



# **Environment Fiscal Reforms (EFR)**

---

**Dr Usman Mustafa**

Chief, T&PE Division, PIDE

Presentation for PIDE "Nourishing Mind Seminar"

December 27, 2007

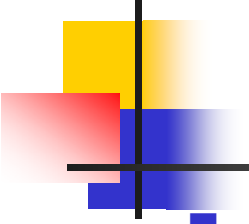


# ROAD MAP

---

- **Introduction about Env. & Poverty**
- **What is Environmental Fiscal Reforms (EFR)?**
- **Research Base**
- **Research Methodology**
- **Decentralization**
- **Main Features of Federal Fiscal System in Pakistan**
- **Major Issues in FD**
- **Major Opportunities in FD**
- **Findings and Conclusions**
- **Recommendations**

# Introduction about Envi. & Poverty

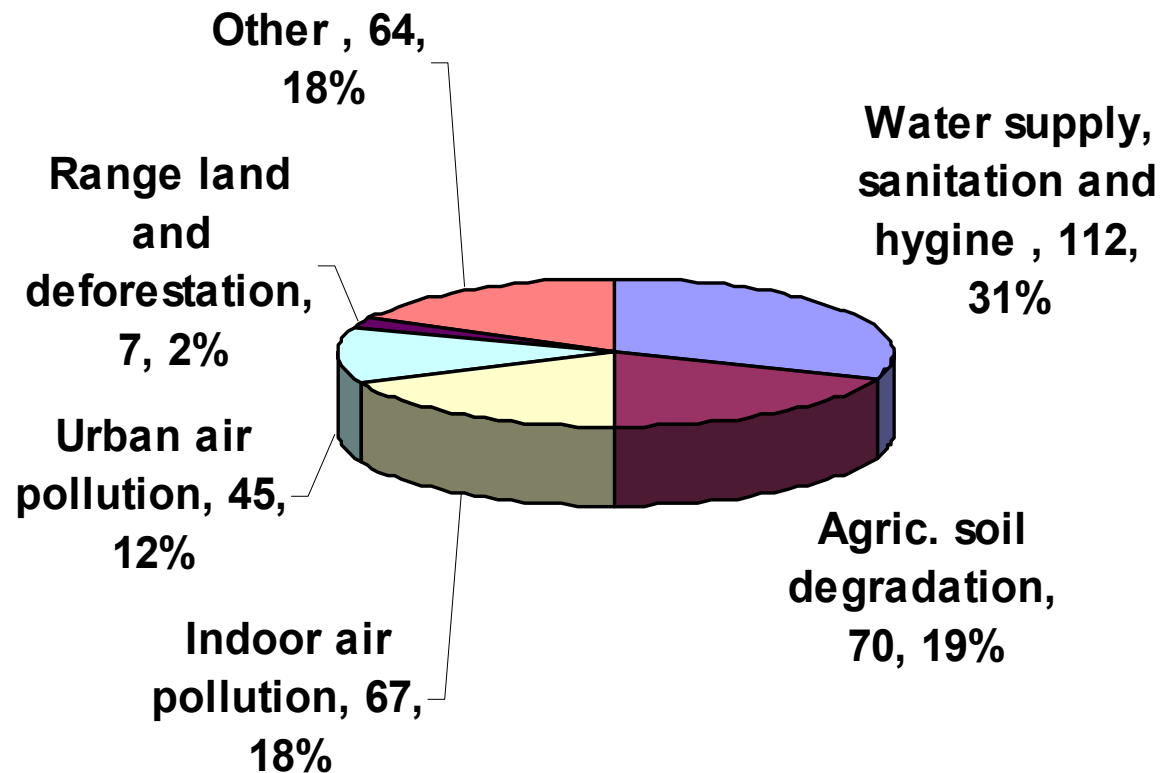
- 
- **Poverty ↓ & its alleviation ≈ Distribution of resources**
  - **Public revenue & benefit are generated through harvesting of NR → distribution of benefits are mismanaged & misallocated**
  - **Macro-economics indicator are impressive → trickledown effects?**
  - **Poverty and envi. relationship (- tively correlated) – vicious cycle → envi. cause & consequence of poverty**



