

**FINANCIAL AND PARTNERSHIP APPROACHES IN
ADDRESSING LAND-BASED SOURCES (LBS) OF MARINE
POLLUTION¹**

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¹ The content of this paper is the responsibility of the author(s) and does not necessarily represent the views of the PAME Working Group as a whole, or its member countries.

I define “Financial and Partnership Approaches” as different methods to assist the industry in how to finance measures and how to get different stakeholders to cooperate in implementation of such measures. The stakeholders will in many cases involve the government because of policy priorities, but also banks, insurance companies and communities may show interest in different projects. The methods of bringing the stakeholders together and finding a suitable division of roles are important, however, the aim is not the partnership as such but to achieve environmentally better or more cost-effective results than each of the stakeholders would have managed on their own.

This paper tries to outline some of my experiences, as a basis for discussion and do not reflect the view of any specific country or organization.

Traditional Pollution Abatement Strategies

The use of governmental regulation, issuing permits and economic incentives like tax, subsidies, fees and fines etc. are traditional and in many respects effective measures to reduce pollution. In most of the Nordic Countries, flexible and step wise regulations have shown good results both in respect of getting a cleaner environment but also in ingenuity and development of industry. However, good results is achieved only if the authorities are enforcing frequent controls and audits and are willing to report offenses to the police and prosecute violation against the rules.

The conditions for the success of the traditional measures are viable industries (meaning that the industry is economically able to implement measures), sufficient knowledge about measures and willingness to implement the regulations. At the same time pollution abatement must have a high priority in the society and in the government.

However, in some cases the traditional abatement strategies are not sufficient. Such cases may *inter alia* be:

- Where the regulation is directed to a large and economically important industry
- When the cost is high
- When the technical solution to a problem is lacking and need to be developed
- When there are many different polluters and we need many business sectors to be involved in the abatement process.
- When we consider cross border pollution and measures

In such cases we need cooperation between two or more stakeholders to solve the pollution problem.

Examples of cases where regulations or economic measures are not sufficient:

- The call for zero-emission from offshore oil and gas activities in the Norwegian sector of the Barents Sea. (*Important industry, lack of technology and high cost*)
- Recycling of plastic waste. (*Many and different producers of plastic waste*)
- The flexible mechanisms in the Kyoto protocol which opens the opportunity for reduction of greenhouse gases in one country and gives part of this reduction as a credit to the partnership industry/country. (*Cross border cooperation*)

Important steps in a Partnership process

Selection of projects

Keeping in mind that we need to establish a partnership to obtain the objective, the selection of a project is clearly dependant on which stakeholders that should be involved in the pollution abatement measures. If the industry is to be involved it is more important to find a company which takes the responsibility to implement measures than to find the most relevant and largest emitter of hazardous substances or a “hot spot”. This is partly due to the requirements from international banks that the owner of the problem is responsible for the loan, and partly that it will increase the probability that the

most cost effective measure will be implemented. In general the chances of success will increase when the project is deeply rooted at the problem owner.

For a project which aims at cross border industrial cooperation the selection process should be left to the industry itself. I don't know any project which has been arranged by the governments and where industries are cooperating over the border. Most successful efforts of industry involvement have so far been initiated by industry itself. The reasons for this reluctance to cooperate to close with the government are not clear, but competition, fear of disclosure of information and fear of exposure to the public may be part of the explanation.

However, this should not exclude governments to take part in some way.

Establishing such instruments as framework agreements between governments and developing financial instruments can pave the way of transferring money, know-how and technology across borders between collaborating industries. At the same time such incentives may open up for keeping the necessary distance to industry and their projects.

Government-to-government cooperation is sometimes also important in partnership processes. Such projects are first of all important with the respect to exchange of experiences in work where the governments have a specific role to play e.g. when regulation or economic incentives is needed. Examples are: handling of hazardous waste, or issue permits, enforce inspections and prosecute industries that violate the regulations or which do not take part in partnership or voluntary agreements.

In some context when regulation or experience is lacking, it may be necessary to start with a government-to-government cooperation and to continue to keep up the pressure on industry to secure the implementation of partnership projects.

Financial arrangements

In most projects it will be a "must" that governments give active support to overcome cooperation and travel costs in the initial phase and arrange for "back up" solutions in the investment phase.

