

**MOBILISING FINANCIAL RESOURCES FOR
THE ENVIRONMENT IN RUSSIA**

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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FOREWORD

In May 2007, the OECD Council agreed to open discussions on Russia's accession to OECD, which will clearly change the relationship between the OECD and Russia. OECD-Russia cooperation on environmental issues dates back from the early 1990s. The Environmental Performance Review of Russia, carried out by the OECD in cooperation with UNECE in 1999, constituted an important milestone in this cooperation. The Review was the first comprehensive and independent assessment of environmental conditions and policies in Russia. Subsequently, analyses of specific instruments of environmental policy, most importantly pollution and natural resource charges, were conducted.

The current report continues this series of policy analyses and provides an update of some of the developments in environmental expenditure and finance in the Russian Federation. It builds on work undertaken under the aegis of the Task Force for the implementation of the Environmental Action Programme (EAP Task Force) for countries of Eastern Europe, Caucasus and Central Asia (EECCA). The OECD serves as the secretariat for the EAP Task Force. A workshop on *Financing for Environment in the Russian Federation* was organised in Moscow in December 2006 and hosted by the Russian Regional Environmental Centre (REC) to discuss preliminary results.

Xavier Leflaive prepared this report. Carla Bertuzzi, Nelly Petkova, Alexander Martoussevitch, all members of the Finance Team, have been involved in the separate projects this report builds on. They have provided valuable insights. Brendan Gillespie, Head of the Environment and Globalisation Division, has reviewed a previous draft of the report. The Finance team owes a special debt to all persons and organisations in Russia who helped in collecting and compiling data reported here.

This report builds on several studies:

- The report on Trends in Environmental Finance in EECCA, drafted by Carla Bertuzzi and Xavier Leflaive. Vladimir Morozov assisted in collecting data from the EECCA countries. The report was published as a stand-alone document and disseminated in the context of the Environment for Europe Process in 2007. The project was supported by UK Defra.
- The case study on Intergovernmental Transfers, drafted by the Institute for Urban Economics, Moscow. The report has discussed and endorsed by experts of the Environmental Finance Network and delegates of the EAP Task Force. It was financially supported by a grant from the government of the Netherlands (Ministry of Housing, Spatial Planning and the Environment).
- The case study on Local Financial Markets, prepared by Mr. Emin Askerov, Institute for Urban Economics, Moscow, under the supervision of George Peterson, from the Institute for Urban Economics in Washington DC, USA. The project was discussed during an expert workshop in Moscow in June 2006 and a meeting of the Environmental Finance Network. It was financed by the European Commission (TACIS).

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TABLE OF CONTENTS

FOREWORD	3
LIST OF ABBREVIATIONS	5
EXECUTIVE SUMMARY	6
BACKGROUND.....	9
Macro-economic trends	9
Environmental policy objectives and obstacles to their achievement.....	9
Trends in environmental expenditure in Russia	11
INSTRUMENTS TO FINANCE ENVIRONMENTAL POLICIES IN RUSSIA	18
Revenues from economic instruments	18
User charges for water supply and sanitation	19
Environmental funds.....	24
Intergovernmental transfers for environmental infrastructures	25
Local financial markets for water supply and sanitation	32
External environmental assistance.....	37
ANNEXES	39
Annex 1. A method to monitor environmental protection expenditure	39
Annex 2. Mechanisms for intergovernmental transfers in Russia	43
Bibliography	52

Tables

Table 1.	Calculation principles and sources of pollution charge payments	19
Table 2.	Federal transfers to regional governments – the Russian Federation	27
Table 3.	Structure of federal assistance to subjects of the Russian Federation	28
Table 4.	Revenue structure of Russian regional consolidated budgets	29
Table 5.	Revenue structure of Russian local budgets	30
Table 6.	Finance structure of FTRDP.....	46
Table 7.	Structure of state capital investments under FTIP.....	51
Table 8.	Investment support provided by FTIP and RDF	51

Figures

Figure 1.	Total environmental protection expenditure in the Russian Federation.....	12
Figure 2.	Environmental protection expenditure as a share of GDP	13
Figure 3.	Environmental protection expenditure by domain	14
Figure 4.	Share of current/investment expenditure in total environmental expenditure.....	14
Figure 5.	Environmental protection investments, by domain and by sector.....	15
Figure 6.	Environmental expenditure as a share of general government expenditure	16

Boxes

Box 1.	Illustration of WSS investment financed by and SPC.....	33
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LIST OF ABBREVIATIONS

BC	Budget Code
BEI	Budget Expenditure Index
CEE	Central and Eastern Europe
CF	Compensation Fund
DAC	Development Assistance Committee
EAP Task Force	Task Force for the implementation of the Environmental Action Programme
EBRD	European Bank for Reconstruction
EECCA	Eastern Europe, Caucasus and Central Asia (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, the Russian Federation, Tajikistan, Turkmenistan, Ukraine, Uzbekistan)
EJT	Economically Justified Tariff
ELV	Emission Limit Values
EU	European Union
FEF	Federal Environmental Fund
FFSF	Federal Financial Support Fund for Federation Subjects
FTIP	Federal Targeted Investment Programme
FTP	Federal Targeted Programme
FTRDP	Federal Targeted Regional Development Programmes
GDP	Gross Domestic Product
GKO	Federal Government Bonds
IFI	International Financial Institution
MUE	Municipal Unitary Enterprise
OA	Official Assistance (flows of assistance going to the following transition countries: Belarus, the Russian Federation and Ukraine).
ODA	Official Development Assistance (flows of assistance going to the following developing countries: Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Tajikistan, Turkmenistan and Uzbekistan).
RDF	Regional Development Fund
REC	Regional Environmental Centre
RF	Russian Federation
RMFRF	Regional and Municipal Finance Reform Fund
SECF	Social Expenditure Co-Finance Fund
SFGs	Subject of Federation Governments
SPC	Special Purpose Company
UNECE	United Nations Economic Commission for Europe
WB	World Bank
WSS	Water Supply and Sanitation

EXECUTIVE SUMMARY

Establishing a modern environmental management system that matches new economic and social realities is one of the challenges that Russia faces. To address this challenge, Russia has dedicated major efforts to the development of its environmental legal and institutional frameworks. Environmental laws and regulations now address most of the priority environmental issues (see OECD, 2007a).

Government agencies responsible for environmental policy design, regulation, and compliance act at both federal and sub-national levels, and environmental policy implementation is increasingly decentralised. During the last five years, innovative policy instruments (such as industry rating, environmental management systems and corporate reporting) have been adopted or further promoted, and traditional instruments (e.g. environmental quality standards, permitting, and environmental liability) have been under reform.

Environmental finance in Russia illustrates this dynamic and some of its limitations. It also illustrates some of the challenges that countries undergoing the transition to a market economy face in financing environmental expenditures, particularly for environmentally related infrastructures.

While environmental finance has witnessed a number of innovative developments in recent years, it currently relies on a limited set of instruments. Innovative approaches (local capital markets, carbon funding) are promising but remain underdeveloped; traditional ones (tariffs for environmental services, intergovernmental transfers) could be adjusted to better fit the needs of efficient environmental policies. This is particularly the case for financing investment in environmental infrastructure (water supply, sanitation, municipal solid waste).

This report sheds some light on these issues.

Recent data collected in Russia and in EECCA countries indicate that environmental expenditure in Russia has increased to levels which compare with some CEE countries. However, the level of expenditure remains low as a share of GDP, and expenditure is still largely concentrated on the water sector; current expenditure still represent the bulk of environmental expenditure and the share of investment remains low. Environment protection expenditure has not fully benefitted from the robust economic growth of Russian economy since the turn of the century: its share in GDP or in general government expenditure has declined since 2000. There are opportunities to increase both public and private expenditure volumes, to increase the share of investment in cleaner technologies, and to allocate resources to a wider variety of environmental domains. This requires making a better use of existing financing instruments and harnessing new sources of finance.

The capacity to mobilise additional sources of finance for the environment and to make the best use of them can contribute to a number of issues which are high on the Russian agenda (OECD, 2006b): sustained economic growth, more effective innovation policies, tackling the health crisis.

Reform tariff policies at local level

Despite significant increases since 2000, tariffs for municipal environmental services usually fail to generate sufficient resources for the development of the service and the (regulated) service providers; there are some exceptions, though, which explain the increased involvement of the private sector in water supply and sanitation and in waste management (although in the latter, compliance with waste regulation is an issue). Municipal tariff policies lack robust legislative and methodological bases. They provide little incentive for cost reduction and fail to anticipate investment needs.

Tariff regulation for environmental goods and services could be reformed to increase cost recovery, particularly for water supply and sanitation. This would generate additional resources and, in addition, enhance the creditworthiness of the providers of such services and their capacity to harness local and financial markets to finance investment in environmental infrastructures. This capacity is underdeveloped, and increases demand for budget support to finance environmental infrastructure.

Disseminate modern mechanisms for intergovernmental transfers

Responsibilities for budget support for environmental infrastructure and services have been devolved to regional/local jurisdictions. However, these administrations have not been given the means required to meet them. Russian municipalities are still largely dependent on fiscal transfers from central or regional budgets. Russia mostly relies on inter-governmental transfers to bridge the financial gap that arises between the costs of local policies and services and the revenues to which local authorities have access. General purpose transfers, typically in the form of equalization schemes, are frequently used but can have negative economic and financial consequences. In particular, they enable local budgets to increase their expenditure without raising additional tax revenues: local governments have no incentives to expand their own tax base or revenues from user charges.

However, there are positive developments: the use of economic, demographic and geographic statistics (not tax revenue statistics) to estimate regional revenue capacities, expenditure liabilities, and need for equalizing transfers; the allocation of resources between regional governments on a competitive basis (see the Regional Finance Reform Fund); the introduction of transfer mechanisms to allocate finance directly to investment projects (the Regional Development Fund).

Further reform should ensure that significant volumes of finance are channeled to local jurisdictions; that revenue flows are stable and can be incorporated into comprehensive financial strategies; that money is not diverted from the initial projects, while respecting the autonomy of the local governments to allocate resources to priority investments.

Turn environmental funds into efficient financing mechanisms

In Russia, environmental funds originated as off-budget, public sources of environmental finance. After a series of reforms, remaining environmental funds are mostly earmarked budgetary funds consolidated into regional budgets. They are one of the main sources of environmental finance for municipalities which are under severe budget constraints. However, most funds focus on resource collection and direct procurement and have weak spending programmes and project appraisal and financing capacities. OECD tools in this domain can help make a better use of these instruments (see in particular OECD, 2006c, 2007c, 2007d).

Harness local financial markets to finance investment in environmental infrastructures

Although Russia has experienced the negative consequences of mismanaged local debt in the early 1990s, the macro-economic and institutional contexts have changed dramatically in the recent years, providing new opportunities to develop market-based approaches.

Local credit and capital markets in Russia remain underdeveloped and difficult to access for environmental infrastructure rehabilitation and development projects. The ongoing reforms of fiscal federal relations and of local self-governance have not helped strengthen the financial position and creditworthiness of the municipalities, and hence their capacity to borrow. This is reinforced in the water supply and sanitation sector, by the poor financial health of water utilities.

Lack of experience with providing long- and even medium- term loans to finance water supply and sanitation (WSS) infrastructure rehabilitation and development projects by Russian commercial banks, is another major obstacle for local credit and capital market development. The appearance of domestic private operators, however, has created new opportunities for financing the WSS sector.

As part of the process of fiscal decentralization, the policy and institutional obstacles that prevent the financial sector from playing a greater role in financing environmental projects should be removed. Possible manoeuvres include the right for local authorities to incur debt within a clear fiscal framework, support for the development of carriers of long-term savings (insurance companies, banks), regulation of the portfolio of these institutions (and the share that they are allowed to invest in local jurisdictions). Experience from countries with more developed local capital and financial markets could assist Russia policy makers to assess how these markets could play a greater role in financing environmentally-related infrastructure.

International environmental cooperation

Domestic finance is the main source of environmental expenditure in Russia.

Bilateral and multilateral environmental assistance remains marginal as a share of GDP (below 0.6%). Its structure has changed since 2001 in the EECCA region. IFI financing almost doubled, although it started from a low level after the financial crisis had affected a large number of projects at the turn of the century. In contrast, bilateral environmental cooperation (including the European Commission) in 2005 is below the level of 2001.

However, projects supported by the international community are recognised as having particularly positive demonstration and catalytic effects, both in terms of technology transfer and the development of new skills and know-how.

BACKGROUND

The Russian Federation has embarked on the transition to a market economy in January 1992. Transition entails: liberalisation, stabilisation, private-sector development, and the redefinition of the role of the state (see OECD 2005).

Macro-economic trends

The Asian financial crisis and the falling commodity prices sparked a crisis in Russia in 1998. The banking sector was hit particularly hard. The government executed a massive fiscal adjustment, refraining from indexing expenditure commitments to inflation. The economy started to rebound fairly rapidly: industrial production picked up in October 1998. By early spring of 1999, it had already surpassed the pre-crisis levels of 1997. Later on (around 2001), the oil sector emerged as the locomotive for growth.

Since 1999, the Russian economy has grown strongly, buoyed by rising terms of trade, which, in turn, are supporting a boom in domestic consumption. Growth has been largely dependent on transitory factors and the transition to self-sustaining, investment- and innovation-led growth will require both continued sound macroeconomic management and a range of structural reforms aimed at improving framework conditions for business.

The recent survey of Russian economic performance argues that fiscal policy should be the primary instrument for tackling this challenge (OECD, 2006b). This is important in the context of this report, as economic instruments and public budgets are essential sources of environmental finance.

Improving the quality of public administration remains a major challenge for Russia: inefficiency, corruption and lack of accountability that afflict public administration in Russia impose substantial direct costs on both entrepreneurs and ordinary citizens. Administrative reform should be linked to a revision of the scope of state ownership and regulation.