# Economic Consequences of Environmental Degradation

- **Economic consequences of environmental degradation → enviro. degradation ↓ 6% GDP**
  - The highest cost → inadequate water supply, sanitation, and hygiene (Rs. 112 billion)
  - agricultural soil degradation (Rs. 70 billions)
  - indoor air pollution (Rs. 67 billion).
  - Urban air pollution (particular matter) adds another Rs. 65 billion.
  - The estimated cost of lead exposure is about Rs. 45 billion.
  - Rangeland degradation and deforestation cost are the lowest at about Rs. 7 billion in total.

# Annual losses due to env. degradation





# What is EFR?

---

- **Environmental fiscal reforms refer to a range of fiscal measures which raise revenues and rationalizing expenditure while furthering environmental goals.**
- **EFR can also help reduce poverty through environmental and fiscal benefits.**

## Guiding Principles

# “Polluter Pays Principle” (PPP)

---

- Polluter causing negative externalities.
- Society is paying this cost
- The cost of these measures should be reflected in the cost of goods and services, which causes pollution in production and/ or consumption.
- Polluter should bear the expenses of carrying out those measures decided by public authorities to ensure that the environment is in adequate state.
- The resources generated should be used to facilitate or support the environmentally friendly measures.



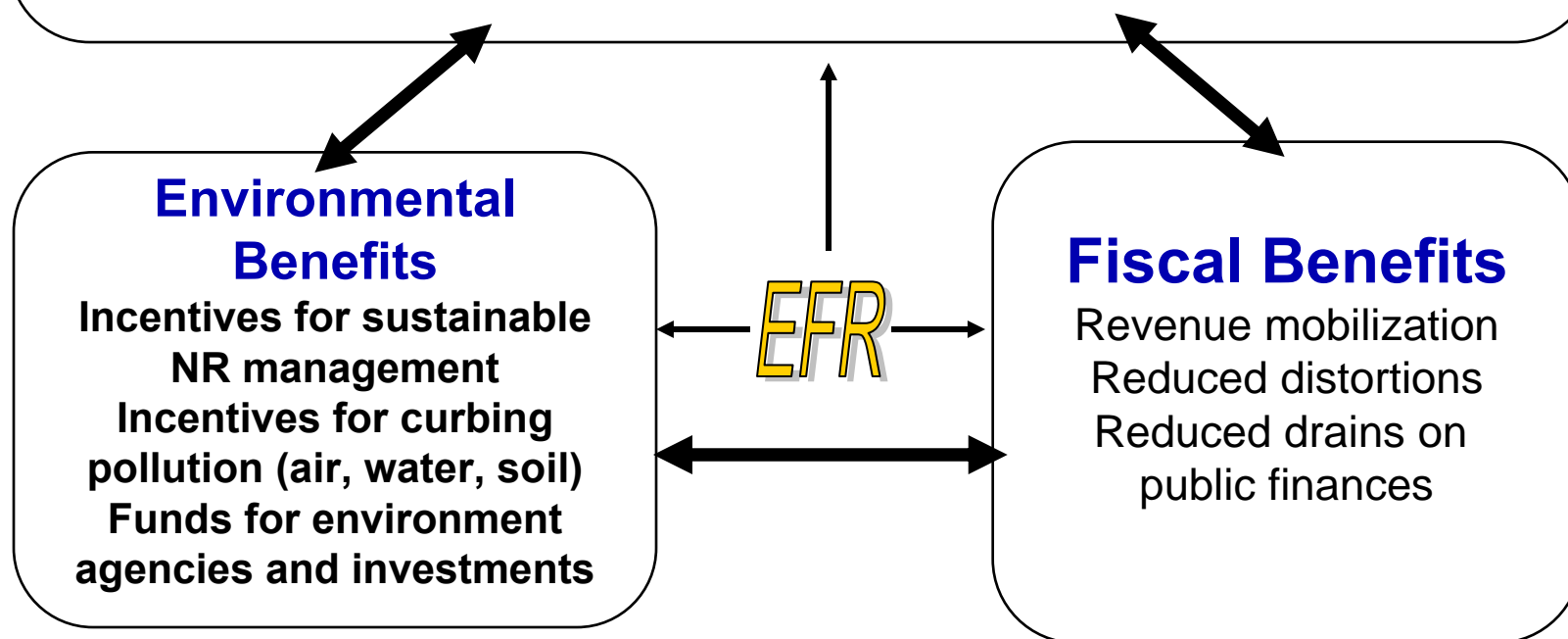
# EFR Benefits

## Poverty Reduction

Improving **environmental** quality eg better natural resource management or provision of environmental infrastructure:

