

**PROJECT INFORMATION DOCUMENT (PID)
APPRAISAL STAGE**

Report No.: PIDA763

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Project Name	Sustainable Financing for Biodiversity Conservation and Natural Resources Management (P127490)
Region	SOUTH ASIA
Country	Bhutan
Sector(s)	Forestry (60%), General agriculture, fishing and forestry sector (40%)
Lending Instrument	Specific Investment Loan
Project ID	P127490
Focal Area	Multi-focal area
Borrower(s)	Ministry of Finance
Implementing Agency	Bhutan Trust Fund for Environmental Conservation
Environmental Category	B-Partial Assessment
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Decision	

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I. Project Context

Country Context

Forests, alpine regions, protected areas and other natural habitats are among Bhutan's greatest assets. They represent the vast repository of biodiversity and their largely pristine condition reflects the country's commitment to maximizing Gross National Happiness (GNH). As the philosophy which forms the cornerstone of Bhutan's development, GNH is being implemented since its introduction in the 1970s. Centuries of isolationism, a small population and topographical extremes helped maintain one of the most intact ecosystems in the world. Environmental conservation is featured explicitly in Bhutan's constitution which prescribes the maintenance of a minimum of 60% of the country's total land area under forest cover perpetually. As a landlocked and mountainous country and a global biodiversity hotspot, Bhutan's development prospects depend upon the extent to which it can capitalize on its comparative advantage – its natural endowment. With an economy highly reliant on the sustainability of its natural resources and a strong commitment to conservation, Bhutan's balanced approach to development calls for considerable investments in its natural assets in order to ensure the country's comparative advantage.

II. Sectoral and Institutional Context

Bhutan entered the current millennium with most of its natural endowments intact. It ranks among the world's top ten countries in terms of species density (i.e. the number of species per unit area). Despite its small size, the country has very high levels of biological diversity at the ecosystem, species and genetic levels. Bhutan has 72% of its land area under forest cover that includes about 50% under protected area (PA) management.

Bhutan has seen rapid growth, averaging about 8% annually during the last three decades. As development proceeds apace, Bhutan is facing pressures on its natural endowment stemming from population growth, agricultural modernization, hydropower and mineral development, industrialization, urbanization and infrastructure development. These pressures are manifested by localized deforestation, overgrazing, forest fires, and conversion of natural habitats to accommodate urbanization and infrastructure development. The use of firewood – accounting for over 57% of the total primary energy supply – and the extraction of timber for house construction may result in grave forest degradation and biodiversity loss. Overgrazing in alpine meadows could lead to a decline in land productivity and soil erosion. The depletion of biodiversity in the alpine areas and broadleaf forests compels herders to move to adjacent forests for grazing. The growth in road construction and electrification of towns and villages has brought additional demographic pressures on the surrounding natural resources. In addition, the country is confronting emerging environmental challenges in the form of pollution, waste and climate change.

The environment takes a central place in Bhutan's development priorities but limits to conservation efforts have been significant. An inadequate system of prioritizing the wide range of environmental needs, weak institutions and capacity as well as limited financing underlie the challenges to biodiversity conservation and natural resource management (NRM). Today, the most pressing needs include: (i) protection and management of areas adjacent to traditional protected areas (PAs); (ii) management of forest resources for sustainable production and utilization; (iii) reduction of grazing pressures on natural ecosystems, in particular alpine meadows and associated broadleaf forests; (iv) sustainable land management (SLM) to protect the productivity and stability of various land uses; (v) promotion of biodiversity to support local livelihoods based on community-based NRM; and (vi) development of markets for sustainable nature tourism.

Thanks to the Bhutanese traditional beliefs and an enduring national commitment to protecting the environment, the country has a good track record of implementing conservation and NRM activities. In the early 1990s, the Royal Government of Bhutan (RGOB) recognized the serious financial, institutional and human resource constraints in implementing conservation programs due to the country's small population, limited economic activity and hence low government revenues. The Bhutan Trust Fund for Environmental Conservation (BT FEC) was established in 1992 in an effort to secure a mechanism for sustainable financing to preserve the country's rich biological diversity. RGOB sought financial support from the Global Environment Facility (GEF) and other donors to capitalize BT FEC. A GEF grant of US\$10 million for a project administered by the World Bank was provided to BT FEC to assist Bhutan's conservation goals through the trust fund mechanism. Implementation took place in 1992-97.

The grant launched the first trust fund set up under GEF and demonstrated the feasibility of a trust fund mechanism for providing potential long-term support for biodiversity conservation. With the GEF grant, RGOB attracted additional funds for BT FEC consisting of US\$10 million from the World Wide Fund for Nature (WWF) and US\$10 million from bilateral donors. Following

BT FEC's initial capitalization, the Fund's Board developed and approved the first strategy and action plan in 1997. The implementation of the first plan led to improvements in BT FEC's administration, financial management, fund raising capacity as well as its grant funding processes. Under the 1997 plan, BT FEC's grant-making focused on establishing and financing a new network of PAs. With BT FEC financing of more than US\$7 million in grants, RGOB succeeded to establish a new PA system of five national parks, four wildlife sanctuaries and one nature reserve that is representative of the country's ecosystems. While the PAs are not fully functioning even today, all of them have PA management plans in place and are at varied stages in implementing those plans with trained staff on the ground.

