

Environmental Finance features
Giving credit to water benefits

12 February 2013

A novel partnership is bringing lessons from the carbon markets to the challenge of financing water projects in developing countries. **Sascha Lafeld** and **Jacob Bourgeois** explain the Water Benefit Certificate initiative.

“We can’t rely on water supplies just being there as they were in the past,” says a smallholder farmer in parched central Maharashtra. “I had to drill 11 times in search of water to irrigate my land, at considerable cost, before I was successful. Who knows how long it will last before I am forced to drill again?”

Some two-thirds of India, a country that remains a land of farmers, is water scarce, with annual water supplies below 1,000m³ per person. This is a problem that is becoming depressingly familiar to farmers, businesses and individuals around the world, with available water supplies under ever-rising pressure from expanding human populations.

By 2025, the UN’s Food and Agriculture Organization estimates that 1.8 billion people will be living in regions with absolute water scarcity, with less than 500m³ available per person. Along with a decrease in available supplies, water quality is also under pressure. The World Health Organization estimates that more than 2.5 billion people lack reliable sanitation facilities.

Against this backdrop, new collaborations, technologies and business models are needed. Companies have become more aware of water-related risks in their own operations and supply chains, and those that ignore these threats face uncertain growth prospects as well as reputational risk. In an effort to engage with communities on water issues and promote sustainable development, many firms are engaging in water-related initiatives beyond their own watersheds as part of a broader water stewardship strategy.

The Carbon Disclosure Project’s 2012 Water Disclosure Report found that 74% of responding companies engage in such initiatives by funding projects that promote the adoption of water-efficient technologies, improve the quality of existing water supplies or supply fresh drinking water to communities.

While it is encouraging to see businesses active in water projects on such a wide scale, the existence of so many parallel initiatives begs several questions. Are their impacts measurable and comparable? How can the quality of these projects be assured and credibly communicated to the public? And what measures are in place to ensure that project benefits are long-term rather than one-off?



The finance needs to flow first

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In 2011, environmental asset management company First Climate set up Water Benefit Partners as a public-private partnership (PPP) to investigate these questions. The PPP brings together the Swiss Agency for Development and Cooperation (SDC) with corporate partners including Nestlé and Bayer, technical advisers such as SGS and Markit and an advisory board composed of WWF Switzerland and the Gold Standard Foundation.

The partners are developing a novel certificate-based initiative – the Water Benefit Certificate (WBC) mechanism – that addresses these concerns. The idea behind the WBC mechanism is to provide incentives for financing water projects around the world through the certification and sale of the project's water benefits in the form of WBCs.

The WBC application and verification process borrows heavily from the certification cycle used to develop carbon projects. First, projects must be developed using a methodology – approved by the Water Benefit Standard (WBS) – to quantify the water benefits that the project generates.

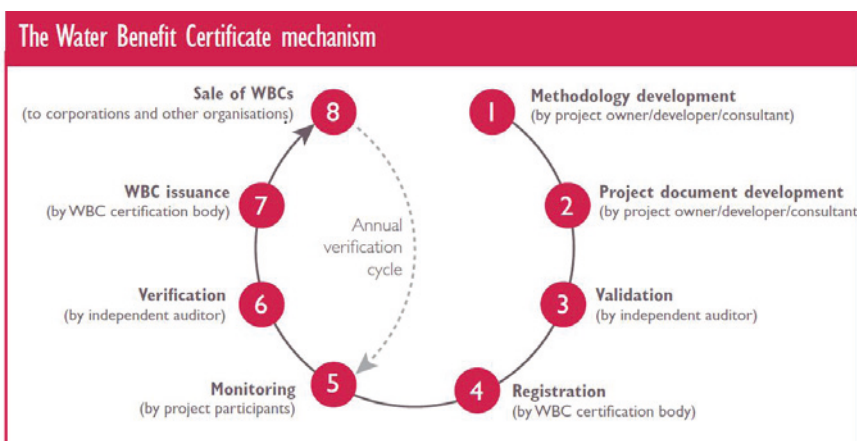
The accompanying documentation is reviewed twice: first by a third-party auditor and then by the WBS administrator, acting as the mechanism's regulator.

If applications are approved and registered as official WBC projects, they must undergo an annual cycle of monitoring and verification, after which the WBC Standard administrator may issue the certificates. Each WBC certifies that 1,000m³ of water has been saved, purified or supplied by a project activity during a specified year, and these certificates can be sold to interested buyers who wish to support the project.

Based on a market approach, the application and verification process under the WBC Standard will facilitate additional, beyond business-as-usual investments in water projects, especially in areas where water-stress and water quality issues are particularly pressing, and finance is urgently needed.

