

PROMOTING PAYMENTS FOR ECOSYSTEM SERVICES AND RELATED SUSTAINABLE FINANCING SCHEMES IN THE DANUBE BASIN

This project promotes and supports land managers who help us sustain the benefits that we all get from nature.

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Lessons learnt from testing payments for ecosystem services in the Lower Danube Basin

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This lesson learnt document is directed to PES/ SF practitioners and conservation experts

Context: The concept of Payments for Ecosystem Services (PES) and Sustainable Financing (SF) schemes are attracting growing attention in conservation and development circles as promising solutions to improve rural ecosystem's conservation and rural livelihoods as well as to transform questionable production subsidies into helpful payments for ecosystem services. The Danube PES project aims to demonstrate how PES and SF mechanism can work in the Danube basin. The project covered 5 pilot sites in Romania and Bulgaria, all of them protected areas, to test the efficacy of the selected approach by developing and applying tailor-made instruments, specific to the case.

Our piloting deliverables

(i) To develop at least 3 local demonstration projects in Romania and Bulgaria involving public-funded PES and sustainable financing schemes. The aim was to show in practice how national payments for extensive fish farming activities, extensive agriculture, co-financed by the European Fisheries Fund and the European Agricultural Fund for Rural Development, respectively, can help deliver ecosystem services while at the same time supporting and –under certain conditions– generating rural livelihoods.

(ii) To demonstrate the feasibility of at least 2 private sector-driven PES schemes. **One**, by working with a water utility company in the **Maramures** area to protect the watershed from which the company draws its water, including possible payments for ecosystem services to local farmers, foresters and other land users. And **two**, by working with fish producers in the **Calarasi** area to develop and market “green” fish that can be sold at a premium price to support extensive environmentally-friendly fisheries management.

The aim is to work with agricultural producers in all potential project sites and retailers to develop and market “green” agricultural products that can be sold at a premium price and thus reward related ecosystem services; to work with local stakeholders in all potential project sites and tourism companies to develop and market environmentally friendly tourism products.

Progress thus far (2010 - 2013)

Over a course of 3 years we worked on:

- two schemes addressing cultural services provided by protected areas in Rusenski Lom nature park, Bulgaria and Maramures, Romania
- one scheme on water regulation services in Persina nature park, Bulgaria

- one scheme on biodiversity maintenance on Ciocanesti fish ponds, Romania
- one national scheme focused on decreasing the water footprint of aquaculture sector in Bulgaria

Main challenges and lessons learnt

Understand the essence of PES internally

Understanding the essence of PES internally, within the team at the onset of the project is extremely important for its success. It was particularly hard to explain the role of economic instruments to conservationists and the ecosystem services approach and PES to communicators within the team. In many cases, "PES" was not the sexy communication word our communications colleagues were looking for. Sometimes, this limitation was also reflected on external communications prepared for local stakeholders thus, creating uncertainties. We tried internally to find a better way of expressing or explaining PES for different target groups but again the term was too abstract for communicators. What helped us in the process was the involvement of:

- (i) a new communications colleague in Romania (new to the WWF) who was never involved in WWF, who brought independent assessment of the situation and fresh ideas.
- (ii) external experts, in order to share their successful stories with the team

Lessons learnt: Communication is a powerful tool that needs to be carefully developed and updated. Internal capacity building is as much important as the capacity building of all other stakeholders. To support this process it is necessary to adapt your approach and communication to different targeted groups and speak from their perspective, even internally. This process requires investment of time! The purpose of a learning process is to assess and analyze how things change (or not) over time and, under what conditions something develops faster/better. Monitoring is in this case critical to measure changes over time.

Baseline data

PES design requires a significant amount of verifiable data. In this regard, a first step must include a detailed review of existing data, both within and outside the organisation. This is crucial for the construction of a timely and efficient PES design. It should be noted that national statistics in Bulgaria and Romania on land use and related practices cannot be linked at present to ecosystems or their services. For example, there is a comprehensive body of forest statistics, but it does not include carbon storage or sequestration capacity. In addition, older data are registered only on hard copies, and extrapolation is not always a solution. Therefore, constructing a valid and reliable baseline study requires additional funding and time, which should be reflected in budgets and work-plans. An additional limitation is that carbon data is region-specific and their use for other areas is not always reliable.

Another data-gathering related issue was the reliability of information sources. It happened that national and local data referred to each other, showing the same trends in the quality of environment, dating back to 1998. This was particularly peculiar in the case of water quality data in a Bulgarian PES scheme, where data showed no significant changes over a course of 20 years, although according to other official sources there were changes in economic activities in the selected river basin, such as sharp decrease of animals raised, depopulation and abandonment of lands.

