

**THIRD ANNUAL CONFERENCE OF THE GREEN GROWTH KNOWLEDGE PLATFORM
"FISCAL POLICIES AND THE GREEN ECONOMY TRANSITION: GENERATING
KNOWLEDGE – CREATING IMPACT"**

CLIMATE CHANGE PUBLIC EXPENDITURE AND INSTITUTIONAL REVIEWS (CCPER): LINKING FISCAL POLICIES TO THE GREEN ECONOMY TRANSITION

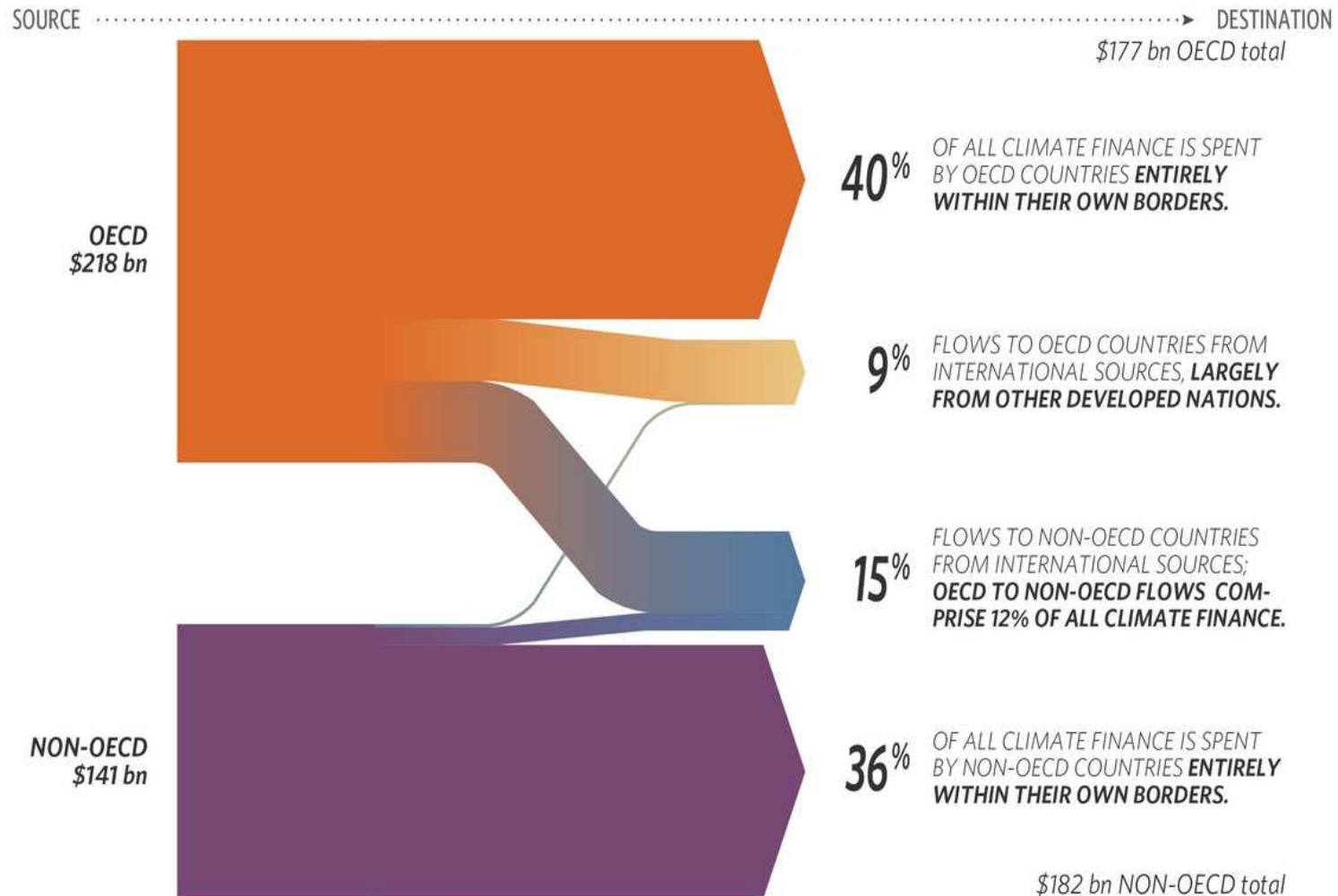
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SNAPSHOT OF TODAY'S CLIMATE FINANCE

76% OF ALL CLIMATE FINANCE IS SPENT BY COUNTRIES ENTIRELY WITHIN THEIR OWN BORDERS, SUGGESTING THAT INVESTORS PREFER FAMILIAR ENVIRONMENTS THEY PERCEIVE AS LOWER RISK.



