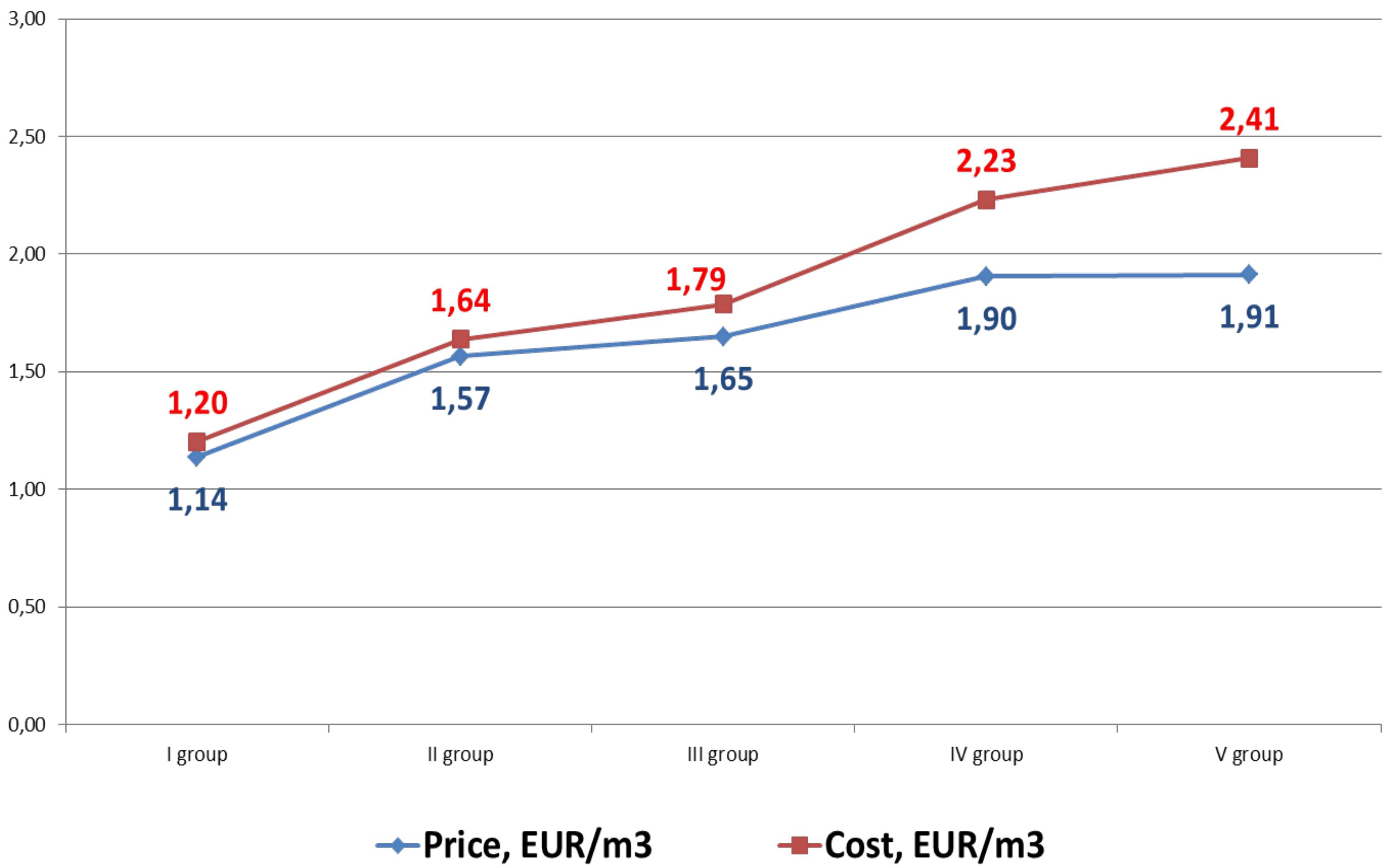
Affordability criteria

- Part of average household income allocated for water and waste related expenditure
- Lithuania:
  - Water – 4%
  - Waste – 1%

