REPORT ON FINANCIAL INNOVATIONS FOR BIODIVERSITY (MAY 98)

A workshop at the 10th Global Biodiversity Forum
Bratislava, Slovakia
1-3 May 1998

The Friday sessions of the Financial Innovations for Biodiversity workshop were attended by approximately 40 participants from some 20 countries and 5 continents. Participants represented numbers organisations including governmental and non governmental organisations such as IFC, GEF, UNEP, and various local and regional trust funds.

The morning session outlined the CBD as a complex deal between North and South and between the private and public sector. Participants acknowledged that financing the global biodiversity agenda is a major challenge involving a wide range of institutions, and not an issue to be addressed by governments alone.

Previous meetings of the Conference of the Parties have been preoccupied with the workings of the Global Environment Facility and the eligibility criteria for funding. Participants acknowledged a need to focus on new and additional financial resources as called for in the CBD. In this regard economic policy instruments including taxes and other fiscal policy could provide a useful vehicle for financing the global biodiversity agenda while at the same time alleviating national budgetary constraints.

Regarding GEF financing for biodiversity it was noted that Sustainable Use projects are problematic because of the need to justify incremental cost. The perception of biodiversity projects has been that they only provide local benefits, making the task of quantifying global benefits more difficult. Thus it is difficult for biodiversity projects to pass the GEF criteria. In contrast, projects mitigating climate change are perceived as having global benefits or costs and are therefore more likely to be financed by the GEF. There was a consensus that although biodiversity requires local solutions, it needs to be recognised as a global issue.

Additionally it was noted that though several Parties to the CBD have drafted National Biodiversity Strategies and Action Plans, few have included a financial strategy for its implementation. As a result, many Parties face severe financial constraints in reaching the objectives of their National Biodiversity Strategies.

Innovative financial mechanisms are needed to finance the implementation of the National Biodiversity Strategies and Action Plans. A number of concrete experiences with setting up and managing Environmental Funds were presented in the afternoon session. Environmental Funds have been financed through internationally funded grant-making endowments and locally sustained by user fees and venture capital. Participants suggested that there is a potential to move beyond this traditional financing for Environmental Funds towards Environmental Funds. Among other things, this means involving the private sector or generating funds brokered under the Clean Development Mechanism of the Kyoto Protocol.

Saturday's sessions will address New Directions in Biodiversity Finance, Engaging the Private Sector in Biodiversity Finance, and Exploring Opportunities for Investing in Biodiversity.

1. Introduction

The GBF10 workshop on Financial Innovations for Biodiversity was organised by IUCN and UNEP. More than 45 participants from some 20 countries and a wide array of international and inter-governmental organisations, industry, academia, governments and non-governmental organisations attended the workshop. Drawing from a wide range of case studies, the workshop had two main purposes: (a) to broaden the scope of discussions on financing biodiversity conservation and sustainable use beyond reviews of the Global Environment Facility (GEF) and beyond calls for increases in official development assistance (ODA); and (b) to explore innovations in both public and private finance which generate substantive investments in support of the global biodiversity agenda.

2. Financing the CBD Agenda

The workshop consisted of seven sessions. The first session provided a general overview on the current status of financing the implementation of the global biodiversity agenda. The Convention on Biological Diversity (CBD) was presented as complex set of deals: a deal between North and South, a deal between the public sector and the private sector, a deal between national governments and local communities, and a deal between present and future generations. Deals imply some type of exchange be it in-kind or financial. Thus in order to understand the financial aspects of the global biodiversity agenda, it is necessary to understand the implications of these deals.

The CBD calls for new financial resources in support of its implementation. Article 20 calls on national governments to provide financial resources and incentives. It also calls on developed countries to provide additional financial resources to developing countries to support their implementation efforts. Article 21 establishes a financial mechanism which, as stated in Article 39, is the GEF. Article 21 also calls on Parties to the CBD to strengthen existing financial institutions in support of the objectives of the CBD. Other articles, such as Article 8(m) on in situ conservation, also call for new investments in biodiversity.