In Romania, according to the National River Basin Management Plans (RBMP) aquaculture as a human activity represents only a potential threat to the ecological status of water systems¹. However, a first sample of water analysis taken in Ciocanesti pilot at the end of 2012 showed that aquaculture practices related to

¹ Can put pressure on a water body in case fish production is increased without taking specific measure for water purification or whenever proper structures according to specific needs of species are not in place. Ministry of Environment & ANAR, *National Danube River Basin Management Plan*, chapter 3.4.2, 2009

fish feeding might affect water quality. Monitoring of water quality in the pilot will continue until the end of 2012, in order to cover the full technological process and come with sound conclusions.

Lessons learnt: Part of the baseline information includes a review of validity/reliability of existing sources. It also includes a review on the availability of required data. This is particularly relevant in the case of pilot testing, where most of the schemes are based on secondary data. It is necessary first to go through all official sources and involve relevant key experts from national institutions to get an idea of the real situation, and then, carry out interviews at local level to define deviations from national/regional statistics.

Ownership of schemes

Involving stakeholders at an early stage of developing a PES/SF is key to a successful ownership and sustainability of a scheme. There are many aspects linked to this, which is necessary to be carefully assessed early in the pilot project, including: **communications, willingness and readiness (capacity) to participate**. In some project pilots, where WWF had been working for already a long time it was not difficult to define and launch a scheme, like in Rusenski Lom. In other areas, like Maramures, despite the presence of a local site coordinator of the scheme, there were no such favorable conditions for launching the scheme.

It is important to mention that despite similarities in the Rusenski Lom and Maramures schemes, there are many features which are setting the two apart, including the number of protected areas covered by the scheme, number and type of sellers of ecosystem services, the availability of management plans for these areas, the relationship of local site coordinators with local stakeholders and cultural differences. All these factors are influencing the work and level of ownership.

In any case, the team had to be really adaptable to and careful about reactions of local stakeholders. For example, in the Rusenski Lom PES scheme the local coordinator identified local leaders and promoted them through media, workshops, providing them with a leading role in the decision-making process, in the presence of other buyers and sellers of cultural services. A successful way to attract new supporters, after defining the elements of PES was: to gather in one place potential buyers and the identified project leaders who were able to transmit the PES vision and messages themselves; to actively involve local/national media to record successes and bring forward the local actors (the buyers and sellers of ecosystem services).

Another example is the Maramures scheme, where the team faced challenges on the side of local buyers of the ecosystem service. Although the team received, over a period of 1 year, positive responses to the idea of introducing a payment mechanism to enhance the scenic services provided by 7 small protected areas, suddenly the local leader gave up his responsibility and so did one of the buyers, while others are still sometimes showing signs of insecurity and doubt over their participation in the scheme. As far as the local leader is concerned, the main reason for this was the fear of assuming too big a responsibility as manager of the scheme; as regards the other buyers (the tourism sector operators), the reason for their insecurity and doubt was the lack of immediate direct benefits of their participation in the scheme, in terms of an increased number of tourists. Overall, the low level of understanding of the scheme led to misinterpretations by locals and the scheme was about to fail. Furthermore, although the team never promised to deliver on tourism, it became obvious that the needs of the buyers had to be taken into account as an enabling and necessary condition for the long-term sustainability of the scheme. A strategy was developed and it included: clarifying the roles and benefits of buyers from applying the scheme in Maramures; look for new partners and define the most motivated one to lead the initiative locally; provide tangible immediate benefits linked to the scheme that the buyers can understand. Following this plan, the team decided that such an immediate benefit would be provided through the elaboration of an ecotourism and local development strategy and the introduction of an ecotourism certification acknowledged worldwide. This strategy is giving positive results already.

Lessons learned: ownership of schemes might be affected by many factors, including cultural issues. These should be analyzed and assessed early enough to avoid risks of failure and/or the time-consuming process of adjusting the scheme. Analysis of stakeholders, especially in case of pilot testing should be performed regularly - despite the existence of a good baseline stakeholder analysis, the situations above might evolve at the stage of implementing the pilot scheme.

Willingness to pay and readiness to participate

There was an interesting test that the project team carried out during workshops (non WWF), when presenting the project. We asked people in the room "Those of you who are willing to pay 0,20 euro for forest protection, important for the quality of water you are drinking, please raise your hands". Everybody raised a hand. "Now, raise a hand all of you who are ready to start paying for this from now on". Very few people (5%) were really ready to pay. And this was tested for regulation and cultural services. So willingness and capacity to pay or participate are two very distinctive conditions/factors, which need to be properly addressed. Sometimes, in our experience, buyers were not willing to participate until they first witnessed the benefit that they would pay for. This was especially the case of cultural services in the 2 of the pilots (payments for maintaining aesthetic values). In other cases, readiness was missing because of the expectancy of high responsibility beyond the capacity of the buyer. In a third situation, the lack of readiness came through because of the lack of financial and technical capacity to get involved (also referring to reporting financial costs of the scheme in the accounting systems of buyers).