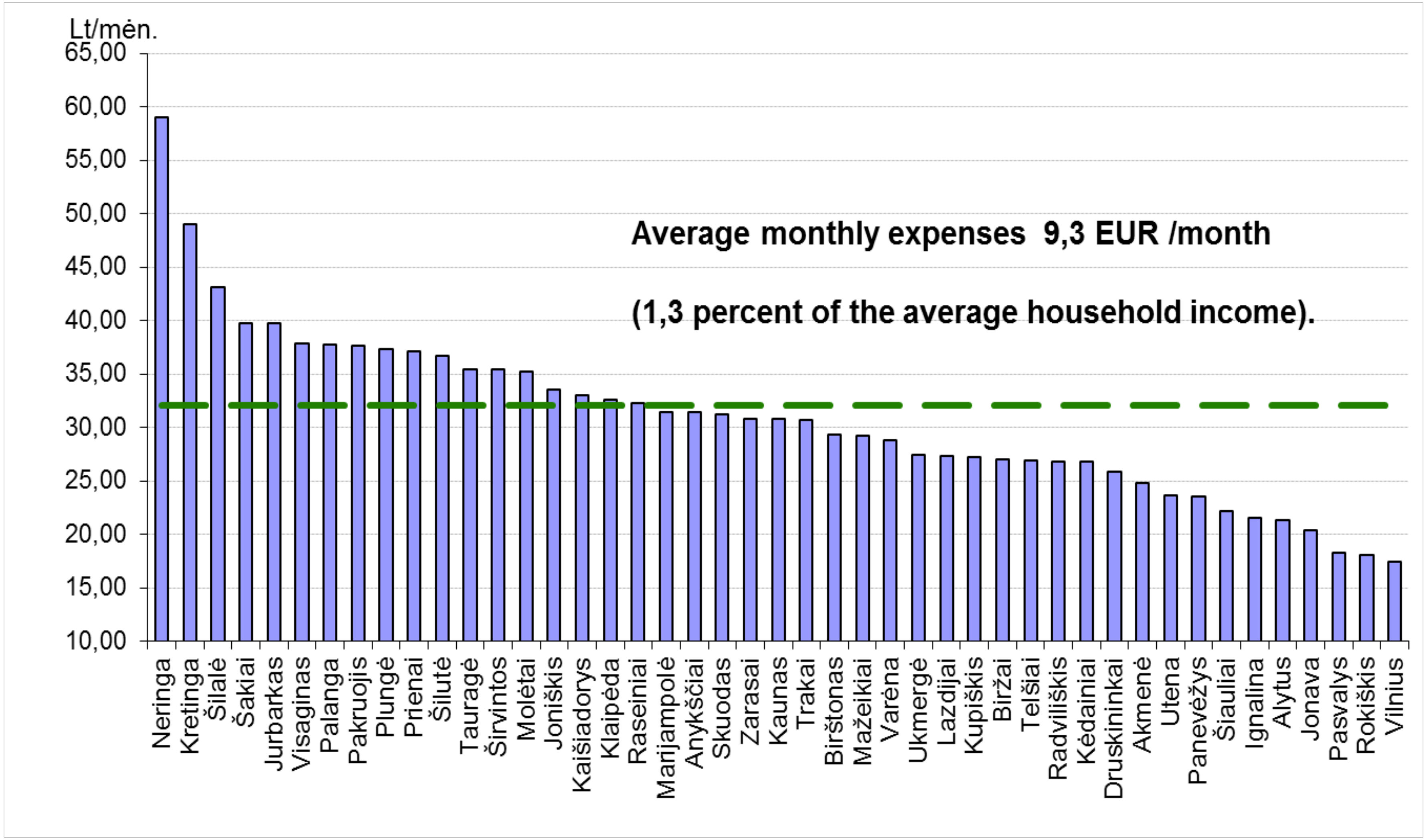
Average price and costs



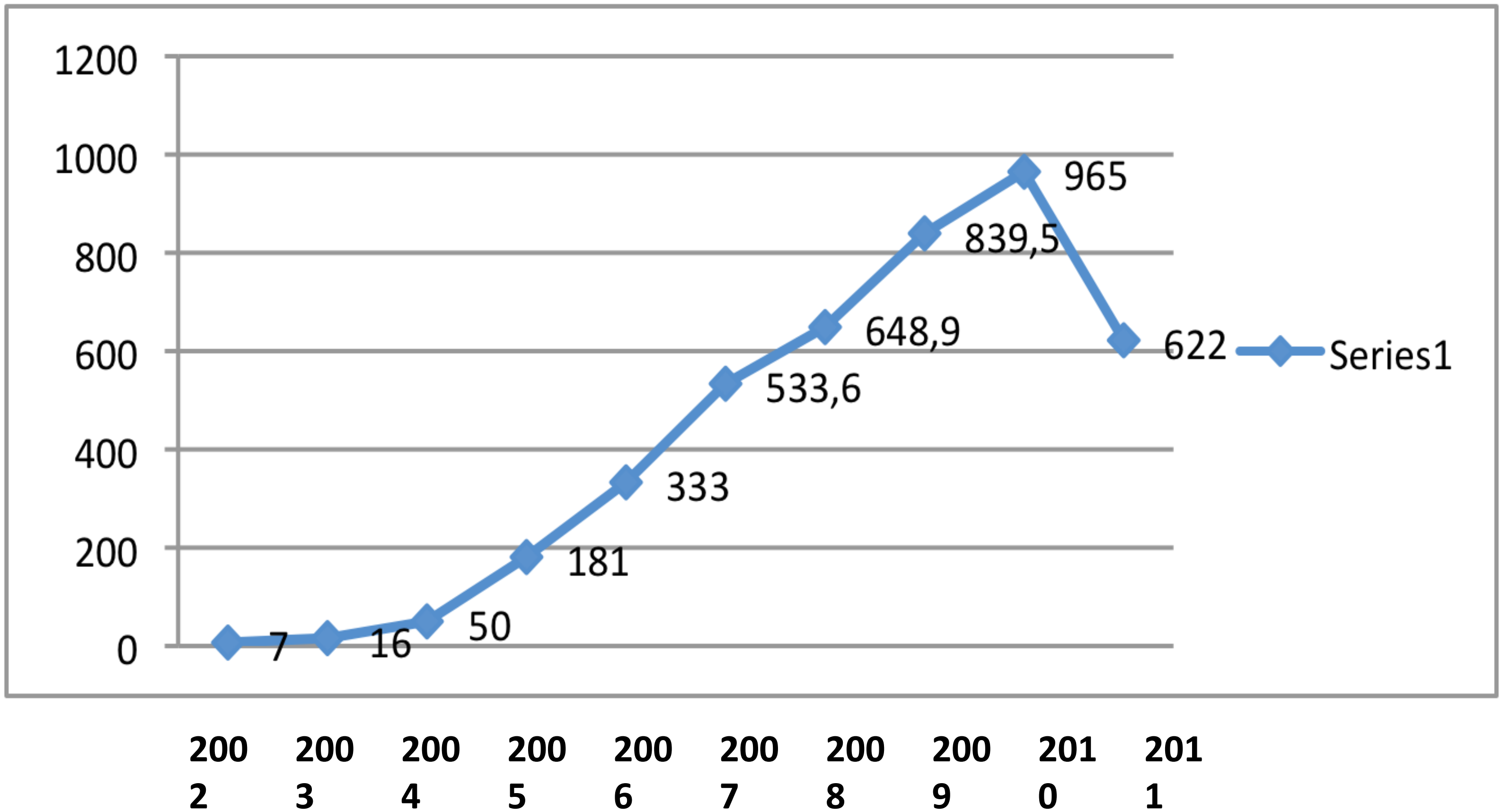
Average price and costs in groups



Monthly expenses for water and waste water



Disbursement of funds MLTL



Work in groups

LINKING SECTOR ACTIVITIES WITH FINANCING SOURCES

Session 5

COOPERATING WITH DONORS TO SUPPORT SECTORAL PROGRAMMES

NEAS. Leading and overarching strategic policies

- **Serbian legislation should mirror EU acquis**
  - no less, no more. This will reduce the cost of compliance.
- **Use of donor funds should be maximised**
  - This involves establishment of appropriate absorption capacity (adequate institutions), pipeline of projects, maintenance of balanced economic strategy
  - That will in turn minimise the needed intervention from Serbian public budgets. This would minimise the costs to be borne by Serbia
- **Implementation should focus on EU requirements**
  - work on approximation and on implementation of the Acquis should have an absolute priority over other national agendas