Securing financing for water projects through WBCs offers a number of advantages compared with official development assistance (ODA) and donor-based funding. Firstly, WBCs are designed to promote long-term project financing. Projects may last for a maximum of 10 years, and WBCs are issued annually only after the intended water benefits have been verified. This provides project developers and participants with the right incentives to sustain their projects over time.

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Secondly, water projects funded by WBCs are highly credible, because multiple steps in the application process are checked by independent and internationally recognised third-party institutions. This not only ensures that the water benefits are delivered as promised, but also that projects meet stringent sustainability criteria and address all stakeholder concerns during each year that the project operates. This guarantees that long-term problems that were not foreseen at

the time of project implementation can be identified and resolved at any time throughout the funding period.

Finally, the WBC mechanism ensures that water benefits are standardised and transparent – with each certificate representing a given volume of water saved, purified or supplied. In addition, all projects and their documentation will be available on the WBC registry, allowing purchasers to select the most appropriate portfolio of projects, which enhances their suitability as investment instruments for a wide variety of potential buyers. These could include private corporations, public institutions or individuals who want to help address global water problems.

The complexities of managing water made it necessary from the very beginning to receive input and criticism from a wide variety of participants in the private, public and NGO communities. The PPP partners were therefore selected based on their track records in the sustainability community to build a diverse body of stakeholders. Technical advisers at LimnoTech and SGS have also been intimately involved with resolving contentious issues throughout the development of the mechanism.

The role of the Gold Standard Foundation in particular has been instrumental in developing the mechanism. The certification cycle of WBC project activities largely mirrors that used by the Gold Standard Foundation to certify high sustainable development impact carbon projects, particularly the crucial aspects of monitoring sustainability and implementing a continuous feedback loop from project participants and other stakeholders. Its experience in the carbon market and extensive network of NGOs and technical experts give it credibility and make it ideally placed to take over administration of the WBC Standard once it is fully operational.

Despite these many advantages, one of the major challenges of developing a universal mechanism to measure water benefits is how to deal with the very local conditions in which water issues are embedded. Unlike carbon, which is a harmful global pollutant, water is inherently a local resource, such that a cubic metre of water from a project in Canada is qualitatively vastly different from a cubic metre of water from a project in the Sahel. Water has value on multiple levels, ranging from economic to social to cultural, presenting a major hurdle when it comes to generalising these benefits into one certificate.

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To meet this challenge, we applied lessons learned from the voluntary carbon market. WBCs will represent one universal volumetric amount of water regardless of project type and size, but the price per WBC shall fluctuate on a project-by-project basis depending on its unique characteristics and the willingness to pay on the part of the purchaser. This will ensure that small volume, high-impact projects will receive the funding that they need on par with large-scale water projects.

One such project was selected by the Water Benefit partners as its first pilot. In partnership with International Development Enterprises of India (IDEI), the pilot project supports the adoption of IDEI's KB Drip Irrigation technology among Indian smallholders. The WBC mechanism will promote the use of a more water-productive – but relatively new and underutilised – irrigation technology, which delivers a 30–70% reduction in water use, depending on the crop.

With the involvement of more than 40,000 smallholders, working plots of less than five acres, this project has huge potential to dramatically increase water productivity on a wide scale among a segment of the population that normally would not have the financial means to make the initial investment. At the same time, farmers can realise an increase in their incomes, allowing them to escape poverty and improve the lives of their families. The aim is to issue the first WBCs for this project by the end of 2013, and to further support the distribution of drip irrigation systems with the funds raised through their sale.

Rolling out the WBC mechanism for general use to support this and other projects will be the main challenge with the planned second phase of the PPP. In addition to the water productivity project in India, First Climate Markets and the Gold Standard Foundation will develop up to three new pilot projects and methodologies covering different project types and geographical locations.

This will both increase the total supply of WBCs while also enhancing the diversity of projects available to purchasers. Getting new corporate partners on board for the second phase of the PPP will be a vital step in building a functioning market for WBCs.

In addition, it will be up to First Climate and the Gold Standard Foundation to enhance the administrative infrastructure for WBCs. This includes creating an electronic registry for available projects, setting up a WBC secretariat and support infrastructure capable of ensuring their quality, and completing a full transition of administrative control to the Gold Standard Foundation.



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The importance of addressing the world's future water needs in an era of scarcity cannot be understated, and the recent attention given to water issues through various corporate social responsibility (CSR) strategies indicates that firms are aware of these risks.

However, it is vital that CSR-driven initiatives deliver the benefits that they promise, and that these benefits are effectively communicated to the public at large to generate greater recognition of the problems at hand and their solutions. Without this credibility, such measures to meet water challenges will be seen as talk rather than action. What WBCs offer is the opportunity for anyone to access this credibility, and to engage directly with water issues that will certainly grow in importance in the years to come. EF

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