–poor depend on environment for health, livelihoods and vulnerability

- Fiscal** revenues: revenues for pro-poor expenditure on health, education etc
- Protection or compensation** to protect poor from price rises





# **How to go about it?**

---

**Benefits can be captured and constraints can be addressed – but requires analysis, research, political and institutional reforms, advocacy and political leadership**

# Project Component

## Project Component 1

- ↗ *Action research and awareness raising*
- ↗ Assess the political economy of EFR

## Project Component 2

---

Developing Enabling Policy/Legal framework

## Project Component 3

Capacity Building

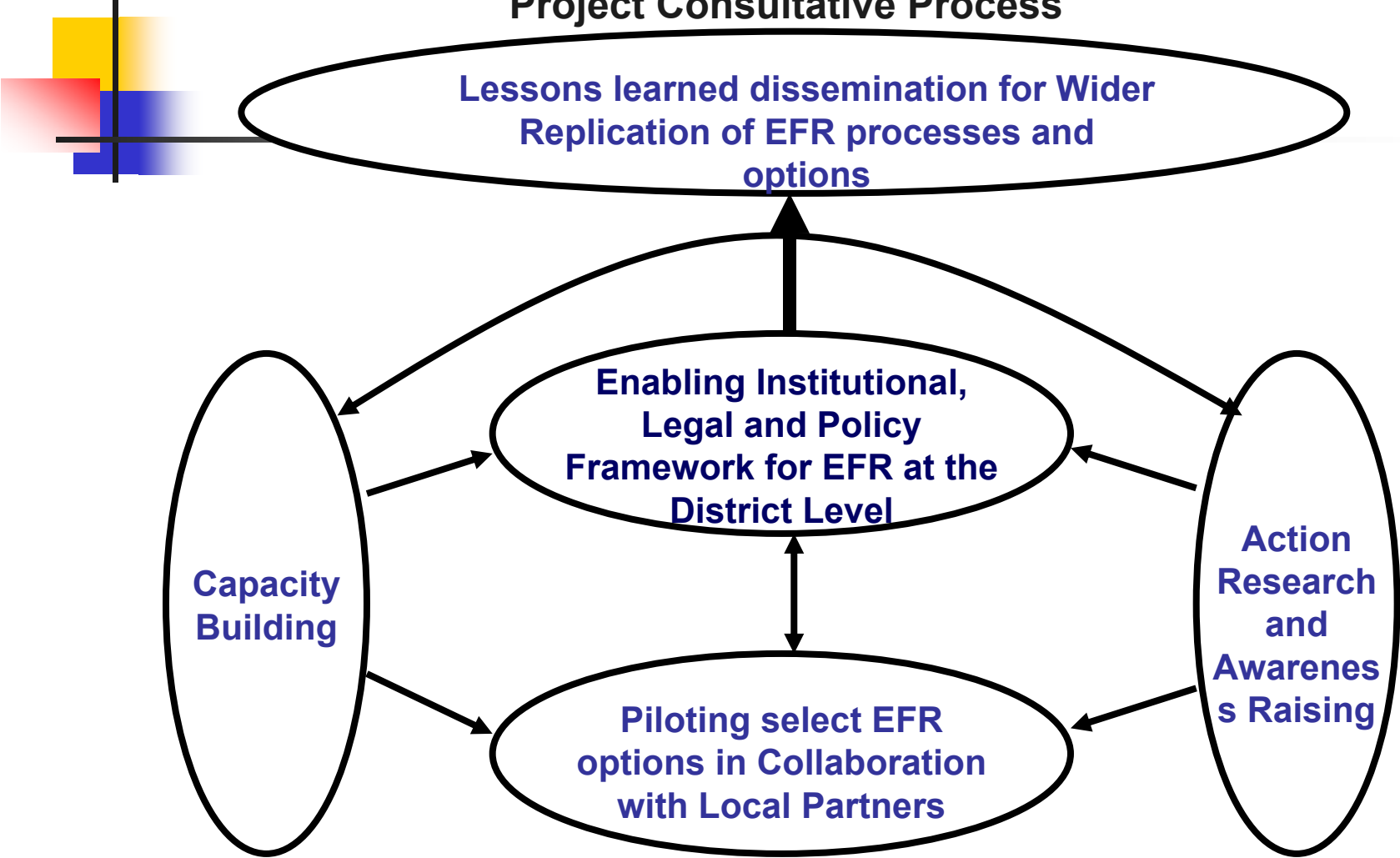
## Project Component 4

Implementation of EFR Demos

(Supported by SDC and implemented by IUCN with PIDE as partner)

# How it comes together?

## Project Consultative Process





# Research Base

---

- **Preliminary Collation of Research on Fiscal Decentralization Issues, Constraints and Opportunities and its Links to EFR Initiative for District Abbottabad: A Scenario Analysis**
- **Preliminary Collation of Research on Revenues & Expenditures, Environment & Poverty Issues, and its Link to EFR Initiative for District Abbottabad: A Scenario Analysis**



# RESEARCH METHODOLOGY

---

- *The "State of Environment and Development" and "An Integrated Development Vision" of Abbottabad district of IUCN – Data up dated*
- *Secondary data*
- *PRA Tools – Stakeholder meeting*



# Decentralization ...

---

**Decentralization provides ↑ equitable distribution in local districts, greater opportunities for empowering and serving the poorest people, and, as a result, better supports poverty reduction.**



# Fiscal Decentralization (FD)

## Public Sector Reform

- Ineffective & inefficient Governance
- Irresponsive to People's Needs
- Interjurisdictional And Interpersonal Inequality