Guiding principles for donors (1)

- **1. Support government ownership and leadership.**
  - Donors must leave the initiative with the partner country government, while offering flexible support, information and guidance
  - Aid co-ordination at the national level is a government responsibility, while the government - donor partnership should be based on mutual accountability
  - Donors should be knowledgeable and sensitive about the country context and its institutions
  - They should seek areas of broad agreement and avoid micro-management.

Guiding principles for donors (2)

- **2. Work with government to strengthen institutional capacity and accountability**
  - Setting up parallel systems tends to undermine the regular systems of government and confuses accountabilities
  - Donors should therefore work as much as possible through partner systems and procedures while collaborating with partner country governments to address identified weaknesses
  - Both donors and partner governments should think in terms of national capacity, not just government capacity

Guiding principles for donors (3)

- **3. Set the sector programme in context**
  – Donors need to be aware of the SWAp's implications for overall coherence across government and its effect on the role of the central co-ordinating ministries, and on the relationship between central and local governments
  – Address cross-cutting issues, including gender equality, the environment, HIV/AIDS, and public service reform

Guiding principles for donors (4)

- **4. Take a long-term, strategic view**
  - Recognise the dynamic nature of SWAps and accept that it will take time to realise all the potential benefits of a sector partnership
  - Sector development programmes take a long time to mature and usually imply long-term institutional change and organisational development
  - They are typically implemented over at least a ten-year time frame, implemented in three- or five-year tranches
  - Donors must have similar time horizons, and must be prepared to commit long-term predictable resources
  - Address all stages of the planning and budgeting cycle for the programme, and build in a strong “results” orientation

Guiding principles for donors (5)

- **5.Be pragmatic and flexible**
  - Design processes which economise on management, planning and policy skills within government, while progressively developing capacity
  - Assess the costs as well as the benefits of proposed innovations
  - Recognise that there are competing interests on both government and donor sides which need to be sensitively managed; undertake a proper institutional and incentive analysis
  - Recognise and manage risks
  - Look for some "quick wins" that can help to build support for the programme (amongst both government and donor constituencies) in its early stages
  - Be realistic and learn from experience (including comparative international experience).

Any problems?

- We would wish:
  - Donor policy planning better responding national priorities
  - Donor policy planning more flexible to reflect rapidly changing situation
  - More transparency regarding available resources
  - Entrance point always through the sector ministry
  - Information about donor activities to be more systematic

How do we cooperate with donors

- Establishing coordination mechanisms
  - Formal (working groups and subgroups, SC, meetings)
  - Not formal (field trips, informal gathering, personal contacts)
- Establishing data base of projects and programmes
- Developing clear policies, programmes and projects, making them available for donors community
- Establishing institutional capacity to plan and implement project
- Keeping promises

What SWAp may change

- Coordination through central institution might be difficult when sector is defined so broadly and competencies are shared among several line ministries
- National institutions do not want to give right to central sector institution to coordinate the process
- Donors have established effective partnerships with certain agencies and actors and do not want to give these up in favour of a sector wide approach

Conclusions

- Coordination process is rather well establish and
gaining speed
- More efforts needed to get water sub-group running
- SWAp extends role of central sector institution.
Other institutions shall be informed and accept this role

Discussion

DONORS COORDINATION

Good practices in aid coordination

- A good framework for aid co-ordination in sector-wide approaches spans partner government - donor relations, intra - donor relations, and individual donor systems including:
  - An agreement on the information, fora, rules and timetables to manage dialogue between partner and donors
  - Arrangements between different donors to enhance co-ordination and to simplify procedures where it is not possible to use partner government systems.
  - Internal donor rules, incentives and culture that promote the ability to form effective partnerships with partner governments and other donors