Several financial instruments can be established or are already available:

- Governmental guarantee liabilities
 - Non or low tax agreement when transferring money, technology and know how across borders
 - Host country's political and economic support/guarantee to the project
 - Home government guarantee to participating industry
- National or internationally pooled equity funds
- Internationally or bilateral donor funds or Trust Funds
- Insurance schemes (*lower insurance costs*)
- Loans with modest borrowing rate

The International Finance Institutions (IFIs) have established several economic arrangements with the cooperation of participating countries to finance environment projects in general and pollution abatement projects in special.

It should be clear, however, that international financing of projects are based on specific requirements, and applications for support will follow a specific project cycle. Such project cycles may last 1– 3 years before an approval can be given. In the contract the bank normally also will require that a bank representative shall follow the project closely.

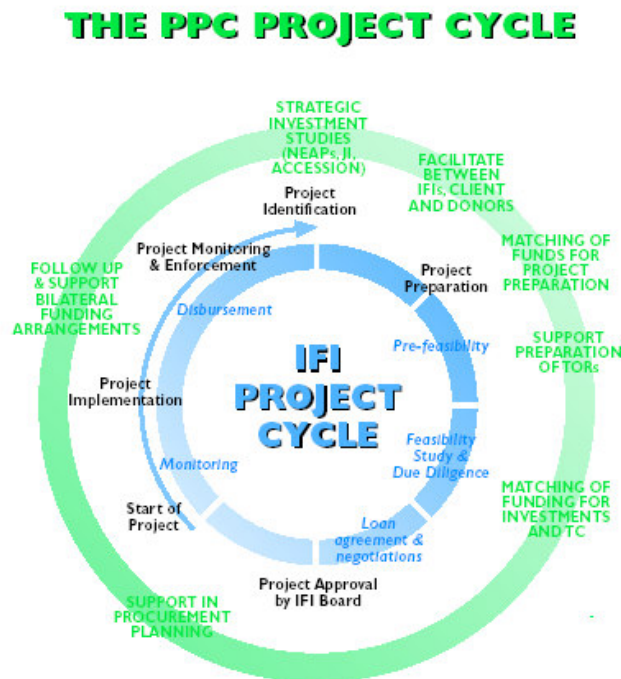


Fig. 1 is an example of one project cycle (for the Project Preparatory Committee under the Environment for Europe process)

The attached paper from PPC: “International Financial Institutions’ Project Cycle” will give you more insight in how the IFIs operate and the role played by stakeholders in the different stages of the project cycle.

An interesting way to stimulate cross border cooperation may be the way the Netherlands are trying to encourage Joint Implementation (JI) when reducing greenhouse gas emissions. They have called for tenders amongst industry for JI-projects and have allocated money to support the winners amongst the companies tendering.

It will also be interesting to see if the Partnership process and the Roundtable discussions assisting the Russian NPA Arctic can encourage industry and other stakeholders to establish viable projects.

International instruments

Regional and global international cooperation (both legal and non-legal instruments are important and necessary to protect the Arctic Marine Environment. The Basel, Rotterdam and Stockholm conventions and the Århus Protocol under the ECE cooperation are all addressing hazardous pollutants but it is up to the Parties of the conventions to obtain the results.

However, such instruments are no guarantee for implementation of measures alone. Public awareness in the participating states, high governmental priority and framework arrangements are necessary to obtain pollution reduction

Conclusions

The responsibility to reduce pollution of the Arctic Marine environment lies primarily on the industry. The industries of the Arctic Countries are the primary pollution sources within the Arctic due to their high level of industrialization and their closeness to the Arctic Marine Region. However, the contribution to the levels of heavy metals and POPs and radioactivity, are also influenced by the earlier and current activities of the armed forces and through long range transport by air, rivers and sea currents from other regions.

Much of the governmental policy has hitherto been based on legal and economic measures to force the industry to reduce their emissions. However, in the later years several countries have also encouraged and stimulated the industry and achieved good results. The use of the ‘stick and carrot’ principle has been applied in different ways to e.g. research support, subsidies, positive labeling, trade able permits, partnership support etc. Some of these incentives have weaknesses or need special conditions to succeed.