**FD** ↑

**Efficiency**



**Transparency**



**Accountability**



## Objectives

- Economic Stability
- Sustainable Growth
- Public Service Provision Equitability Across People and Jurisdiction



# WHY DECENTRALIZATION?

## Is Decentralization Desirable?

<b>ISSUE</b>	<b>YES</b>	<b>NO</b>
<b>Stability</b>	Potentially improves Macroeconomic Governance (Shah,1997)	Inherently Destabilizing (Prud`homme,1995;Tanzi, 1996)
<b>Public Sector Size</b>	Limits the Size of the Public Sector (Marlow,1988;Grossman,1989;Ehdaie,1994)	No Significant Relationship Between Fiscal Decentralization and Public Sector Size (Oates,1985; Nelson,1986)
<b>Economic Growth</b>		Associated with Slower Growth (Xie et al., 1999; Zhang and Zou,1998)

# WHY DECENTRALIZATION?

## Is Decentralization Desirable?

ISSUE	YES	NO
<b>Demo. cratic Parti. cipation and Trans. parency</b>	<ul style="list-style-type: none"><li>- LG under under constituent pressure are managing resources and delivering services effectively (Putnam, 1993)</li><li>- Public security forces elected official appoint competent staff (Fiszbein, 1997)</li><li>- FD enhance political autonomy which in return motivate participation at local level (Int. ADB, 1997)</li><li>- Decentralization system responsive to citizen' preference (Huther and Shah, 1998)</li></ul>	<ul style="list-style-type: none"><li>- LG are more corrupt &amp; greater state capture (Bard han and Mookherjee, 2000)</li></ul>



# Main Features of Federal Fiscal System in Pakistan

- **Federation → 4 provinces, FATA & FA**
- **Most of the revenue are collected by centre – Distribution → Vertically & Horizontally**
- **Systematic (formula based)**
  - i, NFC ii, PFC iii, Fed to L and iv, L to L
- **Random transaction:**
  - i. **development/special grants,**
  - ii. **executives discretionary and**
  - iii. **parliamentarian funds, etc.**