Environmental policy objectives and obstacles to their achievement¹

Russia is facing significant environmental challenges. Their magnitude can be illustrated by the fact that about 15 percent of the country's territory suffers from exposure to high levels of ambient pollution. In many industrial centres (*e.g.* Dzerzhinsk, Irkutsk, Kemerovo, Krasnoyarsk, Novokuznetsk, Norilsk, and Cherepovts), the rates of morbidity and mortality exceed 1.5-3 times the national average.

¹ This section builds on OECD, 2006a, *Environmental Policy and Regulation in Russia. The Implementation Challenge*

A number of factors further worsen environmental conditions in Russia, including:

- Obsolete technologies of industrial production and ageing infrastructure of most industries;
- A sharp increase in the motor vehicle fleet and related environmental concerns (in large cities, motor vehicles account for up to 90 percent of hazardous emissions, and approximately 38 mln people are exposed to excessive noise from transport);
- The growing quantity of untreated wastewater effluents and air emissions (*e.g.* in 2004, only 10.6 percent of the total volume of wastewater were treated to levels that respected the regulatory requirements) resulting from the overloading or lack of treatment plants;
- An increased generation of industrial and municipal waste (for example, waste accounts for 80 percent of extracted ores).

Also, many systemic problems hinder environmental management in Russia, such as low priority of environmental issues on the political agenda, at all levels of governance; the high share of the shadow economy in the use of natural resources; and poor business management.

The population has been increasingly concerned about the growing level of environmental pollution. According to opinion polls, more than 83 percent of the country's adult population are concerned about the environmental situation; more than 55 percent of respondents assess the environmental situation in their places of residence as "unfavourable", "poor", or "critical". Economic losses from illegal use of natural resources and environmental pollution are also high.

Clearer understanding of environmental conditions and pressures imposed a certain shift away from the vagueness of environmental policy making. This shift was marked by the Environmental Doctrine of 2002 that identifies specific policy objectives, such as:

- Eradication of past pollution "hot spots" and promotion of environmentally-friendly territorial planning;
- Reduction in the resource and energy intensity of production, as well as a "greening" of the economy, with a view to increasing the competitiveness of Russia's output in the global market;
- Biodiversity conservation and rehabilitation of distressed territories.

The following policy interventions are highlighted by the Doctrine:

- Reforming the system of environmental quality standards and emission limit values (ELV) and improving the procedures of environmental assessment of business;
- Phasing in process standards (best available techniques);
- Developing tools for environmental zoning;
- Providing economic incentives to improve the environmental performance of industries;
- Developing an efficient system of financial penalties for environmental non-compliance;

- Securing and efficiently using public finance for environmental projects.

The 2006 Programme of Socio-Economic Development of the Russian Federation for the medium-term (2006-2008) includes the following priorities in the field of environmental protection:

- Reform of environmental regulation (legal basis for protected areas, environmental quality standards, permitting system, environmental impact assessment, compliance, fines, support for projects, mechanisms to promote resource efficiency and use of renewable energy);
- Management of industrial waste;
- Clean-up of contaminated land;
- Introduction of economic instruments (including damage compensation).

Providing public finance to address past pollution and implement investment projects with a significant environmental component is regarded as one measure to give impetus to implementation of the Doctrine. The 2006 Programme puts a stronger emphasis on the development of economic instruments.

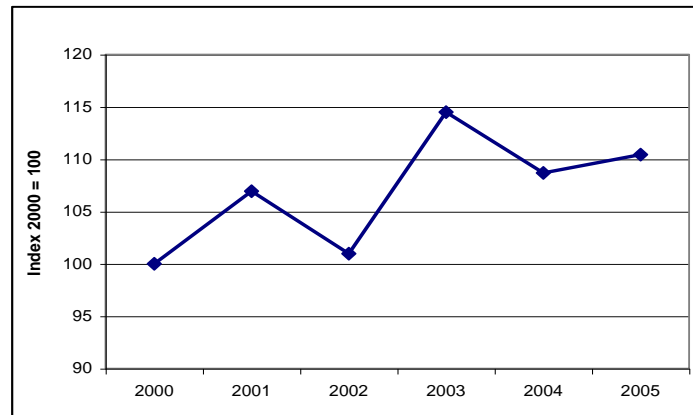
Trends in environmental expenditure in Russia

This section covers data on environmentally related commitments and, to the extent possible, data on environmental protection expenditure, defined accordingly to the internationally agreed classifications (the method used is presented in annex 1). The performance of Russia is analysed in the context of the Eastern Europe, Caucasus and Central Asia region (EECCA) and compared with selected CEE and OECD countries.

Total environmental protection expenditure

Figure 1 shows that total environmental protection expenditure has, at least slightly, increased, in constant terms, in Russia. In 2005, environmental protection expenditure amounted to 5,666 million USD in the Russian Federation (compared with 3,750 million USD in Poland). Over the 2000-05 period, the trend has been positive but erratic.

Figure 1. Total environmental protection expenditure in the Russian Federation, 2000-05, index 2000 = 100



Note Based on constant roubles (2003 prices)

Source : National statistics

Environmental protection expenditure as a share of GDP

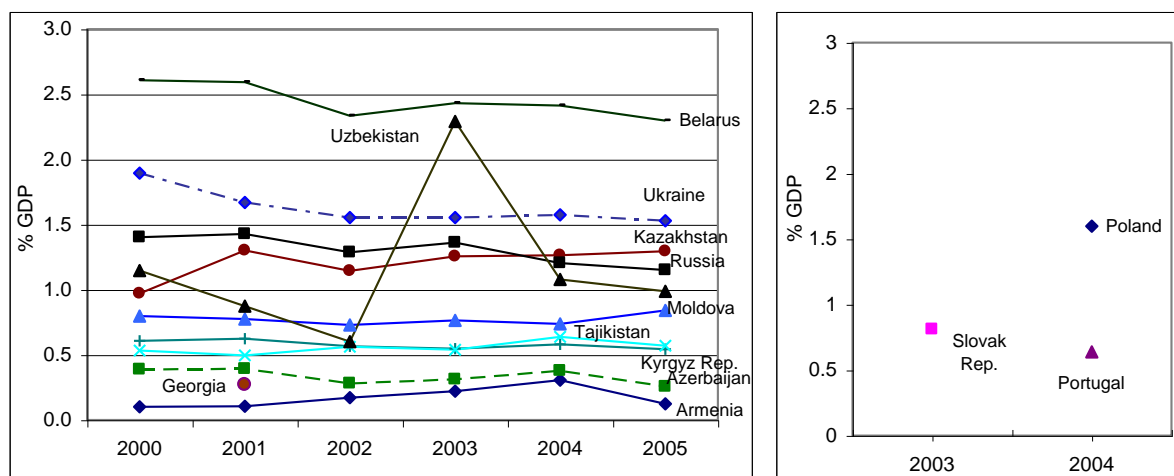
The ratio of environmental expenditure to GDP indicates the share of income that a country is willing to devote to environment protection. As can be seen on Figure 2 below, this ratio varies significantly among countries in EECCA.

A majority of EECCA countries allocate between 0.5 and 1.5% of their GDP to environmental protection. This compares with CEE countries: the Slovak Republic and Poland spend 0.8% and 1.6% of their respective GDP on environment protection.

The ratio has decreased in the Russian Federation, and Ukraine; note that in 1997, the Russian ratio was 1.7 per cent. This shows that environment protection has not fully benefited from the solid economic growth.

Russia spends approximately 40 USD per person and per year for environment protection. This is low in absolute terms; this is low in relative terms as well: it is lower than the amount spent to protect the environment in the Slovak Republic (about 50 USD), and about half what was spent in Poland in 2004 (about 100 USD).

Figure 2. Environmental protection expenditure as a share of GDP, 2000-05



Notes: Preliminary data. Comparisons amongst countries should be undertaken with care as definitions and sector coverage vary across countries. Data for Georgia refer to 2001 only

Source : National statistics, OECD

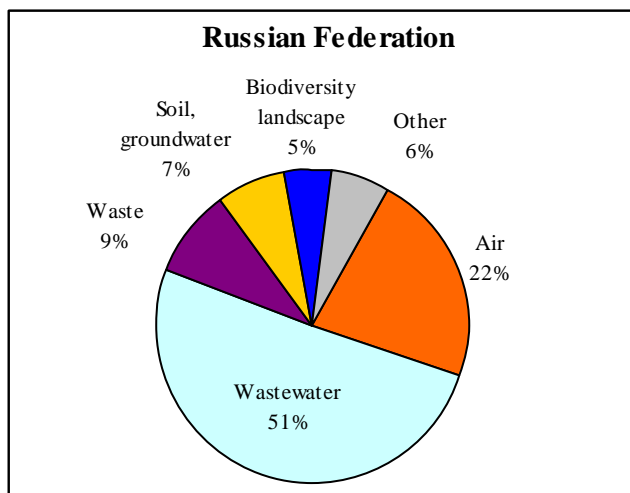
Environmental protection expenditure by domain

The distribution of environmental expenditure by domain (see Figure 3) indicates that wastewater represents the lion's share of environmental expenditure in Russia, as in all EECCA countries (with the notable exception of Kazakhstan and Tajikistan). However, the picture is blurred because, in many countries, the split between wastewater and water supply is not clear cut and the data reported under wastewater also includes water supply.

Air is the second largest domain receiving expenditure in Russia. Other environmental domains attract little attention. Money spent on policy-making and regulatory functions has marginally increased over the 2002-2005 period, as a share of GDP (from 0.16 to 0.17 per cent) and as a share of public expenditure (from 0.4 to 0.5 per cent); this suggests that the effort of central government has remained constant and that the efficiency of the federal administration has somehow increased over the period (data from OECD, 2007a).

The split has been fairly stable since 1997: at that time, water supply and wastewater amounted to 65 per cent of the total, air 21 per cent, and waste (including expenditure on improving contaminated sites) 10 per cent; the relative weakness of expenditures in the waste sector is directly linked to regulation and lax enforcement.

Figure 3. Environmental protection expenditure by domain, percentage share, 2005

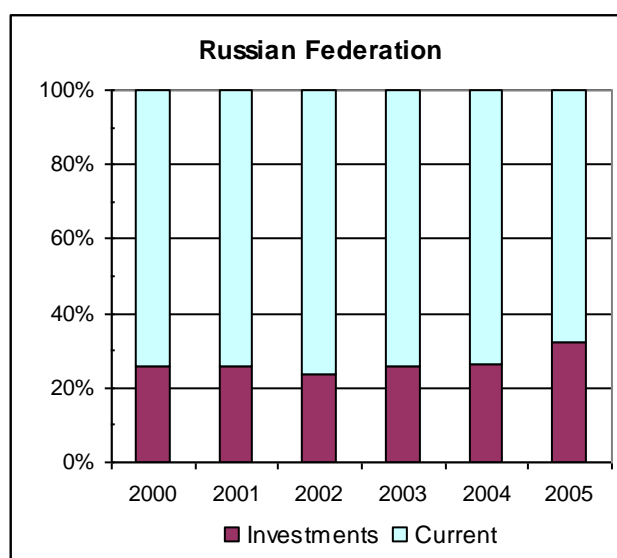


Source : National statistics

Environmental protection expenditure by type of expenditure

In Figure 4, environmental protection expenditure is split between investment and current expenditure. In the Russian Federation, the share of investment is lower than in Poland and the Slovak Republic (around 30%, compared to some 40% in CEE countries). The performance of the Russian Federation has been improving since 2002 and investments made 32% of total environmental protection expenditure in 2005.

Figure 4. Share of current and investment expenditure in total environmental protection expenditure, 2000-05



Source : National statistics

Environmental investment by domain and by economic sector

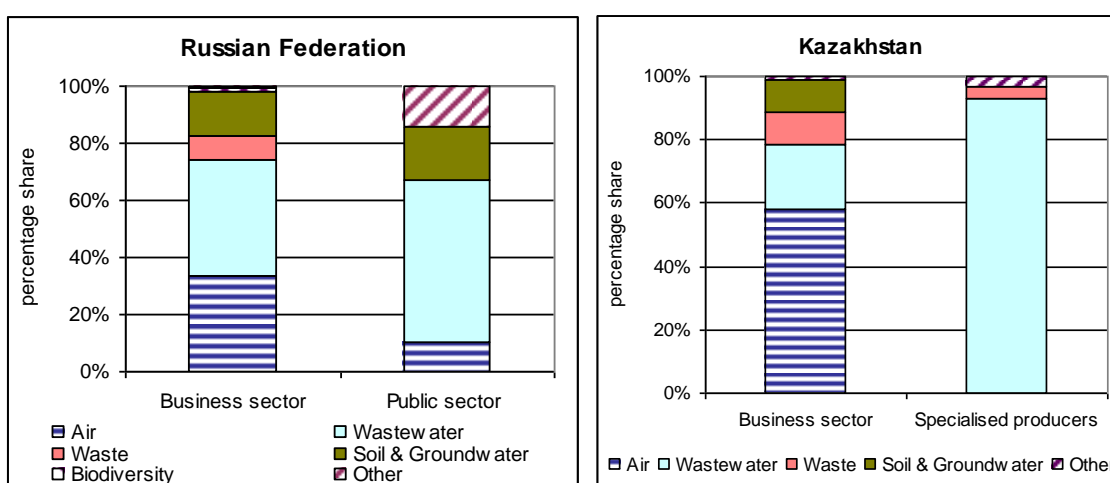
Figure 5 compares, for each country, the profile of public and private investment by environmental domain. It indicates that the public and the private sectors do not put their money in the same domain: the public sector allocates most of its investments to wastewater, whereas the private sector has a more balanced approach: wastewater and air attract a significant share of the private investment for environment protection. This is atypical in EECCA, where the private sector essentially invests on air pollution abatement, as the case of Kazakhstan indicates.

In the Russian Federation, as in Kazakhstan, the business sector has a more balanced approach.

In Russia, the public sector accounts for 80% of environmental protection expenditure; this is so because expenditure made by specialised service producers (which include a number of municipal utilities) have been reported with those of the public sector, and because the private sector has not reported current expenditure.