CHALLENGES OF FINANCING CLIMATE CHANGE SOLUTIONS

- Climate change action requires planning over a long horizon in the face of uncertainty as well as, for many governments, costly financing in the near term.
- Countries need to consider funding from diverse sources within a consistent framework.
- Climate change will affect the core business of finance ministries related to fiscal policy, government budgets, and public debt.
- Good practice is emerging for budgeting for climate action, firmly rooted in the traditional principles of public expenditure management.

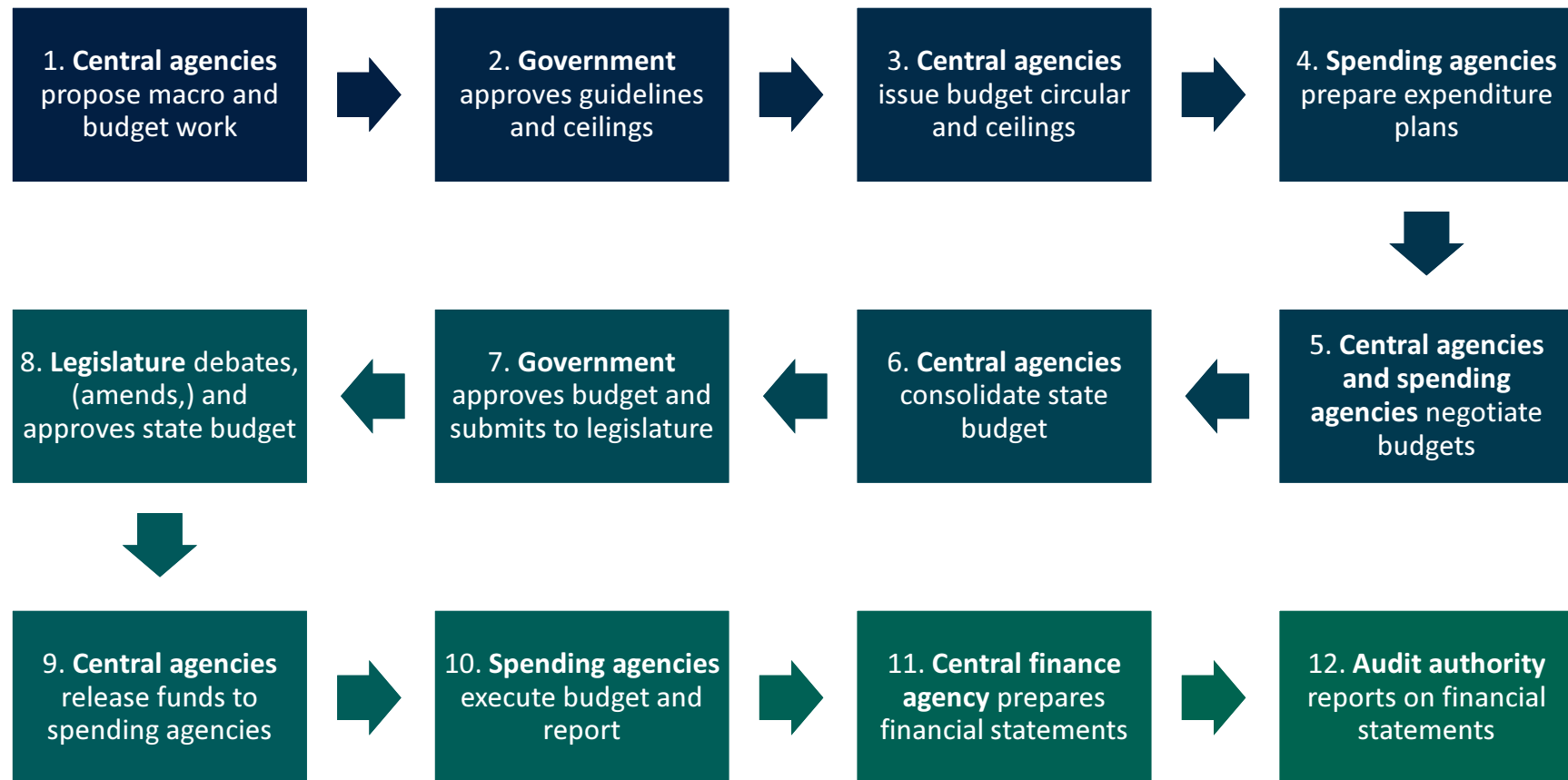
CLIMATE CHANGE PUBLIC EXPENDITURE AND INSTITUTIONAL REVIEW (CCPER) SOURCEBOOK

- Building on more than 400 Public Expenditure Reviews undertaken over the last 15 years and drawing on client experiences, expert interviews, consultations with UNDP and GEF, and workshops with 22+ countries in Asia-Pacific, Africa, Latin America and Europe.
- The [Climate Change Public Expenditure and Institutional Review Sourcebook \(CCPER\)](#) is the first step toward providing practitioners with comprehensive information about the tools and information needed to ***respond to the public expenditure policy and management challenges arising from climate change***.
- CCPERs facilitate the integration of climate change policies into government plans and budgets.

Challenges of Climate Budgeting

- 1. No single institutional advocate:** Spending agencies may pursue climate change policies where these are aligned with agency objectives and interests—but this will not always be the case. Environmental agencies will not be able to shift resources towards climate change policy goals alone, or have an impact on base expenditures while the level of funding is likely to be modest in relation to the overall budget. → ***Engagement by central finance and planning agencies is thus essential if climate change policies are to be reflected in budgets. The instruments available to influence resource allocations are:***
 - Consolidation of parallel - both recurrent and investment - budgeting processes under a single central agency bolsters the central finance agency's authority;
 - Enforcement of agency-level budget ceilings at the start of the budget process;
 - Statutory requirements for agencies to report on off-budget expenditures;
 - Adoption of a medium-term perspective to expenditure planning.
- 2. Many public sector resource allocation decisions that are relevant to climate change are made **outside of the budget process.**** → Central finance and planning agencies should track and report on these expenditures, ideally in budget documentation.

A Stylized Budget Process





☑ At the Start of the Budget Process

At the Start of the Budget Process

Where climate change is an important policy agenda, climate policy measures will typically be laid out in pre-budget statements, the budget circular, and administrative guidelines issued at the start of the budget process.