To achieve the long term goal of a clean Arctic marine environment, both governmental pressure and financial incentives are necessary. In addition it is crucial to establish regional and world wide co-operation to solve the problems in a cost effective way. Exchange of know-how among industrial experts as well as between governments, is of utmost importance to combat pollution. The challenge of Arctic Council is to trigger these types of cooperation in a way that both will give short-term results and long term sustainability.

Draft questions for discussion?

- In which way should the Arctic Council and the Arctic Countries concentrate their efforts to reduce pollution of the Arctic Marine Environment in the future?
 - What type of actions?
 - What type of cooperation?
- In what way could Arctic Council encourage partnership projects?



The Project Cycle

Introduction

The main business of the international financial institutions (IFIs) is to lend for specific projects that are carefully selected and prepared, thoroughly appraised, closely supervised, successfully implemented and systematically evaluated. Each IFI has its own particular internal project cycle, however the borrower will generally be exposed to the same key steps in the project cycle regardless of the IFI providing assistance.

The Project or Operation Cycle is the process through which the IFI implements its mandate, providing assistance to projects for which borrowers are committed. The cycle begins with country strategies and sector operations policies, and continues through evaluation. For each key event in the cycle, the IFI has defined a set of specific procedures to be followed and documents to be completed.

The key events in the cycle

The normal sequence of key events is as follows:

- Identification
- Preparation
- Appraisal
- Negotiations and Board Presentation
- Implementation and Monitoring
- Evaluation

Project identification

The first phase of the project cycle is concerned with identifying projects that appear suitable for IFI support, and to which the IFI and the borrower are committed. Identification is the initial exploratory work concerning an operation proposed for IFI assistance by a government agency, a local or foreign enterprise, an international or commercial financial institution, or by the IFI at its own initiative. Country strategies and sector operations policies translate the policies of the IFI into an operational context. These strategies determine the type of operations that the IFI considers eligible for assistance in each country of operation. This analysis provides the basis for a continuing dialogue between the IFI and a borrower or country on an appropriate development strategy, including policy and institutional changes for the economy as a whole and its major sectors.

During project identification there is a preliminary assessment of the project's technical, financial, economical, environmental and institutional feasibility.

Preparation

Once a project has been declared eligible for consideration under the IFI's policies and priorities, it enters the project "pipeline", and an extensive period - often six months to two years - of close collaboration between the IFI and the borrower begins. It is difficult to generalise about the preparation phase because of the variables that abound: the nature of the project; the experience and capability of the borrower; the technical knowledge available; and the nature of the relationships between the IFI, the government, borrower, beneficiaries, co-financiers, and other donors that may be involved in the sector or project.

The responsibility for preparation rests with the borrower. The IFIs normally play an active role in the preparation, ensuring that the preparation work will meet their requirements and standards. IFIs can also assist in project preparation and provide funding for feasibility studies from trust funds. Preparation must cover the full range of technical, institutional, regulatory, environmental, economic and financial conditions necessary to achieve the project's objectives.

Appraisal

Appraisal provides a comprehensive review of all aspects of the project and lays the foundation for implementing the project and evaluating it when completed. Appraisal covers four major aspects of the project - technical, institutional, economic and financial. In addition, all IFI projects undergo separate environmental review. The environmental due diligence ensures that each project is environmentally sound, just as due diligence is performed to ensure that projects are financially, economically and legally sound.

Appraisal is conducted by IFI staff, sometimes supplemented by consultants. Often additional studies are needed to address issues which have not been sufficiently dealt with in the preparation phase. Discussions between the IFI and borrower continue during appraisal, as the project concepts are refined.

After appraisal is completed the project concept is submitted to the management of the IFI for approval before submission to the Board. Subsequently, the borrower (responsible authority, enterprise, etc.) has to approve the project concept before the next stage in the cycle.

Negotiations and Board presentation

Negotiation is the stage at which the IFI and the borrower endeavour to agree on the details necessary to ensure the success of the project. These agreements are then converted into legal obligations, set out in loan documents. Negotiations are a process of give and take on both sides of the table. The loan agreements will contain specific requirements - covenants - which have to be complied with during implementation of the project.

After negotiations the final appraisal report, together with the President's recommendation and the loan documents, is presented to the IFI's Executive Directors (Board). If the Board approves the operation, the loan is then signed and this marks the end of one stage of the cycle and the beginning of another. Approval of an operation by the Board represents the commitment of the IFI to provide financing.