In 1997, it was argued that industry was the main source of financing for environmental investment in Russia; its share amounted to some 60% of the total (OECD, 1999). This was even more so at the turn of the century (85% in 2000, when the central budget was most severely constrained for macro-economic reasons), but the trend is slowly reversing: the private sector represented 73% of total environmental investment in 2005.

Figure 5. Environmental protection investments, by domain and by economic sector, per country, average 2000-05

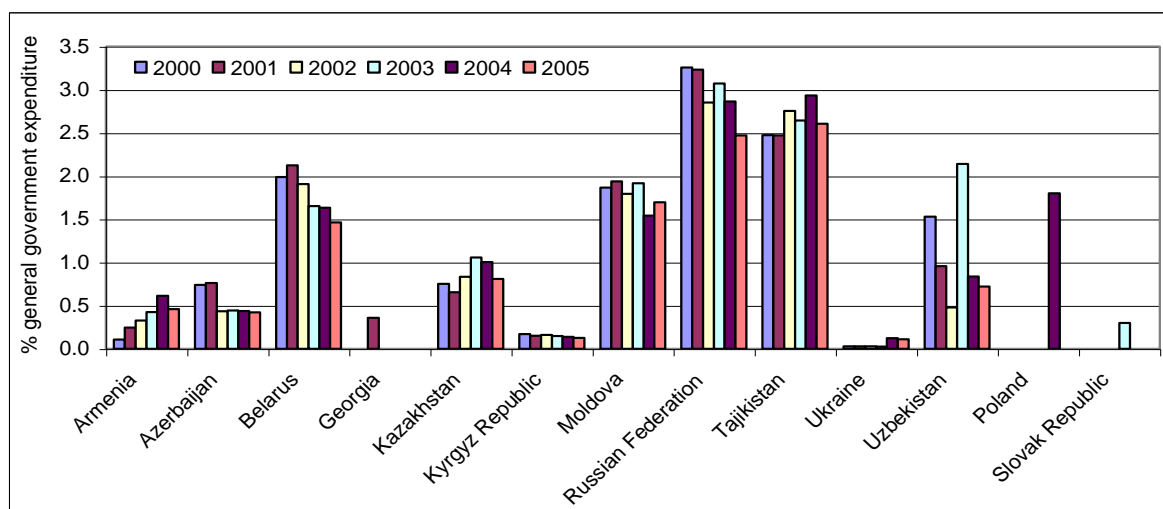


Notes: Comparisons amongst countries should be undertaken with care as definitions and sector coverage vary across countries.

Source: National statistics.

Figure 6 measures the share of government expenditure devoted to environmental protection. Data are available for central governments only. The ratio decreases in Russia over the period 2000-05.

Figure 6. Environmental protection expenditure in the public sector as a share of general government expenditure, 2000-05

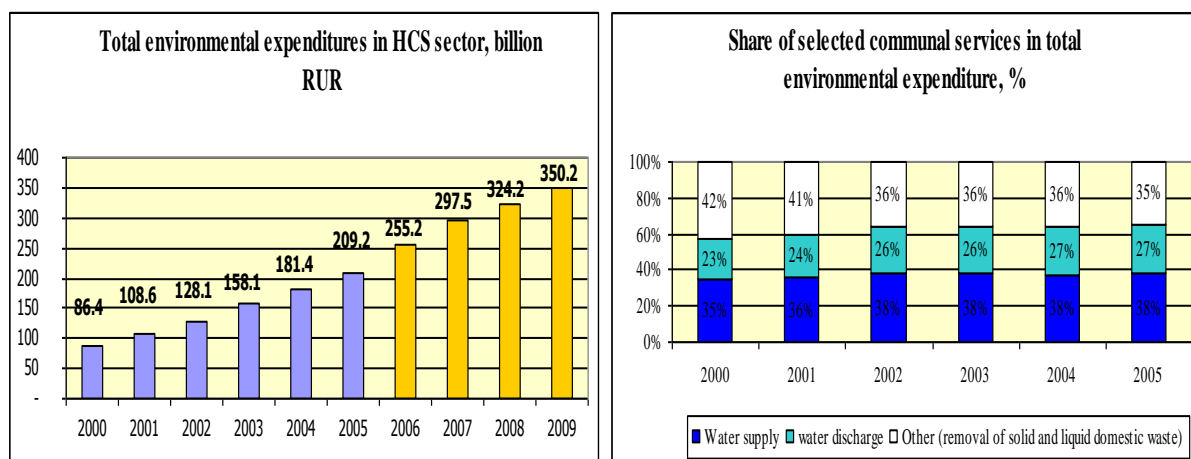


Note: Preliminary data. Comparisons amongst countries should be undertaken with care as definitions and sector coverage vary across countries

Source : National statistics

Complementary data on expenditure from housing and communal services

The Ministry of Regional Development has estimated environmental expenditures from the housing and communal services for water supply, wastewater collection and treatment and other services (removal of solid and liquid domestic waste). These data could not be reconciled with the ones collected by Federal Service for State Statistics, and therefore are presented separately.



Source: Ministry of Regional Development.

The housing and communal services are considered as the biggest polluters in Russia (although they do not produce hazardous waste). These services collect wastewater and waste from households

and from other organisations. In smaller settlements, the share of each category in the origin of waste is difficult to measure.

For 2000-2005, the data comes from the statistical report “Form 22-zhkkh (compound)”. For 2006-2009, the forecast is based on the maximum growth rates set by the Russian Government for tariffs for communal services; growth rates are based on assumptions on collection rate (which is expected to rise, in particular as regards the business community) and the extension of service coverage.

The expenditures are calculated based on total cost of relevant utilities for water supply, wastewater collection and treatment and other services (removal of solid and liquid domestic waste), *minus* the depreciation cost. They are partially financed by revenues from the services. There are limitations to tariffs levels for water-related services and to the total amount of the water bill. It is estimated that households pay some 10% of the total cost. So, there is cross-subsidisation, essentially by industries.

Other sources of finance for housing and communal services include budget support and support from donors and IFIs.

Synthesis: opportunities lost?

A huge backlog and rapid growth in resource intensive sectors have generated severe environmental challenges in Russia (e.g. ambient pollution), the consequences of which are apparent (e.g. on health and mortality).

The Environment Doctrine, which dates back to 2002, identifies objectives related to past pollution hot spots, resource intensity, and biodiversity conservation/rehabilitation. Economic instruments are increasingly emphasised as a source of finance to support this Doctrine (e.g. in the Programme of Socio-Economic Development of the Russian Federation for the medium-term 2006-2008), along with more traditional public finance instruments.

In this context, the various streams of data indicate that environment protection expenditure has not fully benefitted from the robust economic growth of Russian economy since the turn of the century. Environment protection expenditure, as a share of GDP or of general government expenditure, has declined since 2000.

The level of environment protection expenditure remains low (some 40 USD per person per year; less than in the Slovak Republic); half of it is spent on wastewater and about one third is dedicated to investment.

INSTRUMENTS TO FINANCE ENVIRONMENTAL POLICIES IN RUSSIA

This chapter presents the status of a number of instruments used to finance environmental expenditure in Russia. The focus is on water supply and sanitation. Innovative mechanisms such as local capital markets) are promising, but underdeveloped, whereas more traditional ones (tariffs, intergovernmental transfers) could be adjusted to better fit the needs of efficient environmental policies. This is particularly the case when it comes to financing investment in environmental infrastructures (water, sanitation, waste).

Revenues from economic instruments

The economic instruments most commonly used for environmental policies in Russia are: environmental charges and taxes covering a very large number of air and water pollutants, plus solid waste generation, as well as fines for environmental offences and claims for environmental damage. Product taxes and deposit-refund systems, accelerated depreciation of assets, etc. are not commonly used in Russia. If one excludes natural resources use fees, pollution charges are at the core of the economic instruments. User fees and pollution charges constituted 18% of revenues of the federal budget in 2005, of which almost 87% came from mineral resources fees.

Pollution charges in Russia are levied universally on all “nature users” (legal or natural persons) that are subject to environmental permits. They are imposed for 214 air pollutants and 197 water pollutants, as well as on “placement” (storage and disposal) of four categories of hazardous waste (based on toxicity) and two categories of non-toxic solid waste. Among mobile sources, enterprise-owned transport vehicles are charged for air pollution. Private cars, the biggest contributors to air pollution in urban areas, are excluded from the system. The distribution scheme of revenues from pollution charges has been adjusted by the Federal Law of 20 August 2004 No. 120-FZ, 20 percent of the total revenue is transferred to the federal budget; 40 percent, to the regional budget; and 40 percent, to the local budget (effective 1 January 2006).

Introduced in the early 1990s, the charge rates were set at the level that was believed sufficient to compensate for the economic damage resulting from environmental pollution (polluter-pays principle). The estimates were made for a few pollutants and extrapolated for the rest of the regulated pollutants by using “conventional tonnes”. Payments are assessed based on the rates set per unit of pollutant. The methodology to calculate pollution charges is set in Government Ordinance No. 632 of 28.08.1992. The base rates were set in Government Decree No. 344 of 12 June 2003; they were amended by Government Ordinance No. 410 of 01.07.2005 .

A central feature of the pollution charge system is that a set of pollutant-specific basic rates apply to discharges within established ELVs, whereas a much higher rate applies to discharges exceeding the limits. The applicable rate of pollution charges is 5 times the base rate for quantities discharged in excess of the ELV but within the temporary limit. For discharges in excess of the temporary limit (or those without a permit), the applicable rate is 25 times the base rate (Table 1). These multipliers represent the “non-compliance component” of the pollution charge. Thus, pollution charges are used as an administrative tool to bring polluters into compliance or to undergo permitting procedures in a timely manner.

Table 1. Calculation principles and sources of pollution charge payments

Pollution Level	Charge calculation	Source
ELV	Base rate (N)	Production costs
Temporary ELV	5 x N	Profit
In excess of temporary ELV	25 x N	

In 2000, the revenue collection responsibility was transferred from the environmental to the federal tax authorities that had a positive impact on the collection rate. As of 2004, the enforcement of pollution charges was assigned to the newly-created Federal Environmental, Industrial, and Nuclear Supervision Service (*Rostekhnadzor*), which has the task of detecting non-payers more thoroughly and imposing penalties on them.

The Russian environment authorities have been reluctant to reform the system of pollution charges, as it provides them with a small but steady source of revenue that they are afraid to lose once the number of parameters subject to pollution charges is reduced.

Some of the economic instruments provided for by the Russian legislation are still used to a very limited extent. For example, the Tax Code of the RF (Art. 67) provides investment tax credit for environmental research and development. In practice, tax benefits are virtually not utilized because there is no clear mechanism for their application. Higher rates of depreciation for environmental assets were provided for by the Law “On Protection of Natural Environment” of 1996 (Art. 24); however, current Law “On Environmental Protection” does not provide for accelerated depreciation of wastewater treatment plants or other environmental protection facilities.

User charges for water supply and sanitation

Institutional framework

Under the Soviet system, municipal enterprises providing communal services operated on a cost-reimbursable basis, a variation of a “rate-of-return” regulation². Investments were funded separately. They were not estimated according to investment plans, but as a rate of return on operating expenses. In addition, certain types of expenses, such as extra contributions to the employee funds for vacations or training, were covered by investments. The rate of return is set by municipal officials as a percentage of operating expenses.

These Soviet accounting rules are still in force and have a profound impact on the operations of utilities. Utilities are forced to include most investment spending in amortization and maintenance expenditures, as the share of profits that can be used for investment is strictly limited, as is the maximum profit rate.

² The following analysis is the summary of findings of analytical report “Practice of housing and communal sector reforms” The Institute for urban economics, Moscow, 2003.

The regulation of tariffs for communal services for Russian households differs from the standard western tariff regulation of utility monopolies in three important ways:

- The tariff may include not only the tariff for the services of the utility, but also the cost of works and services of other organizations engaged in the service delivery (in case of water supply, the cost of maintaining internal building nets, water meters in buildings or apartments, etc.).
- The tariff for services to the households may cover only a portion of the cost of service delivery, with the remainder covered by other sources: the public budget (subsidies for the difference between full costs and the tariffs) and/or higher tariffs for other consumers (cross-subsidies).
- Tariffs for the households typically regulate not just the cost of the service, but also a normative volume of service consumption when metering equipment is unavailable; thus the payment for the service equals the value of the regulated tariff multiplied by the regulated normative consumption rate. Metering for residential use of water and district heating, even at the building level, is extremely rare.

In the first days of the transition, the federal government transferred to municipalities the ownership of state housing (mostly of state enterprises), municipal housing, and utility assets associated with them. In practice this meant that municipalities became the owners of the great majority of district heating and WSS enterprises.

In 2001, a regulation was issued which actually addressed tariff setting at the municipal level³. For the first time, it declared the need for developing procedures linking tariff regulation at the municipal and regional levels, and established that the tariff structure should correspond to the system of contractual relations in the housing and communal service sector.

At the end of 2002, the determination of tariffs for municipal communal services was influenced by the federal, regional, and municipal levels of government, because the production of these services involves inputs that have prices regulated by the federal and regional authorities. The effective legislation assigns each level its own regulatory powers.

This generates opportunities for multiple overlapping authorities. Prominent among these is that the competent regulatory agency in the area of water supply depends on the legal form of the operating company. Private entities are regulated at the regional level even if they provide services only within a municipality. This creates serious, sometimes irresolvable, problems in attracting private businesses for management of municipal communal infrastructure.

The existing legislation does give some direction to the tariff-setting process by stating that municipalities should establish rates and tariffs for the housing and communal services (except tariffs for electricity and gas) *and* implement cost-reduction measures based on expert examination of the

³ RF Government Resolution No. 797 of November 17, 2001, *On the Subprogram "Reform and Modernization of the Housing and Communal Service Complex in the Russian Federation" of the Federal Targeted Program "Zhilishche" for 2002–2010*.

tariffs for goods, works, and services. The decision to review the rates and tariffs for the housing and communal services should be preceded by such an expert examination⁴.

This statement and the assignment of tariff-setting authority to local governments constitute the entire legislative base.