- In the U.K., for instance, the Treasury's Pre-Budget Report highlighted revenue and expenditure measures in support of environmental and climate-change-related policies.
- In South Africa, policy commitments (such as the proposed carbon tax and establishment of a fund for green economy initiatives) are announced in the medium-term budget statement. The budget circular, meanwhile, supports implementation of these policies by providing guidance on the presentation of climate-change-related expenditures in the agency budget proposals.
- The Philippines Budget Circular, for example, requires agencies to categorize programs according to the government's five priority spending areas, one of which corresponds to environment and climate change mitigation and adaptation.



☑ Adopting Medium-Term Expenditure Frameworks (MTEFs)

Adopting Medium-Term Expenditure Frameworks (MTEFs)

- **Why?** Annual budgets offer limited scope for adjusting resource allocations in line with emerging policy priorities. Limited resources can be released from base expenditures as ongoing programs have legal obligations to staff and suppliers.
- **How?** Medium-term expenditure frameworks (MTEFs) facilitate adjustments in resource allocations and their alignment with new policy priorities (such as climate change), and they provide a predictable basis for agency expenditure planning.
- **Who?** MTEFs have become widespread since the mid-1990s, and 132 countries have introduced some form of medium-term expenditure plan.

Adopting Medium-Term Expenditure Frameworks (MTEFs)

- **A medium-term perspective also helps instill discipline in sector-level expenditure planning.** Sector plans translate policy objectives into program and project level resource allocations by linking expenditures to the intended outputs and outcomes of public policy. Rigorous costing of programs helps focus attention on what can realistically be delivered, forcing sector-level decision makers to consider tradeoffs, priorities, and the appropriate sequencing of interventions. MTEFs facilitate this process by setting a ceiling to budget projections, which then imposes on agencies the need to identify priorities that come on line if additional resources are made available. In the absence of resource constraints set by MTEFs, sector plans can turn into wish lists offering possible interventions that provide little useful guidance to decision makers.
- **Realistic** costing of climate change-related programs and projects is more likely to result from planning processes that bring **together sector agency planning units, operational departments, and finance agencies' staffs**. This has been the experience from poverty reduction planning. Also important are processes that link agency-level negotiations on resource allocations to reviews of program and project-level performance and to the expected results of public spending.