Finance had been a major agenda item in the first three meetings of the Conference of the Parties (COP) and it again featured prominently on the agenda of COP4 which took place immediately after this workshop. In preparation for COP4, the CBD Secretariat prepared three background documents on finance which where noted by the workshop participants. The first document reported on the activities of the GEF and the second provided an analysis its effectiveness. The third document addressed the topic of new and additional financial resources and provided an interesting analyses on tracking ODA and on how to promote the use of private financial resources. Several participants were concerned that the focus of COP4 would again be on ODA which has not been very innovative in bringing new finances for biodiversity. The document essentially requested the Secretariat to monitor ODA support for the CBD which does little to promote financial innovations. (Indeed COP4 made little progress on the topic of financial innovation and thus the insights from this workshop may want to be considered again at COP5).

With regard to GEF, the participants noted that sustainable use projects appear to be problematic for financing because of the need to justify incremental cost-financing in terms of global environmental benefits. For the most part, sustainable use projects generate local benefits. In contrast, projects to mitigate climate change are perceived as having clear global benefits and are therefore more likely to be financed by the GEF. Climate change is a global environmental problem requiring global solutions, while biodiversity is a problem of global significance requiring local solutions. Thus the incremental costs approach for sustainable use projects needs to be reconsidered.

The participants also explored developing criteria and indicators for investments that support the sustainable use of biological resources. Options include certification processes and ecolabelling schemes for forestry, fisheries, tourism, farming, mining and so on. If we are to promote new investments, especially of private capital, in biodiversity-related activities, we ought to have some means of identifying the impacts of the activities on biodiversity.

Overall there is a need to bridge the gap between the private benefits and costs of biodiversity conservation at the local and commercial levels, and the public benefits and costs at national and global levels. One way to approach this challenge is to link financing measures under Articles 20 and 21 to incentive measures under Article 11. Again indicators and criteria for investments in sustainable use and sustainable trade of biological resources are critical.

This session also pointed out that most Parties have completed or are now drafting national biodiversity strategies and action plans. Few if any of these, however, include a financial strategy. A biodiversity strategy without a financial strategy is actually not very strategic. Hence many Parties are likely to face severe financial constraints in implementing their action plans. Financial innovation is needed to finance the implementation of the CBD at the national level.

3. Establishing Biodiversity Funds

The second and third sessions focused on trust funds for biodiversity. Such trust funds are also known as environmental funds, national environmental funds or conservation funds. After a general overview of such funds, several case studies and specific proposals were explored.

The presentations in this session clearly demonstrated that trust funds vary widely in structure depending on the ways funds are sourced, managed and distributed. Nevertheless there are some commonalties. Most funds are governed by a mix of government and NGO representatives. Also funds are ideal vehicles for leveraging additional finance to innovative projects that fall outside the bounds of traditional development projects. For example, the Foundation for the Philippine Environment generates additional funds from various sources ranging from international agencies such as USAID, the World Bank, the MacArthur Foundation, and Keidanren Nature Conservation Fund to local companies, banks and foundations.

The participants also discussed several shortcomings of trust funds. In some cases, fund revenues may be captured by a government agency or by a NGO with little of the money reaching the intended objectives. Funds also often have very high overhead and administrative costs and they are generally far too conservative or unsophisticated with regard to investment strategies. Further the objectives of the donors sometimes differ markedly from those of the intended recipients. In the case study of the Mgahinga and Bwindi in Uganda, for example, the donors are concerned with biodiversity, while the local community recipients are concerned with improving their quality of life.

Despite their shortcomings, trust funds provide a promising long-term mechanism for financing biodiversity and thus should play a central role in the implementation of the CBD. Several participants suggested that the GEF might want to support targeted research on innovative trust funds, such as funds which are replenished by local user fees or private capital. The Clean Development Mechanism of the Kyoto Protocol may also provide opportunities for innovative biodiversity-related funds. Small private initiatives at the community level – as indicated by examples from Nepal, Pakistan, the Philippines, and Uganda – are likely to be more cost-effective and innovative than government-run funds. More research on fund innovations would provide useful guidance for the future of biodiversity trust funds.

4. New Directions in Biodiversity Finance

The fourth session explored several new directions in biodiversity finance. The first presentation re-emphasised the public good and private good aspects biodiversity. Private benefits of biodiversity can be traded in markets. Property rights can be established which will facilitate the emergence of biodiversity markets. One example is the introduction of individual transferable quotas in the fisheries sector. On the other hand, public benefits of biodiversity are more complex, such as the value of biodiversity for research or the existence values of unique habitats. Public benefits are thus more difficult to market and to finance. Since benefits from biodiversity have both public and private aspects there is a need for the innovation of financial instruments and processes which address both aspects. Such a strategy was termed market plus – hybrid instruments that combine economic incentives for private actors with conditionalities to ensure the provision of the public good aspects of biodiversity.