This situation also applies to sellers of ecosystem services. For example, in Ciocanesti and Persina pilots, our sellers were private entrepreneurs, who were ready to participate once we provided them with a set of activities, and related costs and benefits. However, the investment costs of participating in the scheme were too high for the sellers and impeded the start of the pilot. In Persina, the investment entailed purchasing special machineries and equipment (to collect and process wetland vegetation); in Ciocanesti, the costs related mostly to changing current practices related to management of production inputs (and construction of special nets on the fishponds), including use of basins not utilized at the moment. To cover this capacity gap the team had to look for external funding. In Bulgaria, the team submitted a proposal under GEF small grants but the proposal was rejected because it did not deliver immediate financial benefits within the timeframe of the project, and was rated financially unsustainable. The proposal was re-submitted and approved under the Operational Programme Human Resources, under measure BG051PO001-1.2.03 Promoting start-up of projects for the development of independent economic activity.

In Romania, the team looked for funding under the Operational Programme Fisheries. The project was rejected because the management measures the PES team developed and incorporated in the proposal were not approved by an evaluator, recognized by the Managing Authority of the Operational Programme.

Looking for external support, the team also explored the opportunity to attract private funding from tourism developers. For now, testing of measures is still pending because of the lack of funding, but remains a prerequisite to further promote the measures at national level as part of the Aqua-environmental measure of Operational Programme Fisheries. In this sense, the support of the Managing Authority is crucial.

Lesson learnt: conduct an indicative cost-benefit analysis for both buyers and sellers, as part of the baseline information.

Use existing public funding instruments, EU funds, to cover start-up costs of the scheme, especially capital investments.

PES, accounting and taxes

For quite a long time, a main challenge related to PES design has been the financial treatment of cash flows related to both buyers and sellers of ecosystem services. The seller situation referred to:

- (i) if the seller is an NGO, according to the Bulgarian and Romanian legislation, PES appears in accounting terms as income and there will be tax on it. If the income exceeds a certain annual amount, the NGO should go for a VAT registration, which would impact all other externally funded activities (especially EU-funded projects); if the seller is a state authority, the income will be again subject to a tax.
- (ii) on the buyers' side, PES is a cost but not related to the main economic activity. Therefore, this cost will not be deducted from the taxable base of the enterprise and this will increase the tax burden of the buyer because of the PES.

A question among the team was: should PES investments and activities in general be tax-free on both sides? After reviewing national legislations, we found out some windows of opportunity for decreasing the tax load on the PES scheme, such as: in Romania, donations of small amount might be provided without a cash receipt and there is no special accounting procedures for reporting them officially. In Bulgaria, companies can donate up to 10% of their income before tax to NGOs registered in public interest (tax shield). In Bulgaria, donations through mobile operators upon agreement are not VAT charged.

Another aspect is the publication and official reporting of revenue by buyers. In both Romania and Bulgaria, there was the case that local buyers do not report their revenues to tax authorities and in most financial periods they show financial losses. This put another obstacle in the way of the PES schemes because the PES was meant to be collected as a percentage on the income generated from main economic activities (accommodation and tourism in our case). So for this and promotional reasons too, the team developed promotional materials that would generate part of the PES from direct consumers of the aesthetic value provided by ecosystems in the area (directly from tourists).

In addition, in Romania we finally went for a fixed amount to be paid by buyers on an annual basis. In Bulgaria we also gave the option to charge the PES per night, and the team decided that all taxes should be paid according to the legislation - in this way to build trust among the national revenue authorities and to not create problems for business partners.

Lessons learnt: include legal/institutional review as part of the baseline information.

Try to partner with local/regional government authorities with political power to facilitate tax breaks for conservation/development activities which are of national interest.

Conservation vs social and economic priorities

In many cases we faced a situation whereby local stakeholders place economic and social goals before conservation. In this context, PES can really contribute to creating new jobs as well as new business opportunities. Using the reed from wetlands to produce pellets and briquettes is one of the examples we can show.

Lessons learnt: it is important to clearly state from the beginning to all partners that PES is not meant to solve social problems but it can contribute to it. Primarily, this is an economic instrument to conservation, showing clearly to stakeholders the link between their economic activities and nature, and benefits that they can get; it should be also noted that benefits from nature are not like financial income - they cannot run immediately but need time to re-generate (be restored), improve and to be sustained.