In addition to these laws and regulations, three methodological documents have been issued by the national government:

- Methods for planning, counting and calculating the self-cost of the housing and communal services (hereinafter – Methods)
- Guidelines for forming economically justified tariffs for the housing and communal services (hereinafter – Guidelines)
- Methodological recommendations on the financial substantiation of the prices for water and sewerage (hereinafter – Methodological Recommendations for Water).

The first two comprehensive documents are based on the concept of an economically justified tariff for a housing or communal service (hereinafter EJT), which is understood as a fee charged for maintenance or repairs of housing (including capital repairs), or to cover the costs of the provision of a sustainable service in compliance with the service quality standards. The EJT entails the identification of the production cost, and the profit required for normal reproduction of the service. It is recommended to calculate expenditures based on normative indicators that adjust current costs to make them more realistic, rather than on the actual data for the preceding period.

The Methodological Recommendations for Water pursue similar goals, defining cost based on the adopted production and investment programs, effective norms and standards for material, labour, and financial costs, with regard to the data reported by the organization for the preceding period. The price of a unit of service is defined as a fraction of the sum of costs and the planned production volume.

These methods presume normative cost-accounting. On the one hand, this approach is appropriate for production processes involving similar or recurring operations, such as water supply, wastewater collection. On the other hand, this approach imposes very high requirements to the definition of standards which should take into account the current state of fixed assets, technologies, organizational arrangements and qualification of staff. Moreover, the standards-setting process is not just a determination of values, but an instrument of motivation. In other words, the standards are designed as incentives for cost reduction, labor efficiency and product quality, etc. However, experience proves that the existing standards fail to meet these targets.

⁴ RF Government Resolution No. 707 as of June 18, 1996, *On Reorganizing the System of Payments for Housing and Communal Services*.

Recent trends⁵

Over 2000-05, the tariff for population on water supply and sanitation services increased more than 5-fold, reaching \$0.26 by the results of 2005. The growth of tariffs for water supply services was stipulated by growing expenditures of enterprises which provide such services; however, the tariff for population was more influenced by the reduction of cross subsidies. According to the results of 2000, the economically justified tariff for water supply services in Russian in general was \$0.09 per cubic metre of water; however, the Russian population paid on the average a little over half of this cost (\$0.05 per cubic metre of water).

A significantly lower tariff for population, compared to the level of the economically justified tariff on all types of housing and communal services, existed in Russia since the Soviet period and was viewed as a measure of social protection of people. Underpayment by population was compensated for by budgetary subsidies provided to enterprises which provided these services, as well as by increased tariff for communal resources for commercial users. In particular, commercial users paid 2 times more for one cubic metre of water than the economically justified tariff, and it was 3.5 times higher than tariff for population. A similar disproportion was seen in the tariff for wastewater collection services: whereas the economically justified tariff was \$0.07, the tariff for population by the results of 2000 was on average \$0.04 for the country in general, while commercial users paid the tariff of \$0.14.

Over the period of analysis, the ratio between the tariff for population and the economically justified tariff increased significantly: while in 2000 population paid on average 52% of the water cost, then by the results of 2005 the tariff for population reached 87% of the economically justified tariff. As regards wastewater collection services, from 2000 to 2005 the ratio between the tariff for population and the economically justified tariff increased from 53% to 86%.

Positive consequences of decreased cross subsidies are even more obvious at the regional level. Thus, by the results of 2000, in 25 regions of Russia the tariff for commercial users for water supply services was more than 5 times higher than the tariff for population, whereas the maximum difference in this indicator was 13.8 times (Belgorod Oblast). Only in 7 regions the value of this indicator did not exceed 2-fold; in 28 regions tariffs for commercial users were 2-3 times higher than tariffs for population, and in 26 regions this difference was 3-5 times. A similar situation prevailed in wastewater collection services: in 35 regions tariffs for commercial users exceeded more than 5 times tariffs for population; in 23 regions this difference was 3-5 times. The maximum level of this indicator in 2000 was 24.1 times for wastewater collection services (Kamchatka Oblast).

By the beginning of 2006, in 6 regions tariffs on water supply services for population and commercial users were made identical, i.e., according to the economically justified tariff; as regards wastewater collection services, the identical tariffs were introduced in 7 regions. The number of regions where tariffs for commercial users exceeded tariffs for population not more than 2 times, increased, compared to 2000, from 7 to 56 for water supply services and from 7 to 54 for wastewater collection services. Only in 4 regions tariffs for commercial users on water supply services exceeded more than 3 times tariffs for population; as regards wastewater collection services, the number of such regions was 9.

⁵ This section builds on the report Monitoring of the System of Water Supply and Wastewater in the Russian Federation, OECD, 2007b

Conclusion

Practically all methodological recommendations reduce tariff calculation to a cost function, paying lip service to the development goals of the regulated enterprises.

These recommendations say nothing about a system of tariff regulation at the municipal level, tariff regulation procedures, etc. While they are not binding for local governments, they have gained broad acceptance because of the opportunity they offer to fill the regulatory vacuum.

This weak legislative and methodological basis for municipalities results in poor tariff policies. Indeed, tariff regulation practices in Russian municipalities suffer from the following problems⁶:

1. Almost universally, decisions by regulators are a belated response to changes in the environment of service provision, such as general inflation or increased power tariffs.
2. Tariffs are, as a rule, determined as “costs plus profitability.” This system is not an incentive to reduce costs.
3. Tariffs are set without taking into account investment needs of utilities. Several vital expenditure items (e.g., extension or modernization of fixed assets) may be financed from “profit”, repair funds and amortisation. Since profit is determined as a specified percentage of self-cost, it often turns out to be insufficient to finance investment, and sustainable operation.
4. The majority of municipalities lack formal tariff regulation procedures. There is no formal definition of the reasons for which a tariff may be reviewed. Tariff review processes are opaque; they do not provide for the participation of all interested parties; they are not designed to reconcile the needs of the enterprise and the capacity-to-pay of consumers.
5. Tariffs tend to be used to serve the political objectives of the local administrations. As a result of populist decisions, municipal utilities are deprived of the financial resources they need for normal operations, which leads to depreciated fixed assets and reduced service quality.

The new law “On general principles of local self-governance in Russian Federation” has devolved tariff regulation for MUEs in WSS sector to local Dumas. This has generated additional political risks, as Duma delegates are prone to take political, rather than economic, decisions.

⁶ This list was initially prepared by experts at the Institute for Urban Economics in Analytical report “Practice of housing and communal sector reforms” The Institute for urban economics, Moscow, 2003. It is highly consistent with World Bank observations. See in particular, World Bank. 2000. “Project Appraisal Document: Russian Federation, Municipal Heating Project.” Report 21153–RU. Washington, D.C.: World Bank; World Bank. 2001. “Project Appraisal Document: Russian Federation, Municipal Water and Wastewater Project.” Report 21416–RU. Washington, D.C.: World Bank; and Frenkman, L. 1998. “Russian Federation: Housing and Utility Services—Policy Priorities for the Next Stage of Reform.” Report 17483-RU. Washington, D.C.: World Bank.

Environmental funds

The process of formation of environmental funds across Russia started in the late 80-ies as an attempt to create one more self-sustaining public source of environmental finance. Funds were initially established as off-budget public institutions at federal, republican, regional or local levels, capitalized by ear-marked revenue of charges for pollution and fines for non-compliance with environmental regulations. Their status and revenue sources had very ambiguous legal basis. Some of them were independent legal persons (e.g. the Federal Fund and some regional funds), while others could not be distinguished from the environmental departments of the Oblast administration.

Environmental Funds in Russia have been established without clear spending programs. In the law their objectives and mandates were ambiguous.

The Federal Environmental Fund of Russia was abolished on 1 July 2002. The status of the regional and local funds is still not very clear. Most local funds have been abolished too, while most of the Oblast funds the funds of the autonomous republics of Russia have survived. Those which did, have been fully consolidated into the regional budgets and are now earmarked budgetary funds.

The inadequate legislation ruling the performance of environmental funds failed to define who and what types of projects were eligible for financing, or how to coordinate activities of funds at different levels of government.

Environmental funds have never become significant players in financing environmental expenditure in Russia. The volume of resources available to these Funds were typically very small. The Funds have often provided important financial support to environmental administrations affected by frequent budget cuts, but their role in financing environmental investments remained negligible. The total revenue of environmental funds at all levels of government was equal to 6% or 17% of the value of environmental investments implemented in the country in 1997 (depending on the source of data) (OECD 1999; Goskomekologia 1997). In fact, the share of the funds in financing these investments was much smaller because typically most of the Russian funds revenue (up to 75%) consisted of money surrogates, barter and pollution charge offsets. Only Federal Fund was prohibited from using non-monetary transactions and was receiving up to 20 million USD annual revenues in the peak years.

Environmental funds at all levels suffered seriously from the lack of accountability, transparency and managerial efficiency. Most regional and local Funds were not financing institutions as they are mainly focused on revenue collection from pollution charges/fines and direct public procurement on behalf of the government, instead of project appraisal and financing.

The main operations of remaining environmental funds in Russia include ecological monitoring, pollution control and educational programs. Budgetary ecological funds usually have legal status of a Municipal Unitary Enterprise. Their activities in water and wastewater sector are usually financed through collection of water tax from the water companies.

Several private ecological funds not only carry out the same functions, but also involve themselves in financing ecological investment projects such as construction of wastewater plants⁷. Private ecological funds rely on dividends, interest on deposits including bank deposits, share in the

⁷ For example of private environmental fund see Water Eurasia on www.we.ur.ru. For example of public environmental fund, see MUE “Volgograd ecological fund” on <http://volg.ecoinfo.ru/htmls/Efv/efv0.htm>

profit earned in the result of use of the fund's property by manufacturing companies or other businesses currency proceeds from foreign legal entities and grants from private companies.

Russian environmental funds, both public and private, have been financing environmental infrastructure projects for the last decade. However, their share remained small, and they usually provide expert advice, consultancy and oversight, rather than investing their own resources.

Russian environmental funds support their targeted investment activities through grants (most often – public environmental funds) and/or through loans (private). However most of the time, environmental funds provide their expert advice and consultations, rather than direct investments.

Municipalities usually have the ability to request finance from public environmental funds, but these resources are earmarked for environmental projects. Environmental funds always participate in the project in which their funds were invested.

Though, conceptually, environmental funds were designed to become an autonomous source of environmental finance in addition to budgetary and producer's own environmental investments, today, due to the scarcity of budgetary resources and legal constraints, they became actually the only source of environmental finance for municipalities, which also use them to support municipal nature protection services. Local environmental funds were mostly used for making grants to public manufacturing companies and utilities.

Intergovernmental transfers for environmental infrastructures

From a central government perspective, intergovernmental transfers are instruments that the central government can use to improve the performance and control of sub-national public expenditure, and to create incentives for better coherence between national and local public policies.

Surveys in OECD countries confirm that the impact of intergovernmental grants on efficiency, fiscal discipline, and equity, largely depends on their design. The design varies significantly from one country to another, and is strongly influenced by policy objectives and the institutional context. Important lessons have been learnt from European Union accession countries where intergovernmental transfers are a key dimension of relations between levels of government and a major source of finance for local jurisdictions.

Russia, as most countries in EECCA, has engaged in a systematic devolution of responsibilities for the construction and maintenance of urban environmental infrastructure to sub-national levels of government. As owners of the communal service infrastructure, municipalities are responsible for its rehabilitation, modernisation, and development. Now, devolution of responsibilities needs to be matched by ensuring access to the financial resources needed to implement the new mandates assigned to local and regional jurisdictions.

As Russian municipalities are still largely dependent on fiscal transfers from central or regional budgets, they often have to co-ordinate their infrastructure development plans and capital expenditure budgets with national/regional plans and budgets. This makes strategic planning and investment at local level dependant on the policies at the higher level, and generates a risk that local investment plans will not be implemented due to budgetary constraints at other levels of government.

Legislative and regulatory framework governing intergovernmental transfers

Intergovernmental relations in the Russian Federation have a two-level structure: relations between the federal and sub federal governments, and relations between sub federal and local governments. This implies that financial support from the federal budget flows only to sub federal budgets, and local budgets obtain support directly from sub federal budgets.

Intergovernmental fiscal relations in the Russian Federation were restructured in the years 1999-2001, in accordance with the Reform Concept approved by the Russian Government (RF Government Resolution #862 of July 30, 1998). This resulted in a new system of financial support from the federal government to sub federal authorities. The Fiscal Federalism Development Programme for 2001-05 followed the budget reform (RF Government Resolution #584 of August 15, 2001). This Programme was designed to improve mechanisms of the federal financial support of sub federal governments, and has been successfully implemented.

Today the fiscal relations between the federal and sub federal governments are defined by the following essential attributes:

- Financial aid to sub federal governments is divided into two types - ongoing operating support and capital investments - serving different purposes;
- Financial support of the federal government is provided in the form of grants (defined as transfer of funds from one jurisdiction to a government of another level made in a non-repayable manner; RF BC, Article 6), subventions (defined as transfer of funds from a jurisdiction to another level of government or a legal entity made in a non-repayable manner and on a grant basis to cover target-specific costs; RF BC, Article 6), subsidies (transfer of funds from a jurisdiction to another level of government or a natural or legal entity subject to the *target cost sharing principle*; RF BC, Article 6) and other non-repayable transfers, plus budgetary loans;
- The bulk of financial assistance is allocated in accordance with procedures based on testable (reproducible) calculation formulas and objective assessment of the budgetary situation of regions, or under predetermined competitive selection rules and regulations. Budget expenditure and tax revenue statistics are no longer used for the assessment of the budgetary situation of a region, as it has been a strong disincentive for regional governments to improve their taxation base and budget performance;
- Grants from the Federal Financial Support Fund for Federation Subjects are allocated under procedures approved by the Russian Government⁸;
- General principles and standard modes and mechanisms of equalization of budgetary situation of local governments are established by the RF BC;
- Guidelines for regulation of their budgetary intercourse⁹ are provided to regional governments and municipalities by the Ministry of Finance.