Principal forums may include

- **A high-level sector programme liaison committee** entrusted with global oversight, general policy dialogue, as well as dialogue about overall donor support to the sector programme
- **An ad-hoc high-level government-donor forum** for possible conflict resolution, consisting of senior civil servants and a smaller group of heads of agencies with a mandate from the rest of the donors
- A smaller **government-donor coordination body** where operational coordination and more detailed policy dialogue take place
- **Joint technical working groups** to facilitate deeper dialogue and/or analysis in particular areas
- **Periodic (probably annual) joint reviews**; which examine the achievements of the last working period, assess the evolution of key sector indicators, and make recommendations to all parties to the sector programme
- A **wider consultative forum** (again probably annual, and possibly held immediately before or after the joint annual review) that allows participation by a wider range of domestic stakeholders

Few rules

- The rules governing donor coordination, including agreements about the management of the sector approach (e.g. any Memoranda of Understanding, joint financing agreements, codes of conduct, mandate and terms of reference for coordinating committees, etc.)
- An agreed calendar providing rhythm and deadlines for the work of the various management bodies and review forums. The calendar should fit with the government's fiscal calendar, and include timing for donors' funding commitments; meetings, reports, and reviews; a multi-year timetable for roll-over of the main sector programme document; and a work programme for related thematic research and reviews

Session 6

MONITORING AND EVALUATION CONCEPTS AND MECHANISMS

A sector-performance monitoring and accountability system

- An agreed approach to performance monitoring is an essential part of a SWAp
- It provides the means for the partner government and donors to judge whether sector goals are being achieved and whether sector strategies are effective
- It is also the basis for shared accountability.

Sector diagnosis

- Looking to sector in all its complexity
- Areas of assessment:
  - sector policies in a macro-context
  - public financial management
  - institutions and capacities
  - accountability and monitoring
  - harmonisation and alignment
  - **actual sector performance**
  - the wider political economy;
  - governance and accountability at sector level
  - decentralisation and deconcentration

Performance assessment framework (PAF)

- PAF is a set of regular performance measurements which enable managers and stakeholders to reliably assess progress in achieving a set of outcomes reflecting all key dimensions of the system being monitored
- The selection of indicators has to be closely related to the capacity of the system to produce the necessary data
- Increasing capacity may lead to revision of indicators
- The selection of indicators (and the capacity of the statistical and performance measurement system) should therefore be seen as an iterative process

Definitions of the four levels of indicators in a classical result chain

IMPACT	Measures the consequences of the outcomes in terms of wider objectives (for example, literacy rates, health improvement). The definition covers the wider effects of the outcomes but there might also be higher level impacts, related to broader objectives – growth and income poverty, for example.
OUTCOME	Measures the results at the level of beneficiaries (for example, gross enrolment rates in primary schools, vaccination). The definition covers the outcomes (or results) from the use and satisfaction of the goods and services produced by the public sector - it is where supply comes face-to-face with demand
OUTPUT	Measures the immediate and concrete consequences of the resources used and measures taken (for example, schools built, teachers employed, nurses trained) The definition of output covers those goods and services "supplied", “produced” or "provided" by the public sector with the inputs.
INPUT	Measures the financial resources provided and the administrative and regulatory measures taken (for example, resources allocated, resources used, measures taken, laws passed). The definition of inputs can be treated as very broad, covering in some cases what is often called "process indicators"

Issues to be addressed 1 (technical perspective)

- Do the performance indicators selected respect the SMART principles, in being Specific, Measurable, Affordable, Relevant and Time-bound?
- Is the indicator reliable enough to follow trends over time?
- Is there a clear and unambiguous definition of the indicators so as to avoid errors and misunderstandings in interpretation at a later date?
- Is the data source for the indicators clearly identified? They should as much as possible be drawn from the data produced by the National Statistical System, avoiding ad hoc or project-related indicators
- Is there a clearly developed framework for sourcing information and for verifying its correctness?
- Is the methodology used to calculate the indicator clearly described?