The borrower then signs the loan agreement and begins the implementation of the project. In the case of sovereign guarantee projects, the guarantee agreement has to be approved by the Parliament before loan effectiveness.

Implementation and monitoring

The next stage in the life of a project is its actual implementation over the period of the construction and subsequent operation. Implementation is the responsibility of the borrower with whatever assistance has been agreed upon with the IFI or donors. The IFI's role is to supervise the project as it is implemented.

The IFIs are required by their Articles of Agreement to make the arrangement to ensure that the proceeds of any loan are used only for the purposes for which the loan was granted. While this

“watchdog” function is important, the main purpose of supervision is to help ensure that projects achieve their objectives and, in particular, to work with the borrowers in identifying and dealing with problems that arise during implementation.

Monitoring is the continuous assessment of project implementation in relation to agreed schedules and the use of project outputs, including infrastructure and services, by project beneficiaries. Monitoring will include checking of compliance with measures specified in the loan agreement and the IFI will take the necessary action to ensure compliance.

An important element of project monitoring concerns procurement of goods and works financed under the loan. Procurement has to be carried out in accordance with IFI guidelines, incorporated into any loan agreement, that are designed to ensure that the requisite goods and works are procured in the most efficient and economical manner. In most cases, this objective can best be achieved through international competitive bidding (ICB).

Evaluation

Evaluation is the periodic assessment of the performance, efficiency, and impact of the project in relation to stated objectives. The major goal of evaluation is to provide reliable feedback about the impact of ongoing and completed projects and to include this in the design of new projects and operations.

Evaluation measures achievements in relation to programme objectives, institutional policies and the goals set for each project. It is designed to:

- Provide an objective basis for assessing the performance of policies, programmes, projects, and processes;
- Improve policies, programmes and projects by identifying and disseminating the lessons learned from experience.

To assess the effectiveness of completed operations the IFI examines the project’s technical, financial, economic, social, and environmental aspects and provides ratings of their outcomes, sustainability and effect on institutional development. Normally the performance of the IFI, the borrower and implementing agencies is evaluated. The outcome of the operations is analysed in terms of overall outcome, sustainability and institutional development.

For some projects a separate environmental evaluation will be conducted. This will evaluate the environmental aspects of the project and will result in the preparation of environmental evaluation reports which will become part of the overall project completion reports. In some cases, the environmental evaluation may result in environmental monitoring being carried out after project completion.

IFI’s internal project procedures

The IFIs have an associated process focusing on their internal procedures and documentation related to each step in the project cycle. Table 1 gives an example of how an operation cycle might look and how PPC activities fit into this cycle.

Role of borrower, IFI and donors

In the different phases of the project cycle the borrower, IFI and bilateral or multilateral donors play different roles and have different responsibilities. Table 2 outlines the key roles and responsibilities in the different phases of the project cycle.

Table 2: Roles of borrower, IFI and donors at different stages of the project cycle

Party	Identification	Preparation	Appraisal	Negotiations and Board Approval	Implementation and Supervision	Evaluation
Borrower/Client (i.e. Central and Eastern European/ NIS partner or enterprise)	<ul style="list-style-type: none"> Proposes project Identifies sponsor Solicits approval 	<ul style="list-style-type: none"> Prepares feasibility study 	<ul style="list-style-type: none"> Provides further information as needed 	<ul style="list-style-type: none"> Negotiates and approves the terms of the loan and the covenants of the loan agreement. 	<ul style="list-style-type: none"> Prepares detailed design Undertakes procurement etc. Implements the project Supervises the implementation 	<ul style="list-style-type: none"> Provides experiences and lessons learnt Evaluates if project objectives are met
International Financial Institution (IFI)	<ul style="list-style-type: none"> Helps to identify projects in accordance with country and sector priorities Assesses preliminary technical, financial, environmental and institutional feasibility Preliminary confirmation of interest and commitment Undertakes sector studies and pre-feasibility studies 	<ul style="list-style-type: none"> Provides assistance to preparation of feasibility study 	<ul style="list-style-type: none"> Assesses the project's technical, institutional, economic, environmental and financial viability Prepares financing plan and implementation plan Undertakes economic, legal and environmental due diligence 	<ul style="list-style-type: none"> Negotiates Board approval 	<ul style="list-style-type: none"> Disburses loan Supervises procurement Provides technical assistance as needed Monitors implementation of project and compliance with covenants 	<ul style="list-style-type: none"> Evaluates if project objectives are met Audits the project Prepares feedback to update country strategy and sector operations policy
Bilateral and Multilateral Donors	<ul style="list-style-type: none"> Supports identification work Provides resources for project identification Preliminary confirmation of commitment 	<ul style="list-style-type: none"> Provides grants for feasibility studies Determines whether to provide co-financing or parallel financing 	<ul style="list-style-type: none"> Prepares additional studies Confirms commitments for co-financing Provides grants for technical assistance 	<ul style="list-style-type: none"> Negotiates co-financing arrangements 	<ul style="list-style-type: none"> Provides technical assistance as needed Twinning arrangements Monitors the implementation 	<ul style="list-style-type: none"> Evaluates if project objectives are met