⁸ RF Government Resolution “*On Appropriation of Grants from the Federal Financial Support Fund for Federation Subjects*”, #670 of November 22, 2004

⁹ RF Ministry of Finance “*On Guidelines for Regulation of Budgetary Intercourse between Subfederal Governments and Municipalities*”, # 243 of August 27, 2004

The system of intergovernmental transfers

As shown in Table 2, federal transfers to regional governments have continuously made up a stable share in the total expenditure of the federal government (averaging at 15 percent for three years), over the 2002–04 period.

Table 2. Federal transfers to Regional Governments in the Total Expenditure of the Federal Government, million USD

	2002		2003		2004	
Federal budget expenditure, total	62,096	100.0	78,706	100.0	96,087	100.0
including: transfers to other-level budgets	9,411	15.2	12,315	15.6	13,658	14.2

Source: Federal budget laws of the Russian Federation passed in 2002-200

Regional governments receive financial support from five various support funds, revised annually as part of the federal budget:

- Federal Financial Support Fund for Federation Subjects,
- Compensation Fund,
- Social Expenditure Co-Finance Fund,
- Regional Finance Reform Fund,
- Regional Development Fund.

In addition, two instruments can provide federal assistance to regional initiatives:

1. Federal targeted programmes¹⁰. These are a group of research, development, production, socioeconomic, business management and other actions meant to ensure efficient solution of systematic problems in state, economic, environmental, social and cultural development of the Russian Federation;
2. State capital investments into construction, modernization and retrofitting of regionally- and municipally-owned public property, as part of the Federal Targeted Investment Programme (FTIP). State capital investments are a most significant component of the federal budget expenditure related to implementation of federal targeted programmes.

Each year, these funds contribute to more than two third of the total financial aid the federal government provide to regions (See Table 3).

¹⁰ apart from federal targeted regional development programmes (FTRDP) regional governments are engaged in implementation of a variety of other federal programmes (for example, such programmes as *Housing, Children of Russia, Senior Generation, Ecology and Natural Resources of Russia, Russian Culture*, etc.) This component also includes *research and development costs and other expenses* due to implementation of federal targeted programmes. *Capital expenditure* of federal targeted programmes are covered by the Federal Targeted Investment Programme

Table 3. Structure of Federal Financial Assistance to subjects of the Russian Federation, million USD

Federal financial assistance		2002		2003		2004	
		m USD	percent	m USD	percent	m USD	percent
Financial support provided to other-level budgets, total		9,411.2	100.0	12,315.7	100.0	13,658.5	100.0
<i>Including:</i>							
1	Financial Support Fund for Federation Subjects, total	4,703.0	50.0	5,645.2	45.8	6,102.8	44.7
	<i>including:</i>						
	<i>equalizing transfers</i>	4,334.3	46.1	5,273.3	42.8	5,732.3	42.0
2	Compensation Fund	1,299.6	13.8	1,545.6	12.5	1,951.2	14.3
3	Social Expenditure Co-Finance Fund	597.3	6.3	489.0	4.0	218.7	1.6
4	Regional Finance Reform Fund	38.3	0.4	42.4	0.3	42.2	0.3
5	Regional Development Fund	557.8	5.9	417.0	3.4	871.4	6.4
6	Other grants and subventions	772.0	8.2	1,266.6	10.3	1,702.5	12.5
7	Transfers made as part of mutual settlements	218.4	2.3	586.6	4.8	701.7	5.1
8	Road maintenance subventions and grants ¹¹	948.2	10.1	1,333.8	10.8	1,277.1	9.4
9	Regional development initiatives, total	276.6	2.9	989.6	8.0	790.9	5.8
	<i>including:</i>						
	<i>State capital investments</i>	154.9	1.6	329.9	2.7	393.8	2.9
	<i>Federal targeted programmes</i>	121.7	1.3	659.7	5.4	397.1	2.9

Source: Federal budget laws of the Russian Federation passed in 2002-2004

Mechanisms, purposes and terms of allocation of various types of federal financial aid to sub federal governments are appended (annex 2).

The structure of local budget revenues

Table 4 shows the total revenue structure of consolidated budgets of Russian regions. A regional consolidated budget comprises the budget of a regional government (Federation Subject) and budgets of local governments operating in the region.

¹¹ in 2002, subventions and grants regional governments obtained to finance the road maintenance were reported in accordance with the RF Budget Classification as "Road Facilities", although in 2003 they were already reported as "Financial Aid to Other-Level Budgets". For the comparative purposes of this report road maintenance subventions and grants provided to regions in 2002 were included into the group "Financial Aid to Other-Level Budgets"

Table 4. Revenue Structure of Russian Regional Consolidated Budgets in 2002-2004, USD million

Revenues	2002		2003		2004	
	m USD	percent	m USD	percent	m USD	percent
Revenues of regional consolidated budgets, total	51,251.3	100.0	62,930.8	100.0	82,376.7	100.0
<i>including:</i>						
Tax revenues	34,690.9	67.7	43,718.4	69.5	61,364.8	74.5
Non repayable transfers from the federal budget, total	9,764.2	19.1	12,288.8	19.5	13,430.6	16.3
<i>including:</i>						
<i>Revenue equalizing transfers</i>	4,341.3	8.5	5,273.3	8.4	5,732.0	7.0
<i>Other grants</i>	1,469.1	2.9	2,097.9	3.3	1,579.3	1.9
<i>Subventions</i>	1,815.5	3.5	2,347.3	3.7	1,832.6	2.2
<i>Subsidies</i>	1,672.7	3.3	2,197.1	3.5	3,548.9	4.3
<i>Transfers made as part of mutual settlements</i>	465.5	0.9	373.2	0.6	737.9	0.9
Other revenues ¹²	6,796.2	13.3	6,923.6	11.0	7,581.2	9.2

Source: General code of consolidated budget performance reports of Russian regional governments for 2002-2004

The revenue structure shown in Table 4 is not common to the majority of Russian regional consolidated budgets, and does not show the weight of intergovernmental transfers.

The Russian Federation consists of 89 Federation Subjects (regions). Social, economic and fiscal differences between regions (and municipalities in specific Russian regions) are important. Accordingly, the weight of federal non-repayable transfers in regional budgets vary to a large extent. For example, 18 industrially advanced regions with a comprehensive tax base and well-developed infrastructure receive no revenue equalizing transfers. In the rest of Russian regions, equalizing transfers may vary from 5 to 50 percent of budgetary revenues. It is these essential interregional differences that make the regions' subsidizing commitment of the federal government so high.

Table 5 shows the revenue structure of Russian local budgets.

¹² in Table 22 (and Table 23 as well) "other revenues" include non-tax revenues, revenues from business or other profit-making activities of budget-supported entities, revenues of special budgetary funds (road, environmental), non-repayable transfers from state extra-budgetary funds, state organizations, etc. As the specific weight of each type of the said revenues in the total revenue structure is insignificant, they are not analyzed in this report

Table 5. Revenue Structure of Russian Local Budgets in 2002-2004, USD million

Revenues	2002		2003		2004	
	m USD	per cent	m USD	per cent	m USD	per cent
Revenues of local budgets, total	22,569.0	100.0	28,406.2	100.0	36,381.3	100.0
<i>including:</i>						0.0
Tax revenues	12,086.4	53.6	14,580.9	51.3	19,075.4	52.4
Non repayable transfers from regional budgets, total	9,049.7	40.1	11,402.8	40.1	15,799.7	43.4
<i>including:</i>						
<i>Revenue equalizing transfers</i>	<i>3,074.4</i>	<i>13.6</i>	<i>4,269.2</i>	<i>15.0</i>	<i>4,318.2</i>	<i>11.9</i>
<i>Other grants</i>	<i>2,306.5</i>	<i>10.2</i>	<i>1,734.8</i>	<i>6.1</i>	<i>1,706.2</i>	<i>4.7</i>
<i>Subventions</i>	<i>2,051.2</i>	<i>9.1</i>	<i>3,114.1</i>	<i>11.0</i>	<i>6,245.8</i>	<i>17.2</i>
<i>Subsidies</i>	<i>822.6</i>	<i>3.6</i>	<i>1,282.9</i>	<i>4.5</i>	<i>2,406.1</i>	<i>6.6</i>
<i>Transfers made as part of mutual settlements</i>	<i>795.1</i>	<i>3.5</i>	<i>1,001.8</i>	<i>3.5</i>	<i>1,123.3</i>	<i>3.1</i>
Other revenues	1,432.8	6.3	2,422.5	8.5	1,506.2	4.1

Source: General code of budget performance reports of Russian local governments for 2002-2004

The analysis of the total revenue structure of Russian local budgets has demonstrated a relative stability of the proportion between tax revenues and regional non-repayable transfers over the last three years. Intergovernmental transfers account for 40 percent of local revenue budgets. The share of purpose-oriented transfers (subventions and subsidies) in the local revenue structure has increased notably since 2002. This derives essentially from favourable changes in the federal budget policy, towards a reduction of unfunded federal mandates (which for a long time have been a hindrance to fiscal relations between the federal government and regions, as well as between regions and local governments) through allocation of earmarked transfers for carrying out federal mandates devolved to sub sovereign jurisdictions (implementation of federal laws).

Because of the great variety of Russian municipalities, Table 5 can only provide a general pattern of revenues of Russian municipalities which include both cities with 1 million population, and towns with 15,000 inhabitants and budgetary resources mostly made of non-repayable transfers from upper-level jurisdictions.

State support to the WSS sector at the regional/local level

As mentioned above, the main instruments the federal state can use to support investment in regional and municipal social and engineering infrastructure development, including water supply and sanitation, include the Regional Development Fund (RDF) and the Federal Targeted Investment Programme (FTIP).

The total investment support the federal government provided to regional governments via RDF and FTIP amounted to 712.7 million USD in 2002, 746.8 million USD in 2003, and 1,265.2 million USD in 2004.

FTIP specifies the volume of state capital investments that should be made in federal targeted programmes (subprogrammes). In the context of this report, the Housing Sector Reform and Modernization subprogramme of the Housing (Zhilische) Programme approved by the Government

Resolution #797 of 11/17/2001, appears to be of particular interest. Its budget for 2002 – 2010 is 18.5 billion USD¹³, including 7.6 billion USD (41.2 percent) for modernization of WSS systems and 10.9 billion USD (58.8 percent) for modernization of heating supply systems.

Basically, this subprogramme is expected to be implemented by regional and local governments (as part of respective regional and local programmes of the housing and utility sector reform) and utility service producers, including extra-budgetary borrowings. From the total 18.5 billion USD only 179.3 million USD, or 1 percent, is contributed by the federal government. Federal funds will be used to support interregional projects and projects of modernization and completion of major infrastructure facilities that are of vital importance for regions and cannot be implemented without the federal government's support.

The strategy of governmental support to housing sector modernization is to create favourable conditions for attracting investments into this sector from commercial banks, and other sources of debt finance secured by guarantees of the federal, regional and local governments. The first steps towards this goal includes the restructuring of debts of utilities, enhancement of transparency of corporate and financial management, reduction of investment risks and development of appropriate debt finance mechanisms. Another important task of the federal government is to provide necessary legislative, regulatory and procedural framework for reform, modernization and extra-budgetary capital finance of the housing and utility sector.

In the longer term (after 2010) private investments are expected to become a predominant source of finance for modernization and development projects in the housing and utility sectors.

The subprogramme has two types of costs: costs of modernization of the sector infrastructure, and costs of providing social benefits and housing allowances to particular groups at the expense of the Social Expenditure Co-Finance Fund (SECF, see annex 2). Costs of housing allowances and other social benefits provided by the federal law will be covered by the federal, regional and local budgets. All through the programme, housing allowances will be provided in the total amount of 12.1 billion USD, including 1.6 billion USD (13.2 percent) subsidized by the federal government.

In the end, the federal resources of the subprogramme will be assigned to:

- Support the housing and utility sector modernization via FTIP (Federal Targeted Investment Programme); the allocation to the Housing Sector Reform and Modernization Subprogramme was 18.1 million USD in 2003, 39.4 million USD in 2004, and 46.5 million USD in 2005;
- Co-finance the liability to pay housing allowances to particular population groups via SECF (Social Expenditure Co-Finance Fund); the amount of the subsidy from the federal government for housing allowances was 163.0 million USD in 2003, 218.8 million USD in 2004, and 229.1 million USD in 2005.

¹³ total *estimated* cost of modernization of heat distribution and generating nets and water and sanitation facilities. *Specific rates* and types of financial support to be provided to investment projects are stipulated in regular annual budgets

Local financial markets for water supply and sanitation

As mentioned in an earlier section, the role of population as the main source of incomes of water supply and wastewater enterprises has significantly increased: in 2000, the share of incomes received from population in the total incomes from water supply was 30.9%, and by the beginning of 2006 it increased to 55.1%. As a result, the share of other users decreased: according to statistical data, the share of budgetary organizations in the total incomes from water supply decreased from 20% by the results of 2002¹⁴ to 14.3% in 2005, while the share of commercial users decreased from 39.1% to 30.6% (in 2002 and 2005, respectively).

The WSS sector is subsidized both directly and indirectly. Direct subsidies usually take the form of a lump-sum transfer from the budget (municipal, regional or federal). Other kinds of direct subsidies include grants for environmental projects (see “Credit sources”), and in-kind transfers of equipment or technical know-how from other countries water companies. One common practice is cross-subsidized tariff for water and wastewater.

Use of credit in water supply and wastewater sector

The Russian enterprises of the WSS sector have been using credit from commercial banks and municipalities to finance their infrastructure investments. However, these credits were short-term and aimed for financing current expenditure of projects. Long term finance is scarce on the Russian credit market, and lenders usually consider investments in WSS projects to be high risk investments. Thus, credit resources for WSS investment projects have been scarce so far.

The risks of long-term investments in WSS sector are very high. One major source of risk is the current tariff regulation system¹⁵. Another one is the unstable political environment of municipalities. A new mayor and/or Duma may cut tariffs and thus hinder repayment capacity, if they consider the purpose of the loan is not a priority, or the impact on tariffs is too high. Political risks of investment may exceed those of tariff regulation.