# **EXPD. & REV. ASSIGN. AT 3-TIERS OF GOVT.**

---

- **FG → resources to provinces in the form of revenue shares, grants, straight transfers and loans**
- **Revenues → income tax, sales tax, custom duties, and excise duties**
- **Provinces Rev. → minor tax assignments i.e. agric. tax, stamp duties, motor vehicle tax, etc and others which are levied and retained by them**



# REV. ASSIG. AMONG FED. AND PROV. GOVT.

<b>Govt.</b>	<b>Direct Taxes</b>	<b>Ind. Taxes</b>
<b>Fed.</b>	Income Tax Corporation Tax Wealth Tax Property Tax	Sales Tax, Excise Duty, Custom duty, Import Duty, Export Duty, Gas & Petroleum Surcharge, Foreign Travel Tax
<b>Prov.</b>	Land Revenue, Urban Immovable property tax, Tax on transfer of property, Agric. income tax, Tax on professions and trades	Stamp duty, Motor vehicle tax, Entertainment tax, Electricity duty

# RESP. OF DIST., TEH & UC

<b>Responsibility</b>	<b>Dist./Zila</b>	<b>Tehsil</b>	<b>U. Council</b>
<b>Education</b>	<b>Yes</b>	<b>X</b>	<b>X</b>
<b>Health</b>	<b>Yes</b>	<b>X</b>	<b>X</b>
<b>Roads</b>	<b>Yes</b>	<b>Local Roads &amp; streets</b>	<b>Local Streets</b>
<b>Water</b>	<b>Yes</b>	<b>Water Supply System</b>	<b>Wells &amp; Ponds</b>
<b>Sewers &amp; Sanita.</b>	<b>X</b>	<b>Yes</b>	<b>X</b>
<b>Fire Services</b>	<b>X</b>	<b>Yes</b>	<b>X</b>
<b>Parks &amp; Play.</b>	<b>X</b>	<b>Yes</b>	<b>Yes</b>
<b>Animals</b>	<b>X</b>	<b>Slaughterhouses, Fairs</b>	<b>Cattle Ponds &amp; Grazing Areas</b>
<b>Cult. &amp; Sports</b>	<b>X</b>	<b>Fairs, Cultural Events</b>	<b>Libraries</b>
<b>Street Services</b>	<b>X</b>	<b>Street Lighting, Signals</b>	<b>Street Lighting</b>



# RESP. SHARED BET. DIFF. TIERS OF GOVT.

**With the passage of time, FG has overstressed itself into several matters that are purely the subject of lower tiers mainly due to political reasons.**

**Table: % share R&E of Diff. Tier of Govt.**

<b>Tier of govt.</b>	<b>Rev. share</b>	<b>Exp. share</b>	<b>Surpl./ defi.</b>
<b>Nation.</b>	<b>90.8</b>	<b>67.1</b>	<b>23.6</b>
<b>Prov.</b>	<b>4.8</b>	<b>28.8</b>	<b>-23.9</b>
<b>Local</b>	<b>4.4</b>	<b>4.1</b>	<b>0.3</b>



# POLITICAL ECONOMY OF FISCAL TRANSFERS

- **Sole criteria for NFC is pop. Allocations → politics.**
- **An ↑ in overall distrib. of resources → ↑ generation of resources → proportionally remains. The prov. % share of NWFP awards is ↓.**
- **Complaints from NWFP govt. regarding the share of royalties, mainly bec. the Fed. and NWFP govt. have diff. political background.**
- **Special devel. funds/grants, random transfers under the control of PM, P, CM, Gover., → disbursed on political basis w/c are even much ↑ than the allotted resources of a district.**



# INFLUENCE AT THE PROVINCIAL LEVEL

- PFC → 50, 25 & 25 % on population, backwardness based on multiple indicator cluster survey (**income, drinking water, education & literacy, child survival & nutrition, immunization & EPI (Children up to 5 year of age) with equal weight**), and lag in infrastructure (LII)
- LII Peshawar → 2.10% ↑est, Tank 0.5%, Abbottabad 0.94% (24 Districts)
- Backwardness & LII → Peshawar = ↑est (2.78%) and Chitral the lowest (1.27%) while Abbottabad 1.5%