Key experiences

Introduction

Some key experiences related to the project cycle are presented in the following paragraphs. The aim of this presentation is only to provide key messages, not to address all issues comprehensively.

Evaluation suggests that when development projects perform well it is usually for one or more of the following reasons:

- Beneficiaries of the loan/project participate sufficiently. Participation means involving beneficiaries in decision making and not only explaining the project to key stakeholders (individuals and groups who stand to gain or lose from the project).
- Borrowers are committed to project goals. Their ownership has been sought by making them responsible for preparation and implementation, ensuring that the impetus for the project is local and that the process provides explicit opportunities for consensus building.
- Risks are adequately assessed and managed.
- Capacity building has been a core objective that permeates the whole project pursued through separate technical assistance components, for example staff training.
- Project design is adjusted to changing conditions in a timely way.

Some key experiences related to each step in the project cycle are highlighted below.

Identification – the key activity to successful implementation

- ***Project ownership and responsibility rests with the borrower - IFIs and donors can only support and assist in project preparation and implementation.***

Client orientation means working to ensure that projects meet the needs of the borrowers and that the borrowers are strongly committed to the projects. This requires that the borrowers have a strong participation in project design and implementation. The institution proposing a project might be different from the institution, which will be the borrower and the implementor of the project. Identification of the borrower and the institution responsible for the project should be included in the identification phase. This will increase the transfer of knowledge through the whole project cycle, increase the capacity of the borrower to implement the project and enhance ownership feeling.

In the identification phase the project promoter should contact all relevant authorities to verify whether the proposed project complies with laws and regulations etc. If financing an environmental project in Central and Eastern Europe/NIS requires a sovereign guarantee from the government, the Ministry of Finance should be contacted as early as possible. If the Ministry of Finance indicates that a guarantee will not be given the client/sponsor has to consider whether sufficient security for the loan can be obtained elsewhere. The World Bank only work with sovereign guarantee lending. The issue of guarantee should be addressed along with other aspects of financial engineering early on in the project cycle.

Stakeholders should participate in the identification of the project. This underlines the central role of the borrower and the potential beneficiaries right from the start of the project cycle. Views and concerns of all significant stakeholders should be solicited to clarify project goals and to gather relevant experience and insights. This brings the demand side into the project identification process.

- ***The structure of project financing is one of the most critical areas - develop financing strategies considering various options on the financial market.***

Risk sharing among project partners (owner, supplier, IFIs, consumers) should be considered early in the process. The same applies to the issue of guarantees and new financing instruments which can be used. It is

normally required that the borrower provide equity. Joint ventures should be considered where possible. Furthermore, IFIs are lenders of last resort and thus other financing sources should be explored first. IFIs may also provide financing through existing local financial intermediaries (i.e. local banks).

- ***Role of consultants***

Consultants are in most cases needed to prepare the required documentation. To the extent possible local consultants should be used since they have better knowledge about local conditions. However, in some cases specific expertise is required which cannot be obtained domestically, in which case external (foreign) consultants will need to be hired.

- ***Public sector projects - appropriate policy and institutional framework is an important prerequisite.***

A fundamental prerequisite for most investment projects is that the policy and institutional framework needed is in place. Most projects include institutional strengthening and capacity building.

Preparation - a well prepared project is a prerequisite

- ***The borrower is responsible for project preparation.***

The borrower is responsible for preparing the project so it meets the requirements of the IFIs. By making the borrower responsible for preparation and implementation, commitment and ownership will be enhanced.