The second presentation provided examples of innovative biodiversity finance in the US Rocky Mountains. The Great Outdoor Colorado programme is financed through earmarked state lottery funds. This allows residents and visitors to support conservation through gambling! The lottery has already provided US$100 million for over 800 conservation projects. There is also a proposed Colorado Wilderness Tax on non-consumptive users of natural resources which would be levied on items such as cameras, films, binoculars, and camping equipment. The revenues raised from this sales tax would be earmarked to conservation activities. An important insight from this presentation was that social factors, such as community's tolerance for gambling, and political factors, such as acceptance of earmarked consumption taxes, must be considered in developing new instruments to finance biodiversity.

The next presentation reviewed financial innovations for wildlife conservation in Kenya. Despite the high economic value of Kenya's wildlife – both in national and international terms – it has failed to generate sufficient financial returns to cover the costs of conservation. Kenyan conservation also faces an inequitable distribution of benefits and costs, with benefits primarily accruing at the national and international levels and costs accruing at the local level. The funding gap and inequitable distribution of benefits and costs are due to a complex array of government and market failures. These lead to the inability of wildlife to pay for itself and thus ultimately to the loss of wildlife. Kenya's wildlife sector aims to overcome these distortions by innovations such as increasing the financial autonomy of government wildlife operations, restructuring existing wildlife markets, developing new markets and financial mechanisms for wildlife products and services, sharing government-earned revenues with private and communal landholders, devolution of rights to manage and use wildlife, the promotion of new wildlife enterprise partnerships, and innovative forms of capturing increased global funding. For a low-income developing country like Kenya, financial innovation is absolutely essential to the conservation of biodiversity.

This session also reviewed two case studies of financing biodiversity in Switzerland. The first case study demonstrated how the reformed Swiss agricultural policy contributes to biodiversity conservation and sustainable use by providing direct payments to farmers that apply biodiversity-sound management practices. The second case study described the Swiss Foundation for the Conservation of Cultural Landscapes. It is financed by federal, cantonal, communal and private donations to support specific nature and landscape conservation projects.

The participants noted that innovative economic policies could stimulate new financial resources. Such policies are more likely to succeed if they are focused, initiative-based, locally-driven, vertically-integrated, based on good science, provide the right incentives, are culturally acceptable, and are socially appropriate.

5. Engaging the Private Sector

The workshop then looked at several initiatives to engage the private sector in biodiversity finance. The first presentation provided some interesting insights from the experiences of the International Finance Corporation (IFC) – the private sector investment bank within the World Bank Group. Over the last five years it has begun to co-finance biodiversity-linked enterprise in sectors such as forestry, agriculture, tourism and wildlife use. One programme has focused on small and medium-sized enterprises which generally do not have access to long-term capital. Additionally the IFC is setting up a private venture capital fund for biodiversity enterprises in Latin America. This fund will start up with a base of US$ 20-50 million from various sources including the GEF, the IFC, the government of Brazil and Switzerland and other private sector sources. The IFC experience indicates that the major challenge is not finding the money, but rather finding viable biodiversity projects in which to invest.

The second presentation described a innovative Dutch scheme for green investment funds. This government-created scheme uses a fiscal tax subsidy to promote private investments in environmental projects. It allows Dutch citizens to put their savings or investments into green funds run by commercial banks. The interest on loans from these funds are exempt from tax as long as the money is invested in green projects. Starting in 1998, the funds will be able to invest in a selection of countries outside of The Netherlands. This is because the funds have attracted far more capital than can be invested in green projects within the country. This approach shows how a well-targeted 2% tax subsidy can generate billions of dollars of private finance for biodiversity.

The third presentation highlighted an exciting new biodiversity partnership between a private company and a NGO. British Petroleum has teamed up with Flora and Fauna International to develop a corporate biodiversity strategy. Just as national governments are developing biodiversity strategies under the CBD, it also provides a framework for national companies and multinational corporations to develop their own corporate biodiversity strategies. BP is taking the lead in exploring new opportunities for directing their corporate earnings as well as corporate investments in ways that support biodiversity.