# Budget and Revenue of Abbottabad District

Amount released by finance department to  
district Abbottabad 2005-06 (Rs. Million)

Salary	Non Salary (Other)	Non Salary (Elect.)	Develop	Zila Tax	Canton ment
1087.82	45.873	24.768	27.192	6.948	4009.1
91 %	4 %	2 %	2 %	1 %	3.4

## Own Receipt

Total Rs. 3.2 (Millions)

Income from Rest Houses, mutation, export tax share,  
commerce & trade, education & hospital entry nominal  
fees, C&T.



# **MAJOR ISSUES IN FD ...**

---

- **↑ fiscal deficits**
- **Poor revenue collection/mobilization,**
- **Persistent trend of centralization,**
- **Massive vertical imbalances bet. Fed. & Pro. Govt. (i.e. very large gaps bet. Pro. Gov.s' expe. and own revenues, w/c have to be made up by means of fiscal transfers from the fed. Govt.), and**
- **Lack of accountability of the public sector**
- **Local Government Elections - non-party**



## **... MAJOR ISSUES IN FD**

---

- **Halting and reversing the envir. degradation issues**
- **Efficiency related issues – Economic efficiency – Technical and allocative efficiency**
- **Equity related issues**
- **Effectiveness related issues**
- **Budgetary Process Pro-poor and Pro-environmental**



# Other issues ...

---

- **Limited managerial authority of Local Govt.**
- **Limited community involvements in service delivery.**
- **No resource mobilization at local level**
- **Friction bet. Prov. & Dist. Govt. over devel. projects.**
- **Violation of Rules of Business by all parties.**
- **Encouragement of regionalism-loss of national cohesion.**
- **Policy constraints – power distribution**
- **Econ. & polit. factors w/c drive envir. degradation received limited attention.**



# Opportunities

---

- **Δ in electricity tariff rates and improved collection - pilot examples of more effective collection of irrigation costs and more markt. based fuel prices.**
- **Water, sanitation and solid waste services**
- **PFC resources award criterion is better than the NFC w/c - Backwardness principle five indicators i.e. income, drinking water, education & literacy, child survival & nutrition, immunization & EPI (Children up to 5 year of age).**
- **Cater envir. & poverty as separate indicator.**



## **... Opportunities**

---

- **New tax avenue, better tax collection and recovery of user charges.**
- **Local revenue mobilization – property right.**
- **Zila and town councils are mandated to formulate local policy - mirror the real needs of the district – streamlining local resources effective and efficiency.**



# Findings and Conclusions

---

- **Devolution of power and decentralization of resources offers many opport. in the shape of hopes for empowerment of people and resolution of their local problems at local level.**
- **Formulation of new NFC award on multiple basics.**
- **PFC should be implement on its true sprit. Should include more indicators.**





## **... Findings and Conclusions**

---

- **The resource pie has been increasing at a systematic pace due to the large reliance on the indirect taxes.**
- **Clearly defining the roles of each tier of the government and giving the required resources (both human and financial) to them for their planning and development autonomy.**
- **Devolution of power to some extent but devolution of resources?**



# Recommendations

---

**International experiences must be incorporated in the resource distribution formula (NFC award)**

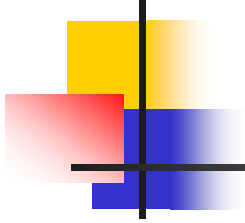
- **Backwardness and development gap.**
- **Inverse income distribution (rural urban income disparity).**
- **Natural resource endowment.**
- **Revenue generation/revenue collection.**
- **Population density.**
- **Poverty.**
- **Area**
- **Non-formula transfers.**
- **Environmental consideration**



# Recommendations ...

---

- **Fundamental tax reform - Taxes on air and water pollution could generate substantial revenue for the economy - PPP**
- **Best management practices (BMPs)**
- **Mainstreaming EFR in Social, NRM and Economic and Development Sectors**
- **Planned EFR Research Studies**



**THANK YOU**

**for your Patience**