- ***Technical preparation of the project is not enough - the IFIs require extensive environmental, institutional, economic and financial analysis.***

There has been a tendency to emphasise the preparation work on design and engineering. What is lacking is preparation of sound, high quality institutional, economic and financial analysis. This is partly due to lack of expertise and knowledge. Emphasis needs to be put on such analysis in the preparation phase to comply with the IFIs' requirements.

Long-term project sustainability should be ensured by including relevant measures to address operation and maintenance. In case of revenue generating projects, the project should at least raise enough revenue to cover recurrent costs.

- ***Explore the least-cost alternative.***

The project concept should be based on a comparison of different alternatives including the situation without the project. Internal Rates of Return (IRR) and Net Present Values (NPV) should be calculated. The least-cost option should be pursued.

Modernisation and better utilisation of existing assets should be reviewed before considering construction of new assets. Rehabilitation may be more economically, financially and environmentally beneficial than developing new or "greenfield" projects. Although rehabilitation work is not politically exciting, it is often more efficient where existing systems are in a very poor state of repair - as is common in central and eastern Europe and the NIS - and where efficiency gains are not an issue of marginal improvement.

- ***Include implementation in preparation.***

Cost over-runs are often a problem as it sometimes takes longer than planned to implement the project. By carefully preparing an implementation plan, the risk of cost over-runs can be minimised. Contingencies should be included in the budget.

- ***In planning Technical Assistance (TA) consider first the availability of local skills. Foreign TA should only fill the existing gaps.***

Local consultants should be used to the extent possible since they possess considerable local knowledge and experience which are essential to take into account in the preparation phase. All IFIs promote the use of local consultants. Before foreign consultants are contracted to prepare a study a careful assessment of available local skills mix should be undertaken. Foreign consultants should be used to complement the local

skills mix and to address issues in which local expertise is lacking. In most central and eastern European countries and the NIS there is a need for assistance in the areas of management, economic and financial analysis and institutional analysis.

Bilateral donors are willing to finance TA; however most of them require tied procurement. It is therefore not always necessary to borrow for the implementation of TA. Through the PPC mechanism, for example, TA resources are being channelled to support environmental investment projects.

- ***Address environmental issues as early as possible in the project cycle.***

The potential environmental impacts of the project should be assessed (screened) as early as possible in the project preparation. Possible mitigation actions should be included in the project. By taking environmental issues into account early in the life of a project, potential environmental problems should be avoided or minimised.

Appraisal - an activity undertaken by the IFI

- ***Information will be required.***

The appraisal of a specific project is based on all available data and information. During the appraisal phase the IFIs might request additional information and this information must be provided in a transparent and timely fashion to avoid delays.

Implementation and monitoring - the responsibility of the borrower

- ***Monitoring is the least glamorous part of project work - but in several respects it is the most important.***

No matter how well a project has been identified, prepared and appraised, its objectives can only be realised when it has been properly executed. All projects face implementation problems, some of which cannot be foreseen. Adequate supervision is therefore of high priority.

- ***Implementation - Define project objectives in terms of project costs, time schedule and project quality and assign respective responsibility for their achievement.***

For each project a detailed implementation plan/schedule should be prepared. This plan outlines actions to be taken by the respective parties responsible for the implementation. This plan should be prepared in sufficient detail to ensure that the project is implemented efficiently.

- ***IFIs' procurement rules may require international competitive bidding - Design the procurement plan carefully.***

Consider pros and cons of turnkey versus sub-contracting in the given project condition with respect to achievement of principal project objectives (project cost, time compliance, quality) when designing the procurement plan.

In accordance with IFI guidelines procurement of goods and works financed under the loan will normally require international competitive bidding (ICB). The client is often unfamiliar with these procurement rules and guidelines. Through procurement seminars convened by the IFIs, information on the procedures is passed on to the borrowers. Compliance will be rigorously monitored.

Remember that procurement rules are designed to procure goods and works in the most efficient and economical manner to the benefit of the project and the borrower.

The borrower, not the IFI, is responsible for preparing the specifications and tender documents and evaluating the bids. The IFI's role is to make sure the borrower's work is done properly and the guidelines are observed so that the IFI funds may be disbursed for the contract.