Legal framework

The main legal challenges for implementing PES pilots in the area is the fact that there are no previous payments for ecosystem services experiences at national level, and therefore there are no legal frameworks and/or documents stipulating the rights and obligations of buyers and sellers of ecosystem services (See in this regard Wunder (2005) in his definition of PES). Therefore, the teams in Bulgaria and Romania had to think about how to legally protect the interests of all parties involved in a PES deal.

Consultations were made with lawyers specialised in environmental legal practices. Even for them it was necessary to investigate the issue from different perspectives so that the eventual contract to be signed by parties is not in violation of tax and/or public administration legislation. Partnership Agreements (PAg) were specifically developed for the 2 cultural schemes and they were different because of the legal status of parties involved - some of them being public administrations, third class users of state budgets, while others being private entrepreneurs and NGOs. The main elements of the PAg were the definition of an ecosystem service (Rusenski Lom scheme), the definition of PES, the service itself and contractual obligations. It should be noted here that before this PAg, in the case of the Bulgarian pilot, ecosystem services and PES were only mentioned in the Forestry Act, also thanks to the actions undertaken by the WWF in Bulgaria, but no clear definitions of these were provided (still in 2013).

The PAg also contains information about the duration of the project - 5 years for the Rusenski Lom pilot and 3 years of the Maramures pilot. It specifies procedures for excluding and/or including old/new partners, as well as sanctions (penalties for both sides) in case of failure to comply with agreed rules. It is important to mention that WWF is not a signatory of the agreements. However, WWF is included as a member of Steering Committee (SC), playing a special role in the monitoring of progress of the scheme.

Legally, there are several parties linked to the cultural services scheme: (1) buyers, mostly private companies (in the Maramures pilot) and tourism-developing NGOs (in the Rusenski Lom pilot); (2) sellers - NGOs*; (3) Steering Committee - comprised of representatives of local stakeholders, monitoring the implementation, approving annual work-plans and budgets, able to take corrective and adjustments actions to the PES set-up, if necessary.

The relationships between buyers and sellers are stipulated in the PAg. The obligations of the SCs are stipulated in Statute of the Work of the SCs.

* One interesting aspect of the legal structure was the potential presence of an intermediary in the Rusenski Lom pilot. The seller of the cultural ecosystem services is an NGO established by the Directorate of Rusenski Lom Nature Park, who manages the territory of the pilot. The NGO was established in the late 90s to enable the Directorate to access external (non-state) funding. Initially, the team planned that the Directorate sign the PAg with businesses, but this would create problems with the income generated. The problem came from the internal procedures of reporting revenues from economic activities (that would appear in the case of a PES deal). Firstly, there would be a tax on this income; secondly, the income had to be transferred back to the state authority the Directorate was subordinated to and this could create a time gap between the moment of providing the PES and the moment of implementing obligations under the PES deal. For this reason and to avoid creating a too long, expensive and suspicious to buyers “supply chain” of ecosystem services, the signatory of the PAg in the Rusenski Lom pilot is the NGO.

Despite the development of a good legal basis of the scheme, we also found out that trust must exist among all those different players. Trust turned to be the baseline of business relations and when developing the legal documents we tried to put reasonable limits to buyers and sellers. Otherwise, we risked to lose them as partners in these pilot initiatives.

Lessons learnt: A legal framework is crucial for the whole functioning of a PES scheme. Where it does not exist be brave and create such a framework yourselves, with the support of legal and financial advisors. Trust is something that should exist even before the legal framework is set up because if we are too suspicious of private companies and put too many limitations on them, the scheme may not start. Cooperation needs to be based on trust in addition to legal agreements.

Overall lessons learnt and recommendations:

So if you think you may face some of/all these situations we recommend the following:

- Be careful how you develop your PES proposal to donors. Try to be realistic and commit to develop a feasible number of schemes!
- Ensure that your conservation and communications colleagues understand the approach and to test this, ask them to describe a PES mechanism in their own words
- Identify and involve key experts from national/regional administrations at an early stage. This will help you get an idea of the real picture of the ecosystems status and the level of services currently generated
- Get to know well the local stakeholders and their situation. Learn to listen to people and do not push them to enter an initiative they feel uncertain/insecure about
- Assess buyers and sellers not only for their willingness to participate but also for their capacity (readiness)
- Stick to the definition of PES as an economic instrument for conservation, and not a purely economic development instrument. Conservation is the starting point!
- Try not to put too many limits in the legal document and/or to buyers. Two aspects here: a flexible legal basis of the scheme to allow for an easy way of adapting it when necessary; trust is a key in business relations!
- Develop a monitoring system once you know which ecosystem service you want to target!
- Share your lessons