Due to high risks, infrastructure investment is usually carried out in the following manner. A vodokanal (an MUE that is responsible for water supply and wastewater) sets up a special purpose company (SPC) for carrying out a particular investment, jointly with investors, usually commercial banks. Having a stake in the project somewhat reduces investors’ risks, as they can easily claim whatever infrastructure has been built, as their own in the event of default. Then, investors issue short-term credits to finance current expenditure of the new company.

Special purpose companies (SPCs) are created when it is necessary to finance significant amounts of investments and when a collateral for the loan can be identified and isolated (in financial terms) from the rest of the infrastructure. Thus, reconstruction of pipelines is not usually carried out by SPCs: this would fragment the network and increase transaction costs associated with regulation. However, construction of wastewater treatment plants or water pumping stations can be financed through SPC.

One such example is the construction of new wastewater treatment plant in Ekaterinburg.

¹⁴ Official statistical reports for 2000 and 2001 contain information only about the share of population and other users in the incomes of water supply and wastewater enterprises; therefore, it is not possible to differentiate separately commercial users and budgetary organizations from the group “Other users”.

¹⁵ See part “Tariff regulation” for more information on the rate setting.

Box 2. Illustration of WSS investment financed by and SPC

The city of Ekaterinburg is planning to build a new residential area in a northern part of the city. The building site does not possess any water and wastewater infrastructure and it is estimated that existing wastewater treatment plants will not have the capacity to process wastewaters from this area.

Thus, a decision was made to build a new wastewater treatment plant, using the resources of municipal unitary enterprise "Vodokanal" and private sector investments. MUE "Vodokanal", jointly with Ecological Foundation "Water Eurasia" and commercial bank "Interregional investment bank" have founded a SPC named "Direction of wastewater treatment facilities". The SPC is in charge of all construction work. The total amount of investment is estimated around 590 millions rub.

Project financing is carried out on the following basis. The "Interregional investment bank" provides short-term (one year) credit (with interest rate equal to current Central Bank interest rate plus 2%¹⁶) to SPC, which is used to finance current operations. "Vodokanal" has an investment agreement with SPC by which all expenses of the project are included in the wastewater tariff and "Vodokanal" transfers these funds to SPC¹⁷. The credit is repaid when SPC receives the funds from "Vodokanal". In case of default by SPC to pay the principle of the loan, the "Interregional investment bank" has the right to seize assets already in place. This includes rather expensive technology which can be separated from the plant and sold.

Long-term investment is still not an issue as tariff regulation risks remain high. Unfortunately, there is no data on the level of such investments in WSS.

Private sector participation

The government has stated that private sector participation was one of the key elements of housing and communal sector reform in the Russian Federation¹⁸. The main aim of private sector participation is provision of funds to invest in the housing and utility sectors. However, events seem to overtake government plans. In 2004, there were at least five private companies in Russia that are already engaged in provision of water and wastewater services at municipal level. Four of these companies are Russian and one is a German private operator.

The creation of Russian Utilities Systems (RKS), a first national scale private operator, as a part of RAO UES was a clear signal of the trend towards private sector participation in WSS sector. Approximately at the same time¹⁹, a private company "Modern City", a subsidiary of Interros holding, announced that it would operate Perm vodokanal (a regional center with population over a million people) on a 49 years lease contract. Already in Zelenograd, WTE Wassertechnik GmbH, a German company, has built a wastewater treatment plant, under a BOOT²⁰ contract.

¹⁶ At the moment, the Central Bank interest rate is 14%.

¹⁷ The exact contents of this agreement is unknown as relationships between the "Vodokanal" and SPC are opaque.

¹⁸ Government Resolution N 797 from 17/11/01 "On sub-program "Reform and modernization of housing and communal complex of Russian Federation" of targeted Federal program "Zhilische" for years 2002-2010"

¹⁹ May 2002

²⁰ BOOT – acronym for Built-Own-Operate-Transfer.

Despite increasing activities of private sector in WSS, very limited investment activity is underway.

Credit market development in WSS

As stated in Government Resolution N 797 from 17/11/01 “On sub-program “Reform and modernization of housing and communal complex of Russian Federation” of targeted Federal program “Zhilische” for years 2002-2010” government expects that the main bulk of investments in WSS sector will be carried out by the private sector. Whether that will be commercial banks, or private operating companies is unclear. It is also unclear whether commercial credit will go to the existing MUEs, or whether private operators of WSS sector will operate and invest their own funds. The share of municipal budget and other budget resources is planned to be small and mostly directed towards provision of guarantees for private investments. Hence, municipal bonds are not likely to be the source of finance for municipal infrastructure projects.

The ministry of Gosstroi of Russia is considering a possibility of creating a special guarantee fund that will provide expertise for private investors in terms of risk assessment, and provide guarantees to their investments. The start-up capital of the “Guarantee Agency” will be provided by the federal budget; however, the Agency will operate on a competitive basis.

International multi-lateral organizations have recently started to actively support development of Russian water and wastewater sector through provision of credit, grants and consultancy services. At present, several investment projects in WWS sector are funded by the World Bank, EBRD, Danish government and DFID. Most of the projects are still in their early stages and it is difficult to draw conclusions from them.

The largest project so far has been the World Bank Municipal Water and Wastewater project. The total value of the project is 168.9 million US dollars and the project is implemented in 14 Russian municipalities. The main objectives of the project are:

- providing support for improvement in the operations in water and wastewater systems,
- implementing a specific set of institutional and commercial reforms aimed at improving physical system operations and financial performance of vodokanals.

The project focuses not only on providing funds for investments, but also on provision of technical assistance, training, project management and implementation support.

The project was initiated by Russian Federal authorities, and Russian Federation provides guarantees for the World Bank loan. This is a common situation with most of the municipal water and wastewater projects that receive financing from multi-lateral organizations. A Federal Government guarantee is usually required, even for less expensive projects. Other loans usually have a guarantee from regional authority and/or municipality.

Project financing by multi-lateral organizations is done either through on-lending from federal or regional level, or through direct landing to a Vodokanal. The former mechanism was implemented in the World Bank Municipal Water and Wastewater project and in EBRD project in Komi Republic. The latter mechanism was used in the EBRD project with Yaroslavl Vodokanal. In any case, multi-lateral organisations provide only a portion of finance, while the rest is provided by the federal, regional and municipal budgets, and vodokanal’s own resources.

Most projects that involve multi-lateral organisations usually involve not only direct investments in particular projects, but also provision of technical assistance, encouragement of reforms in utility sector and provision of support in project management. The level of such assistance varies with each project. However, this kind of assistance is necessary as current management practices of vodokanals and regulatory practices of municipalities may seriously endanger successful project realization.

Obstacles to the development of credit market in WSS sector

The main obstacle to greater and more efficient use of credit in WSS sector is underdevelopment of institutional arrangements that help to reduce risks of such investments. On the demand side, municipalities find it hard to attract long-term finance due to its scarcity and high costs. Municipalities are also cautious to borrow, as they may lose their assets in case of default. Ceilings placed on municipal borrowing by the Budget Code also restrict the use of borrowing by municipalities.

Borrowing by MUEs is also severely restricted. One of the main reasons is that most of municipally-owned vodokanals operate with net losses and have high outstanding debt to energy companies. Management of MUEs is another risk factor: managers usually refer to a technical approach, and tend to ignore the economic and financial dimensions of service provision. Most of managers at MUEs have held their positions since the times of the Soviet Union and they are managing their enterprises with methods that are long outdated in a transition economy. Creating a special purpose company to carry out investments is one of the ways of reducing management risks, as it allows investors to hire trusted professional managers.

On the supply side, provision of credit to municipalities is a risky undertaking. Loan repayment is often done by inclusion of interest and principal repayment in the tariff, but current tariff regulation systems provides no guarantees that the tariff will be high enough to repay the loan. A high share of vodokanal's revenue consists of budget compensation for privileges, tariff differences²¹ and subsidies. These compensations are almost never paid in full. This generates cuts and uncertainty on vodokanals' revenues and may hinder loan repayment. Finally, the Russian credit market is mainly short-term, and availability of long-term resources is limited. Municipalities find it hard to compete for long term finance with oil, gas and energy companies which are commonly viewed as relatively low-risk investment compared with municipal WSS sector.

Conclusions

The development of credit market for WSS sector in Russia is closely tied to increasing private sector participation in this sector. Commercial lenders view private companies in WSS sector as more reliable borrowers than municipalities. However, before private sector can fully enter the market for water and wastewater services, several steps have to be taken.

First, there is a need to clarify the legal and institutional framework for private sector participation in WSS sector. This will facilitate the development of credit market for financing investment projects in WSS sector. The law on concessions in utility infrastructure has set the framework for long-term contractual relationships between private companies and municipalities. Private sector participation through concession agreements will reduce contractual risks of investments and thus lower the cost of capital for private operators.

²¹ Russian municipalities set tariffs for households, but frequently they adopt what is called "the level of payment by households". It means that citizens do not pay the full tariff, but only a portion of it, as set by municipality. The difference between the actual tariff and the level of payment is supposed to be financed out of municipal budget but frequently, the budget does not have necessary funds.

Another important step is devising an efficient tariff regulation system for water utilities. Tariff setting procedures have to allow for recovery of invested funds, and the tariffs should be so stable that investments can be planned. Tariff regulation system also has to reduce political risks to minimum, by establishing rigid regulation procedures and methodologies for tariff calculation. Tariff regulation procedure has to account for budget debts, increases in prices of inputs and has to set profit rates, not as normatively defined rates of return but as a result of planned investments. The regulatory level also has to be consistent with the scale of water and wastewater enterprise. In other words, if vodokanal provides WSS services to a municipality, it has to be regulated by the municipality. The legal status of an enterprise should not be the factor defining regulatory level. All these issues are addressed in the law on tariff regulation in utilities sector.

Development of municipal credit market will have little impact on WSS sector financing as it will be the concern of private utility companies. However, financing of social improvement programs of municipalities can, and should be done through municipal credit market. The development of pension funds and insurance companies in Russia will increase the demand for long-term, low-risk financial securities that can be provided by municipalities.

The provision of institutional and legal framework for WSS credit market development however will not solve the problems of inefficient use of funds for WSS investment projects, poor management quality and will not in itself help to create effectively functioning credit market. There exists a great scope for provision of technical assistance and training for municipal officials, managers of MUE and private companies management.

Training

It is necessary to create resource centres for information dissemination and provision of training. Such resource centres will train municipal officials and utility managers in the areas of municipal finance, strategic planning, budgeting, tariff regulation, contract preparation, utility financial and investment management, public sector awareness, public relations and so on. Resource centres will also disseminate information on best local and international practices in public-private partnerships and other issues through holding conferences, seminars, issuing practical guides and handbooks.

Technical assistance

There is demand for technical assistance at federal and municipal levels. At federal level, this includes provision of legal support with drafting legislation for concessions, tariff regulation and strategic development of national WWS sector; technical support may come in the form of:

- Development of methodology and a database of technical and financial performance indicators of WWS companies,
- Provision of expertise in risk assessment in WWS sector investments,
- Provision of financial support to Environmental agencies,
- Provision of financial support to foundation of Guarantee Agencies,
- Encouraging competition among consultancy firms in WWS sector.

At the local level, technical assistance is required for the development of local credit markets, assistance to potential borrowers and potential lenders in loan terms negotiations, assistance to

municipalities in various areas that will help to strengthen local governments capacity to efficiently allocate budget resources and develop solid contractual relationships with private operators of WWS infrastructure. Such areas include:

- Preparation of tenders for WWS delegated management,
- Contract preparation,
- Financial and fiscal management,
- Capital investment planning, including preparations of business-plans, optimal allocation of funds, increasing energy efficiency, reducing water leaks etc.
- Strategic budget planning,
- Complex strategic city development planning.

Technical assistance can be delivered in a variety of ways, including the provision of expert advice and consultancy services, research of potential opportunities in developing credit market for WWS sector, monitoring indicators and development of the sector, or providing guarantees for private investments and financing consultancy and technical assistance services for potential borrowers.

External environmental assistance

External environmental assistance includes Official Development Assistance/Official Assistance (ODA/OA), and lending from International Financial Institutions (IFIs).

A note on method

This section presents trends in international environmental assistance to EECCA countries over the period 2001-05. Environmental assistance data have been compiled from databases at the OECD and supplementary data collected from donor countries. IFI data have been collected directly from those institutions and are based on their own definitions of environmental assistance that do not always match categories used in reporting bilateral assistance. The project team has tried to reconcile OECD sources and data collected from donors and IFIs so that the data set is as consistent as possible, in particular in terms of scope.

Environmental protection expenditure (previous chapter) does not refer to the same environmental activities covered by environmentally related assistance (this chapter); generally, the latter is a broader definition than the former. Furthermore, ODA/OA measures commitments, not disbursements. Thus, comparisons with the previous chapter are not reliable.

In addition to direct environmental international assistance and environmental lending, some environmental expenditure is made indirectly by integrating environmental elements into investment projects having non-environmental purposes (e.g. more energy-efficient processes). In domestic expenditure these flows are categorised as “integrated processes” and in IFI lending as “mainstreaming of environment”. International sources usually do not record these expenditures as “environmental”. Over the last couple of years, the focus on these types of environmental improvements and expenditures has increased. For EECCA, the World Bank and the European Bank for Reconstruction (EBRD) report financing for environmental projects. When appropriate, they also report the financing which supports the environmental component of a project which is not essentially in the environment

domain. The World Bank has identified the environmental component of non-environmental projects and it is included in the dataset, whereas the other IFIs have not done so. Therefore, the data reported overestimate environmental assistance by the IFIs. Similarly, indirect environmental assistance for bilateral donors is not accounted for.

Other issues, such as export credits, international commercial lending, international leasing and trade are not covered even though they have both positive and negative effects on environment.

Trends in environmental assistance in Russia

Environmental assistance to EECCA has witnessed a structural change since 2001. IFIs assistance has multiplied by almost 2, although it started from a low level after the financial crisis had affected a large number of projects at the turn of the century. In contrast, bilateral environmental assistance (which includes the European Commission) in 2005 is below the level of 2001.