☒ **Review by Central Finance and Planning Agencies**

Review by Central Finance and Planning Agencies

- **Specialist climate change policy units or committees** can support this review or challenge function. Central finance and planning agency officials' limited capacity to understand climate change policy issues and their implications for particular sectors may hinder effective integration of climate change policies. Awareness raising and training can strengthen this capability.
- **Central finance and planning agencies** can also involve specialist climate change institution in the review process. This may range from advisory support, such as commenting on a budget policy or on budget proposals' review criteria from a climate change perspective – to more formal involvement in the review of specific programs and projects.
- **Inter-ministerial arrangements** for coordinating climate change strategy significantly differ by country. The coordinating committees on climate change can be headed by the prime minister, by the minister of environment, or by the head of another government agency, and can include different ministries and government agencies.



☑ Creating Incentives and Scaling Up by Setting Budget Targets

Creating Incentives and Scaling Up by Setting Budget Targets

The **central and spending agencies** have to put in place systems for target setting and monitoring. The extent to which these systems are compliance-oriented will depend on whether the targets are “hard” or “soft.” The systems needed to support this function comprise four elements:

1. The **central finance and planning agencies** have to determine **how targets should be applied across government** so that the sum of agency climate change expenditures equals the aggregate target. Because some programs will have closer alignment with climate change objectives than others, a single target across all agencies and programs is not recommended.
2. The **central finance and planning agencies** have to determine the **criteria** that define climate change expenditures and provide guidance on the **presentation of these expenditures in the budget** submission and budget documents used for the government’s decision making and in communications with the legislature. (Budget classification will be discussed later on.)
3. **Central and finance authorities** have to put in place a **robust budget review process** to ensure that the spending agencies are applying the climate change criteria appropriately, instead of “green-washing” programs.
4. The government’s financial reports will need to generate information that allows the **central finance and planning agencies** to **monitor resource allocations** during **budget execution and for the end-of-year reporting**.



☑ Long-Term Expenditure Planning

Long-Term Expenditure Planning

- **Why?** Short-to-medium-term perspectives fail to capture the fiscal implications of economic, social, and environmental challenges that will emerge over the long-term. And when longer-term fiscal forecasts are prepared, they are usually for the purpose of assessing fiscal sustainability, which is narrowly defined in terms of financial solvency. They may miss the opportunity to adjust current policies in such a way as to mitigate risks and reduce future costs.
- All OECD countries now undertake long-term fiscal forecasting focused on the major risks to fiscal sustainability, but **only a handful of OECD countries have recently started to consider the long-term fiscal impacts of climate change**. The central finance agencies of the United Kingdom and Australia each discussed climate change risks in long-term forecasting exercises prepared in 2010.
- **For most governments, the first step in any long-term expenditure planning exercise is to simply take stock of climate change impacts, the fiscal risks that may arise, and their implications for current policy.** Risk assessment is a useful exercise in itself, identifying the areas where the government has to take action today to address long-term challenges.
- **Estimating the costs of adaptation poses significant challenges for financial planners given uncertainty regarding future impacts, the nature of the policy response, and the implications for current policy.** The challenge is that most of these forecast the economic cost of adaptation rather than the financial costs to the public sector. There are also significant data constraints for this kind of exercise, but simply identifying these cost drivers is an important step in understanding the likely climate change impacts on program costs.



☑ Resource Allocation Outside the Budget Process

Resource Allocation Outside the Budget Process

- **Many public sector resource allocation decisions that are relevant to climate change are made outside of the budget process.** These typically include externally financed expenditures, both from development assistance and climate change finance; mandatory expenditures; expenditures of autonomous entities, state-owned enterprises, and local government; and off-budget expenditures related to quasi-fiscal operations, government guarantees, and taxes.
- Climate change expenditures may be included, and indeed may be significant, in all of these categories. The challenge for **central finance and planning agencies** is first and foremost to **track and report on these expenditures, ideally in budget documentation.** Once information is available in a context which reveals the financial implications of allocation decisions taken outside of the budget, decision makers are better placed to assess the trade-offs between alternative uses of funds and to align resources with government policy objectives.

Ongoing Work

- Climate Change PERs hold the potential to both better coordinate fiscal policy and fiscal instruments within a country across the range of climate change action as well as the potential to motivate more coherent and deeper action by countries.
- The special public expenditure policy and management challenges posed by climate change are not yet resolved, in particular, decision making under uncertain future climate conditions, expenditure planning for extreme weather and climate events, and the lack of agreed –upon budget classifications for climate related activities.
- The Sourcebook will continue to be updated to reflect the latest knowledge on good practice to best inform policy making by providing clear operational guidance, helping to raise awareness, and supporting policy dialogue.