The last presentation of this session introduced UNEP's Financial Services Initiative. This initiative includes more than 100 of the world's largest financial institutions. All have signed the UNEP Statement by Financial Institutions on the Environment and Sustainable Development which commits them to incorporate environmentally-sound practices into their external and internal operations. The financial services sector harbours key skills, technologies and economic resources which could contribute to biodiversity conservation. As the most important contributor of private sector credit, the signals they send to their clients about the relationship between environmentally-sound management practices and credit lending rates is critically important for biodiversity finance. This is especially true in the context of globalisation, since banks and other financial intermediaries are inextricably linked through international lending and investment practices to activities that can degrade biodiversity. Also investments in the provision of biodiversity goods and services are increasingly becoming attractive due to emerging biodiversity markets. The UNEP initiative can provide a forum for bridging the gap between private banking and biodiversity conservation.

The participants noted that the underlying factors behind private sector biodiversity finance include:

- institutional failures, such as missing markets and non-existent property rights for biodiversity goods and services;
- information failures, such as lack of scientific knowledge, lack of public awareness and lack of sustainability criteria; and
- enforcement failures, such as lack of appropriate legal systems.

To address these failures and to conserve biodiversity there is a need to consider targeted structural reforms of the systems of public finance and private finance. Such structural adjustment for biodiversity is probably necessary to stimulate financial innovations.

6. Exploring Opportunities for Investing in Biodiversity

The final session included four forward-looking presentations on increasing funding for the implementation of the global biodiversity agenda.

The first presentation noted the desperate situation of biodiversity loss and the critical need for financing emergency actions for biodiversity conservation. Financing emergency actions involves an adaptive management process which could include:

- acquisition or renting of representative and unknown ecosystems;
- restoration and management of natural environments;
- increased research, inventories and training;
- compensations to eligible parties for losses; and
- opening of profitable markets for wild products issuing from sustainable extraction.

To finance these actions, governments could agree to levy a sales tax of 10% on exports of biological products. The revenues from this tax would be substantial and could be earmarked for national biodiversity programmes. Though the participants supported the idea of focusing on emergency actions, they were skeptical about the general acceptance of a system of national excise taxes on wildlife and nature related trade.

The second presentation provided a fresh perspective on how bankers perceive biodiversity. It highlighted examples from the Peruvian situation noting that in order to finance biodiversity through private banks there is a need to bridge the gaps in understanding, approach, philosophy, language and perception between bankers and conservationists. Today a banker's perception might allow for investments in brown issues, but more needs to be done to encourage bankers to consider green issues. If we are to attract private finance to biodiversity, we need to connect the language of biodiversity to that of banking.

The third presentation provided a comprehensive set of tools for landowners and policy makers to support ecosystem management and increase financial resources. Several of these tools where considered in earlier sessions. This presentation, however, provided a conceptual framework and identified six broad categories:

- property rights;
- tax policies;
- incentive-based tools;
- private-public partnerships;
- government programmes; and
- voluntary initiatives.

The challenges and opportunities of linking two Rio Conventions – the CBD and the Framework Convention on Climate Change (FCCC) – where explored in the final presentation. The Kyoto Protocol could potentially create incentives and generate significant financial resources for more effective and sustainable management of forests and other carbon-sequestering ecosystems. Three measures are included: joint implementation, the clean development mechanism and emission trading. These measures will allow countries to buy, sell or trade reductions in greenhouse gas emissions. It is still too early to assess the potential impacts of the Kyoto Protocol for biodiversity, but with careful consideration of both the climate change and biodiversity agendas, the Kyoto Protocol could be developed as an innovative financial instrument that supports the objectives of both the FCCC and the CBD.

7. Conclusion and Recommendations

The participants agreed that financial innovations for implementing the biodiversity agenda are crucial. These innovations need to be developed as part of the broader framework of enabling conditions which include clearer definition of property rights, strengthening of the legal system, reform of fiscal policies, increased public awareness, and new partnerships between public agencies, private companies and NGOs. Financial innovations is a necessary, but not sufficient component of any national or corporate biodiversity strategy.

There was a clear realisation that biodiversity conservation will not and cannot be achieved by governments acting alone. The private sector has a pivotal role to play and should become involved not as a matter of corporate philanthropy, but as a matter of self-interest. Business should profit from the sustainable use of biological resources and in the interest of its stakeholders – customers, employees and shareholders – business should ensure that its activities do not threaten biodiversity.

The workshop ended with an open and lively discussion of the key points and insights from the various presentations and interventions. Out of this discussion emerged a statement of recommendations for consideration by COP4.