The Russian Federation is the second major recipient of bilateral environmental assistance in EECCA, after Kazakhstan (195 million USD since 2001, compared to 251 million USD) and has received 21% of bilateral environmental assistance over the period 2001-05. Major donors over the period have been the US, the Nordic states (Sweden, and to a lesser extent, Finland and Denmark), the European Commission and Germany.

The split by domain indicates that Environmental policy and administrative management has attracted 42% of bilateral assistance since 2001; the European Commission is particularly active in this area. Water supply and sanitation, and biosphere protection are second priorities (14% of the total each). Other domains comparatively attract little attention.

Multilateral environmental assistance from IFIs is spread differently: Russia has received 63% of the total flows over the period (1.2 billion USD). The EBRD is the main provider of assistance. The World Bank and the EIB also have strong stakes. NEFCO has been playing an increasing role since 2004.

Multilateral environmental assistance is focused on three domains: water supply and sanitation has attracted 38% of total financial flows over 2002-05. Over the same period, the share of assistance to power generation and renewable energy production amounted to 27%. Water resource management has attracted 21% of IFIs assistance since 2001.

The relative weight of external environmental assistance in Russia (as a share of GDP) is negligible. However, projects supported by the international community are recognised as having particularly positive demonstration and catalytic effects, both in terms of technology transfer and the development of new skills and know-how.

ANNEXES

Annex 1. A method to monitor environmental protection expenditure

Domestic expenditure data were collected from national official statistics. The data have been cross-referenced where possible with other data sources. The data on international commitments have been collected from the OECD Development Assistance Committee (DAC) Aid Activity Databases and cross-checked by directly surveying international financial institutions (IFIs) and international co-operation and environmental agencies in individual donor countries.

The analysis of environmental expenditures is impaired by methodological and procedural problems: data is collected by a variety of national authorities, which use different definitions and tools, and it has not always been possible to reconcile them. Monitoring environmental expenditure is also weakened by the lack of resources devoted to data collection and processing. These are barriers to policy making and to the more effective allocation of financial resources.

The data set developed for Russia has the following features:

- It covers environmental protection expenditure, but not natural resource management;
- It makes no distinction between, water supply and sanitation;
- The public sector is partially covered; the other economic sectors (specialized producers of environmental services, business sector) are properly covered;
- It has not been possible to sever the investments made by the public and the private sectors.

Domestic expenditure

OECD work on Pollution Abatement and Control (PAC) expenditure dates back to the late 1970s. A first questionnaire was sent to member countries in 1991. Since 1996, data have been collected through a joint OECD/Eurostat questionnaire, periodically revised to foster cross-country comparability and to minimise reporting efforts. Following the 2001 revision, the current questionnaire focuses on expenditure for environmental protection activities composed by the flow of investment, internal recurrent expenditure, subsidies and fees directly aimed at environmental protection. It includes expenditure incurred by the public and business sectors, households and specialised producers of environmental services.

The definition of environmental protection expenditure (EPE) excludes expenditure on natural resources management and prevention of natural disasters, expenditure that primarily complies with health and safety requirements or motivated by commercial, technical or efficiency grounds. Also excluded are: the depreciation of fixed capital; the cost of capital as well as the payment of interest, fines and penalties for non-compliance with environmental regulations.

The OECD, in conjunction with Eurostat, has promoted the adoption of a common framework for environmental expenditure accounting in a number of EECCA countries that will facilitate harmonisation of methodologies, comparison of resulting data, and support sound environmental policies. The EAP Task Force has implemented a number of projects to facilitate the dissemination of this framework in EECCA countries (in Georgia, the Kyrgyz Republic, and Ukraine).

The OECD/Eurostat questionnaire has been used by the EAP Task Force as a basis for the analysis of environmental protection expenditure in EECCA.

External environmental assistance

Official Development Assistance (ODA) and Official Assistance (OA) are defined as aid flows to developing countries (Armenia, Azerbaijan, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Tajikistan, Turkmenistan, and Uzbekistan) and countries in transition (Belarus, the Russian Federation, Ukraine), respectively²².

To qualify as ODA/OA, a transaction must be undertaken by the official sector for the main purpose of promoting economic development and welfare, be concessional in character, and convey a grant element of at least 25%. Data are collected annually from the members of the OECD's Development Assistance Committee (DAC), which comprises 22 members and the European Commission, through two reporting systems: the aggregate DAC statistics and the activity-specific Creditor Reporting System (CRS)²³. The data cover aid loans and grants, other official flows, private market transactions and assistance from non-governmental organisations to each recipient country and regions. In addition to financial flows, technical co-operation is included in aid. Grants, loans and credits for military purposes are excluded.

The data presented also includes revision and updates from donor countries and IFIs collected throughout the preparation of this report. Those IFI flows that qualify as ODA/OA are included in this report as IFIs commitments, and not as bilateral ODA/OA.

The definition of assistance reported here includes "environmentally related" commitments following a classification proposed by the World Resources Institute (WRI) (Donge and others, 2001). The choice of a definition has a profound impact on the magnitude of estimated commitments. For example, in 2000 the total environmental assistance to all developing and transition countries was USD 1.4 billion under the strict OECD environment terminology, but was USD 7.3 billion under the expanded WRI definition.

Contrary to the domestic expenditure data, the international flows data used in this report are reported based on commitments, not disbursements. Commitments may, however, be different from assistance actually received, as they may be cancelled or postponed. Therefore commitments data are an overestimate of the actual flow of assistance. There are also problems with comparing commitments with Gross Domestic Product (GDP) and other macro economic indicators as commitments taken in one year may involve disbursement over several years.

²² As from 2005, donors are no more required to report OA to transition countries, therefore data for this year may underestimate the amount of assistance provided to the EECCA region

²³ For further details on the databases coverage and reporting directives consult the DAC site at the following address: www.oecd.org/dac/stats.

The assistance and development lending is reported at aggregated levels as well as at disaggregated levels (project specific data), and unfortunately these two reporting frameworks do not give the same results. Reporting at the aggregate level is comprehensive and more or less complete, but does not allow for distinguishing environmentally related assistance from total assistance or breakdowns of expenditure by environmental domain. At the project level (CRS project database) environmentally related assistance can be identified with higher accuracy, but only about 60% of total ODA/OA flows are reported. Not all countries report their assistance at the project level to the CRS database.

For the purpose of this report the effort was made to supplement missing project specific data in the CRS database to achieve comprehensiveness of the aggregated DAC database and not to lose the structural insight of the CRS. Therefore the major donor countries and IFIs operating in the EECCA region have been asked to update the information on environmentally related projects in the CRS database. Some donors have provided project-specific information with purpose code identification, whereas others have provided aggregated figures. The OECD/EAP TF Secretariat has added the information provided by the countries and IFIs to the CRS database figures. All major donors to EECCA have either reported assistance at the project level to the EAP TF Secretariat or provided aggregated figures for environmental assistance to EECCA countries.

GENERAL INFORMATION	<p>Environmental protection expenditures are published annually by Rosstat (State Statistics Department of the Russian Federation).</p> <p>Data on investments and current expenditures for environmental protection have been published since 1990.</p> <p>Forms of statistic observations include data on environmental protection activities for protection of water sources from waste waters, for air protection from emission of pollutants, land and forest protection, restoration of fish population, protection of specially protected natural areas and biodiversity, construction and exploitation of installations (facilities, buildings) for recycling, disinfection, dumping, disposal of solid municipal and industrial waste, etc.</p>
MAIN USERS AND RECIPIENTS	<p>President of the Russian Federation, the Government, the Council of Federation of the Federal Assembly of the Russian Federation, the State Duma, other federal agencies, scientific organizations, enterprises, citizens, international institutions, etc.</p>
SOURCES OF INFORMATION AND TYPES OF EXPENDITURES	<p>Statistic information on environmental protection expenditures is based on data from federal public observation forms and also on summary financial reports of application of budget funding and other expenditures of environment protection institutions.</p>
LINES OF ENVIRONMENTAL PROTECTION ACTIVITY	<p>All activities are represented, excluding noise and vibration protection, which are considered in context of human health protection. Statistic observations for human health and vibration are not implemented. There are no skipped reporting periods.</p>
SECTORS OF ECONOMY	<p>Rosstat does not dispose methodological recommendations of OECD on formation of public and business sectors of environmental protection expenditures.</p> <p>Rosstat treats data on environmental protection investments, current expenditures for environment protection activities in general for economy and for individual kinds of business activity according to All-Russia classification of economic activities (NACE), harmonized with NACE (version 1)/</p> <p>There are no observations of environmental protection expenditures at households.</p>

Annex 2. Mechanisms for intergovernmental transfers in Russia

Federal Financial Support Fund for Federation Subjects (FFSF)

The Fund is formed with a view to increase revenue capacities of particularly weak regions and to equalize their capacities to finance *operating* expenses. FFSF resources are used for granting *general equalizing transfers*²⁴, which means that they are provided to regional governments with no specific purpose.

According to the procedures, equalizing grants are calculated on the basis of unbiased evaluation of revenue (taxable) capacities and expenditure liabilities of regional governments. Taxable capacities of regions are assessed by measuring the volume and structure of their regional gross outputs, to see the potential revenue-generating capacities of regional economies with due consideration of their specific development level and structure. Differences in revenue-generating capacities of regions are taken into account by using the taxable capacity index when estimating their per capita revenue budget flow. Differences in expenditure burden of regions are assessed with the budget expenditure index (BEI). BEI is a calculated index showing relative differences in the cost of standard public services caused by demographic, socioeconomic, geographical, climatic and other external factors and terms affecting regional consolidated expenditure budget planning. BEI makes possible to estimate how much (or less) regional governments will have to spend per head for production of a similar volume of public services, with all real regional factors and conditions considered, as compared to the national average.

In 2004, the Russian Government approved the Procedure for Allocating Grants from the Federal Financial Support Fund for Federation Subjects by issuing Resolution #670 of 11/22/2004.

This method is designed to help regions with per capita tax resources below the national average to improve their revenue, and accordingly to access the minimum flow of revenues to finance their operating expenses.

In accordance with revisions made in the RF BC in 2004, the resources of the FFSF should be increased by the anticipated inflation rate for the next year, to make it more predictable.

In 2002-2004, FFSF-funded equalizing transfers were provided to 71 (out of 89) Federation Subjects (regions), including 31 regions that were particularly highly subsidized. According to the RF Budget Code, regions which receive more than 50 percent of their revenues from FFSF, and which do so for two years over a three year period are eligible to continue receiving FFSF equalizing grants (and budgetary loans from the federal government) over the next three years, if they reach an agreement for budget management and tax and non-tax revenue enhancement with the Russian Finance Ministry. Agreement conclusion and administration are regulated by the Russian Government.

Compensation Fund (CF)

Annually revised as part of the federal budget planning from 2001, the Fund was formed with the view to ensure financing of implementation of federal social laws at the expense of consolidated

²⁴ before 2005, alongside with general equalizing transfers FFSF resources were also used for paying product acquisition grants to specific regions where the product delivery time was limited due to seasonal factor, and paying electricity tariff compensation subventions to Far East and Arkhangelsk regions. Grants and subventions of this type financed by FFSF averaged to 3.2 percent of the total financial aid provided to regions in the reporting period

regional budgets²⁵. Before 2004 Compensation Fund resources were used for paying *block (earmarked) grants and subventions* to regional governments. From 2005, CF resources are used only for paying subventions.

Compensation Fund provides financial support to each and all regions, no matter what per capita revenue level they have. Funds are allocated between regions pro rata the number of eligible users of social assistance they have subject to the public service appreciation factor varying with regions.

Distribution of Compensation Fund subventions is regulated by the Compensation Fund Subvention Allocation Procedure set by the Russian Government (Resolution # 670 of November 22, 2004). The Russian Government also establishes rules for granting, spending and accounting of CF-funded block subventions (and grants in the period before 2005).

Social Expenditure Co-Finance Fund (SECF)

As a component of the federal budget, the Fund is subject to annual approval and used for partial reimbursement of high-priority social expenditure of regional governments and implementation of federal social mandates (laws).

SECF resources are allocated as *subsidies* to each and all regions under the SECF Subsidy Allocation Procedure that is annually revised and approved by the Working Group set for improvement of intergovernmental relations in the Russian Federation.

In 2002 – 2003, SECF resources were used for partial reimbursement of public sector wage increases performed by regional governments, and payment of housing allowances to eligible population groups; in 2004, they were spent only on payment of housing allowances.

According to the federal Budget, in 2005 SECF resources will be used for:

- Housing allowances to eligible population groups;
- Social assistance to rehabilitated victims of political repressions;
- Social assistance to labor and home front veterans;
- Public allowances to families with children.

Similarly to Compensation Fund subventions, SECF subsidies are allocated under procedures set by the Russian Government and placed on treasury accounts of regional governments. Control over SECF subsidy spending is executed through the delivery of respective reports of regional governments to the Russian Finance Ministry.

Regional and Municipal Finance Reform Fund (RMFRF)

The Fund was established as part of the federal budget in 2001, to accelerate the financial recovery of Russian regions and implementation of budget reforms at the regional level.

²⁵ a consolidated regional budget is an aggregate of the budget of a regional government and budgets of local governments operating inside the region

In 2002 – 2004 resources (*subsidies*) were allocated between regional governments on a competitive basis. Regional governments interested in receiving a subsidy had to file a *Subsidy Application* containing tabulated information on the basis of which their paying and financial management capacities, programmes of regional finance reform and subsidy plans were assessed. Regions were selected in accordance with findings of the summary evaluation of subsidy applications. Regions could be disqualified if they had disqualifying features (nonobservance of RF BC debt and budget deficit limits, overdue liabilities, etc.). Subsidy applications were evaluated under the dedicated procedure.

In 2005, the Regional Finance Reform Fund was renamed as the Regional and Municipal Finance Reform Fund (RMFRF), given that Russian municipalities have become eligible. RMFRF subsidies can be provided to no more than 8 regions and 8 municipalities.