Issues to be addressed 2 (technical perspective)

- Are the timing and lead time in the availability of the data to construct the indicators known?
- Are indicators disaggregated by gender, by socio-economic category or other criteria so that it is possible to assess the impact of the programme on both men and women, on the poor and the less poor, on specific vulnerable groups?
- Does the group of indicators chosen cover the necessary requirements both for short-term management information (data on inputs and outputs) and for performance measurement (outcomes and impacts)?
- Is the structure of indicators consistent with the way in which spending has been structured within the sector programme's budget? In particular, is there a consistent breakdown by sub-sector, programme and where relevant sub-programme?
- Is the structure of indicators also consistent with the wider requirements of monitoring the national development strategy or PRSP?

Issues to be addressed 3 (political nature)

- Reflecting:
  - the need to demonstrate progress in achieving international, global commitments such as the MDGs and local priority setting and ownership
  - a set of indicators that is comprehensive enough to encompass key areas of sector performance and the reform agenda while being limited in numbers
  - having indicators that are meaningful to local communities and citizens yet useful for sector management and resource allocation
  - choosing indicators that enable tracking achievement of medium- to long-term sector goals (more output/ outcome) and can function as triggers for annual donor disbursements (more process/output)

Issues to be addressed 4 (political nature)

- Reflecting the issue of ownership of the framework:
  - Has the performance assessment framework for the sector programme been established through the leadership of the government?
  - Has the team responsible for this included senior management within the ministry as well as statisticians and data processing staff? In short, is there a sense that the issue has been taken seriously at senior levels and that adequate internal consultation has been conducted?
  - Have the other major stakeholders in the sector programme been consulted? In particular have consultations involved not only donors and the core sector stakeholders but also the Ministry of Finance and, for decentralised components, the Ministry of Local Government (or equivalent)?

PAF review process 1

- Management review: Analysis of performance indicators is presented to responsible managers in sector ministry for review and comment. Managers are asked to explain significant deviations from targets
- Management analysis: Where deviations are major it may be appropriate to analyse the source of deviation more deeply. (Were resources available as planned? Are there possible exogenous reasons such as a natural disaster? Is the deviation derived from unexpected results in certain parts of the country?)
- Investigation: It may be appropriate to commission some rapid field assessment to understand the deviation better
- Peer Review: Once managers have been allowed an opportunity to analyse, investigate and understand the performance data there should be an opportunity for them to present this information and its implications for future action to their peers

PAF review process 2

- Strategy review: Senior managers of the sector need to absorb this information and develop initial proposals for strategy change, increased efficiency, resource reallocation, adjustment of future targets
- Inter-ministerial coordination: Most governments are organised in a manner where most service Ministries cannot implement their strategies without substantial support from other Ministries such as Finance (financial resource), Public Service (human resources and government-wide structural reforms), Local Government (coordinator of the local authorities who actually deliver the services), Legal Affairs (coordinators of any legislative programme). So once the sector Ministry has developed a robust analysis of its own performance and a set of responsive strategies to enhance future performance, it has to go out and sell its proposals to the rest of government both in Cabinet but also at a more technical level with its sister Ministries
- Public accountability: The final step in the internal review process is the presentation of performance data to the appropriate public forum specified by the law or constitution. This could be a specific Senate committee or an annual parliamentary review of public expenditure.

Good practice

- **Support links between planning and monitoring, avoid overload, and strengthen national data systems**
  - Sector plans need to provide a clear structure of goals and objectives that can be monitored
  - Focus on a few high-level indicators
- **Emphasise dissemination and use of findings**
- **Monitor so that domestic accountability is reinforced**
  - Sector programmes should be monitored in a way that reinforces the accountability of a developing country government to its citizens

Work in groups

ESTABLISHING OF SECTORAL PERFORMANCE ASSESSMENT FRAMEWORK

NEAS

- Chapter 6. FRAMEWORK FOR MONITORING APPROXIMATION PROGRESS AND FOR NEGOTIATION
- Considerations regarding institutional system for monitoring (Group for chapter 27)
- No indicators

Session 7. Work in groups: Way forward

DEVELOPMENT OF ACTION PLAN FOR SWAP ENVIRONMENT