On January 05, 2005, the Russian Government approved the RMFRF Subsidy Allocation Regulations (Russian Government Resolution #2 of 01/05/2005), which established recipient selection, subsidy rating, allocation and spending procedures for regions and municipalities.

Subsidies are placed on treasury accounts of regional (municipal) governments and incorporated into their budgets.

Decisive selection criteria are the quality of the regional (municipal) finance reform programme and the quality of the application (without any disqualifying feature). Subsidized regional and municipal administrations are obliged to report about implementation of their reform programmes and spending of RMFRF subsidies in accordance with procedures and deadlines established by the Finance Ministry.

RMFRF subsidies can be used for co-financing the following types of regional (municipal) budgetary expenditure:

1. Implementation of the Reform Programme (purchase of equipment, software and consulting services; inventory making, cadastre and database management; resource and energy saving measures; training and personnel development);
2. Servicing and discharge of liabilities and accounts payable;
3. Infrastructure development (construction, modernization of social infrastructure facilities, public utilities, transport and environmental infrastructure);
4. Implementation of social security measures (reimbursement of the cost of payment of social benefits and housing allowances, purchase of medical equipment, other socially important costs).

The Guidelines establish different rates to co-finance the aforementioned types of expenses: reform programmes can be co-financed at 80 percent, debt service and discharge costs at 60 percent, infrastructure development at 40 percent, and socially important costs at 20 percent. This helps the federal government to accomplish the key mission of RMFRF – acceleration of budget reforms at the regional level. Recent practice has demonstrated that RMFRF subsidies are mostly spent on implementation on reform programmes and discharge of liabilities.

Regional Development Fund (RDF)

The Regional Development Fund was established in 2000. Its resources are earmarked for supporting investments into regional infrastructure; they take the form of subsidies to regional authorities to co-finance investments into regionally- or municipally-owned projects.

In 2001, the federal budget incorporated 41 Federal Targeted Regional Development Programmes (FTRDP) co-financed by RDF (32 in 2000). Then, the federal government decided to curtail significantly the number of federal programmes co-financed by RDF starting. This was achieved mostly by enlarging and consolidating programmes, in an effort to increase the efficiency of budget outlays and to concentrate budgetary resources on the development of large economic areas and regions of particular geopolitical importance, and on creating conditions to narrow the gaps in the development of specific territories. In 2002, RDF financed only 6 FTRDP (see below); the programme on *Social and Economic Development of Bashkortostan Republic till 2006* was added in 2003.

Table 6. Finance Structure of Federal Targeted Regional Development Programmes (FTRDP), USD million

Federal targeted regional development programmes	Total	Including									
		Federal budget		Regional budget		Local budget		Corporate budgets		Other extra-budgetary sources ²⁶	
		m USD	per cent	m USD	per cent	m USD	per cent	m USD	per cent	m USD	per cent
Kaliningrad Oblast Development in Period till 2010	3,105.7	257.4	8.3	Kaliningrad Oblast consolidated budget				690.5	22.2	2,062.0	66.4
Social and Economic Development of Far East and Trans-Baikal in 1996 – 2005 and till 2010	12,223.9	933.0	7.6	751.3	6.1	67.7	0.6	3,277.7	26.8	7,194.2	58.9
Social and Economic Development of Kuril Islands in Sakhalin Region (1994 – 2005)	275.6	49.3	17.9	17.8	6.5	8.8	3.2	82.5	29.9	117.1	42.5
Russian South	2,662.8	519.1	19.5	274.1	10.3	60.0	2.3	760.2	28.6	1,049.3	39.4
Social and Economic Development of Tatarstan Republic till 2006	12,755.5	2,767.1	21.7	2,131.1	16.7	207.0	1.6	4,003.7	31.4	3,646.6	28.6
Social and Economic Development of Bashkortostan Republic till 2006	5,453.9	1,081.9	19.8	903.2	16.6	120.5	2.2	1,651.1	30.3	1,697.3	31.1
Leveling Out Differences in Social and Economic Development of Regions in the Russian Federation (2002-2010 and till 2015)	2,248.2	420.8	18.7	Consolidated budgets of Russian Federation regions				728.8	32.4	584.5	26.0
				514.2		22.9					

Source: Russian Government resolutions on approval of mentioned federal targeted programmes

The table shows that the projects benefit from other sources of finance: the federal budget contribution ranges from 7.6 to 21.7 percent. Thus, FTRDP finance by the federal government encourages the use of alternative sources of finance.

²⁶ commercial bank loans, international loans and other extra-budgetary sources

RDF subsidies are targeted. All RDF-funded programmes, except the programme of *Leveling Out Differences in Social and Economic Development of Regions in the Russian Federation*, definitely specify the lists of investment projects and regions where they should be implemented as well as implementation stages and amounts of finance to be provided for each phase. Federal and regional contributions to FTRDP are subject to annual revision.

The programme of *Leveling Out Differences in Social and Economic Development of Regions in the Russian Federation* differs from other FTRDP by the requirement to annually revise lists of regions and projects eligible to receive RDF investments. The selection of regions for RDF subsidizing under this programme is performed jointly by the Ministry of Economic Development and Trade and the Finance Ministry under the peculiar Fund Allocation Guidelines established by the Russian Government for that Programme²⁷.

The Guidelines suggest giving financial priority to life support projects (power-, water-, heat-, gas-supply, etc.) and to social projects (education, health care, construction of homes for the disabled, refugees and migrants).

Governmental support for *engineering infrastructure* development projects (power, water, heat, gas supply and other similar projects) aims to level out the infrastructure development status of regions, by constructing necessary infrastructures. Only those regions that have a significant deviation from the national average indicators of engineering infrastructure development are eligible to receive the governmental investment support. It is also worth noting that governmental investments from RDF are provided only to regions that have already created a favorable legislative environment for businesses and investments.

RDF subsidies are subject to targeting and, hence, may be used only to support specific investment projects. The Guidelines suggest selecting projects for the Programme by inviting regional governments for bidding. The goal of such bidding is to select projects that particularly require federal support, that are well-designed and that can really help reduce developmental differences between regions.

Another decisive criterion is preparation of a project rationale showing how the implementation of a specific engineering infrastructure will help reduce regional differences.

The amount provided under the programme to each region is calculated via a standard formula, based on the degree of their deviation from the national average development indicators.

The rates of co-financing established by the Programme of Leveling Out Differences in Social and Economic Development of Regions in the Russian Federation for the federal and regional budgets come to 18.7 and 22.9 percent respectively (see Table 6). These rates are differentiated according to per capita revenue capacities of regions when they go through the annual selection for participation in this Programme. Certain, particularly underdeveloped, regions, may receive 50 or even 70 percent support from the federal budget.

²⁷ RF Government Resolution #737 of 12/03/2004, “On Making Changes in the Federal Targeted Programme of Leveling Out Differences in Social and Economic Development of Regions in the Russian Federation (2002-2010 and till 2015) Approved by the RF Government, Resolution #717 of 10/11/2001”

Other grants and subventions

Other grants and subventions, which amount to 8.2 percent (in 2002) and 12.5 percent (in 2004) of federal financial assistance, include:

1. Grants to cover costs of maintenance of housing and utility facilities placed under the jurisdiction of local governments;
2. Grants and subventions to finance infrastructure costs of Baikonur City (Kazakh Republic) as is specified by the Baikonur launch space lease;
3. Grant-in-aid to Sochy City as a major health resort;
4. Grants to ensure stable revenue flows in regions (compensation of lost revenues due to changes in the budget and tax law of the Russian Federation);
5. Subventions paid to closed territories in order to support their development programmes;
6. Other grants and subventions paid to closed territories;
7. Subventions paid under the Programme of development of cities – research centers;
8. Subventions paid to winners of the Most Comfortable City National Competition;
9. Subventions paid to Moscow City for implementation of the federal mandate on collection and recycling of radioactive waste in Central Russia.

Grants and subventions to closed territories have a particularly great weight in the total financial assistance: in 2002, they made up 37.2 percent of the total assistance provided as “Other Grants and Subventions”; in 2003, they made up 36.0 percent, and in 2004 – 27.9 percent.

Transfers made as part of mutual settlements

Transfers are paid from the federal budget to regions, as compensation of additional costs incurred to implement federal decisions and from the Presidential Reserve Fund, the formation of which is regulated by the RF BC, Article 82 (in amount of no more than 1 percent of the approved federal expenditure budget). Resources of the Presidential Reserve Fund are used to finance unforeseen or extra costs approved by Presidential Decrees. Money from the Presidential Reserve Fund money can be disbursed only upon written authorization by the President of the Russian Federation.

Such transfers do not play a significant role in the total structure of the financial assistance Russian regions receive from the federal government.

Road maintenance subventions and grants

This type of assistance is provided to regional governments in support of construction and modernization of public roads and road infrastructure facilities.

In the reporting period this type of subventions and grants has somewhat lost its weight in the total structure of the federal assistance to regions, although it still remains comparatively large (9.4 percent).

Regional development initiatives

This component of the federal financial assistance to regions is designed to finance:

1. Federal targeted programmes²⁸. These are a group of research, development, production, socioeconomic, business management and other actions meant to ensure efficient solution of systematic problems in state, economic, environmental, social and cultural development of the Russian Federation;
2. State capital investments into construction, modernization and retrofitting of regionally- and municipally-owned public property, as part of the Federal Targeted Investment Programme (FTIP). State capital investments are a most significant component of the federal budget expenditure related to implementation of federal targeted programmes.

FTIP development and implementation procedures are regulated by the Russian Government Resolution #594 of 06/26/1995. Procedural management and co-ordination of works on FTIP development and implementation is performed by the Russian Ministry for Economic Development and Trade.

FTIP are financed out of the federal and regional budgets and extra-budgetary sources as well (contributions of state and non-state enterprises and organizations – project participants; targeted deductions from profit of interested enterprises; bank loans; resources of funds and nonprofit organizations; resources of foreign investors interested in implementation of a programme).

In order to improve policies and practices under the Federal Targeted Investment Programme, the Russian Government issued the Regulations for Making a List of Construction Projects of Federal Importance and Providing the Federal Financial Support to them. This list specifies how FTIP capital investments will be allocated between specific construction projects in the next year. It includes federally-owned projects, but may also include projects belonging to regional or municipal governments or non-state commercial entities. For projects belonging to regional or municipal governments, funds are allocated in the form of subsidies.

The list is prepared by the Ministry for Economic Development and Trade based on the social and economic development forecast, the long-term financial plan of the Russian Federation, and the next year draft of FTIP. The next-year Federal Targeted Investment Programme is planned in accordance with investment priorities of the Russian Federation:

1. Modernization and development of production infrastructure of national importance (transportation, pipeline and communications networks);

²⁸ apart from federal targeted regional development programmes (FTRDP) regional governments are engaged in implementation of a variety of other federal programmes (for example, such programmes as *Housing, Children of Russia, Senior Generation, Ecology and Natural Resources of Russia, Russian Culture*, etc.) This component also includes *research and development costs and other expenses* due to implementation of federal targeted programmes. *Capital expenditure* of federal targeted programmes are covered by the Federal Targeted Investment Programme

2. Modernization of public utility infrastructure in accordance with advance energy-saving technologies for the benefit of improvement of service quality, cost saving and attraction of extra-budgetary funds into utility infrastructure modernization projects;
3. Investments into social infrastructure facilities of federal importance including investments in research, education, public health; investments in renovation of cultural sites of world and national importance;
4. Targeted support of investment projects supported by the federal government because of their potential impact on the competitiveness of the national economy;
5. Investments into the judicial system infrastructure, to improve its autonomy and independence;
6. Building up and developing engineering capacities of the “new economy”, first of all scientific researches;
7. Implementation of nature protection measures and creation of a favourable environment for safe habitat.

Table 7 below shows the structure of state capital investments made under the Federal Targeted Investment Programme in 2002 – 2004.

Table 7. Structure of State Capital Investments Made Under the Federal Targeted Investment Programme (FTIP) in 2002-2004, million USD

State capital investments	2002		2003		2004	
	m USD	percent	m USD	percent	m USD	percent
FTIP state capital investments, total	1,421.1	100.0	2,122.5	100.0	2,785.8	100.0
including						
Social sector, total	866.1	60.9	1,414.1	66.6	1,769.2	63.5
<i>including</i>						
<i>Housing and utility sector</i>	343.6	24.2	627.1	29.5	770.4	27.7
<i>Education, culture and public health</i>	202.6	14.3	297.1	14.0	441.4	15.8
<i>Central authorities</i>	166.6	11.7	201.5	9.5	221.8	8.0
<i>Scientific research organizations</i>	26.1	1.8	29.9	1.4	36.4	1.3
<i>Metro building</i>	75.3	5.3	201.5	9.5	230.9	8.3
Industrial complexes	224.2	15.8	298.1	14.0	426.6	15.3
Special complex ²⁹	330.8	23.3	410.4	19.3	590.0	21.2

Source: federal laws on federal budget in 2002-2004

Table 8 below shows the dynamics of total investment support in the overall structure of financial assistance the federal government provides to Russian regions.

Table 8. Investment Support Provided to Russian Regions by FTIP and RDF, USD million

Federal budgetary assistance	2002		2003		2004	
	m USD	percent	m USD	percent	m USD	percent
Financial assistance to other-level budgets, total	9,411.2	100.0	12,315.7	100.0	13,658.5	100.0
<i>including:</i>						
investment assistance to social and infrastructure development projects:	712.7	7.5	746.8	6.1	1,265.2	9.3
- <i>Regional Development Fund (RDF)</i>	557.8	5.9	417.0	3.4	871.4	6.4
- <i>State capital investments (FTIP)</i>	154.9	1.6	329.9	2.7	393.8	2.9

Source: Russian Federation annual federal budget laws of 2002 – 2004

²⁹ military-industrial complex, technical upgrading and modernization of high-tech industries under the federal targeted programmes, Military-Industrial Complex Reform and Development (2002-2006), «Civil Aircraft Engineering Development in Russia in 2002-2010 and for the Period till 2015», «Federal Space Programme of Russia in 2001-2005, World Ocean

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