The GEF grant helped to create a permanent, well capitalized institution. BT FEC's capital (in cost value terms) grew to US\$41.1 million as of June 30, 2011 owing to the Board's and the Secretariat's careful management of investments and administrative spending. By comparison, BT FEC's grant-making performance has been quite modest. The funds from investment earnings available to finance conservation during the 15 years since BT FEC was capitalized amounted to about US\$27 million. On average, slightly less than US\$2 million per year were available for distribution as grants but actual grant making averaged only US\$0.7 million per year.

Recognizing the need to bolster its operations and capacity, BT FEC commissioned an assessment of its functioning in 2012. The assessment report – that was carried out by a consultant with extensive experience in evaluating the effectiveness of conservation trust funds – concluded that the modest pace of grant-making reflects the limits to the Fund's operational effectiveness and sustainability. Moreover, the impact of its grant-making has been diffused and difficult to measure because the selection of individual projects for funding has been largely ad hoc, non-transparent, and opportunistic. The Fund's constraints include the: (i) lack of a clearly articulated long-term strategy; (ii) absence of a transparent, open and competitive grant-making process; (iii) lack of civil society engagement in defining conservation priorities; (iv) limited technical capacity for monitoring and evaluation (M&E) of the conservation impact of BT FEC grants; (v) absence of arrangements for analyzing and utilizing lessons and experiences; (vi) limited capacity to review its investment management strategy and performance; and (vii) absence of legal instruments to allow for the generation of non-budgetary resources for self-sustaining management of PAs, such as revenue from payments for environmental services, tourism and concession fees.

RGOB made progress in building up the PA network with BT FEC's support along with financing from the national budget and external donors. However, the rural population in and around the PAs aspire to reap the benefits of economic development. The demand for electricity and roads by the local people intensified with the advent of constitutional democracy in 2008. With the socio-economic development needs of a modernizing and growing population, BT FEC has a greater challenge at hand. It needs to gain greater prominence, authority and credibility as an effective and reliable institution for sustained funding of conservation activities and for setting annual conservation priorities. Attaining such leadership would require BT FEC to consolidate its capacity by enhancing the transparency of its grant program, working with partners to develop programs that would best address Bhutan's conservation priorities, encouraging the creation of indigenous capacity to design, manage and monitor programs and improving the M&E of the impact of its grant program on conservation outcomes.

BT FEC developed its second strategy – called the Strategic Plan 2010-15 – that provides the basis for the much needed expansion of the Fund's role. The Plan covers seven program areas (described

in Annex 2). Those seven areas and associated actions are comprehensive in scope. The diversity demonstrates the challenges facing BTFEC which has tried to maintain the flexibility to address a large range of environmental issues. The Plan is rather ambitious in what it is trying to achieve in a five-year period, especially as it presents a number of new program areas for grant-making and proposes new ways of doing business. While the Plan has been developed, the project provides an opportunity for the Plan's refinement to make its execution more efficient and capable of demonstrating impact. Such fine-tuning would allow BTFEC to respond to the country's changing environment priorities and recent political transformation.

The proposed project aims to help BTFEC implement an updated strategic plan by introducing improvements to the Fund's grant selection criteria, procedures for the evaluation and assessment of the impacts of its grants, transparency, accountability and financial management.

In parallel to the planned overhaul of BTFEC's operations during the proposed project implementation period, RGOB has embarked on a program to intensify its conservation efforts in the high altitude northern areas (HANAS). This region forms part of the fragile eastern Himalayan ecosystems. RGOB feels that the adoption of the BTFEC grant mechanism, including its policies and processes, will strengthen the prioritization and management of conservation activities in HANAS. Therefore, the GEF funding for the conservation activities in HANAS will be channeled through BTFEC and the latter will manage the selection and the monitoring and implementation of the HANAS grant proposals which are subsumed under the project's second component.

Located between 3000 and 5000 meters in altitude, the alpine and sub-alpine meadows and temperate broadleaf forests in HANAS support a globally important biodiversity. Three of Bhutan's ten PAs are located in the high altitude northern region and they are ecologically linked to the PAs in the mid-hills and duars (foothills) especially by animal migrations and hydrological processes. HANAS has globally significant natural habitats for charismatic and iconic species such as the tiger, snow leopard, takin, blue sheep and several species of hornbills, pheasants and large raptors. Ecologically, the highaltitude ecosystems maintain critically important ecological links to ecosystems lower down the mountains and far beyond Bhutan's southern borders. The river systems that originate from the glaciers and water towers of Bhutan's mountains sustain biodiversity as well as human lives and livelihoods in the mountains, the Gangetic Basin and the mangroves of the Sunderbans mangroves.

It is estimated that around 65,000 people (roughly 10% of Bhutan's total population) live and eke out a livelihood in HANAS. The temperate broadleaf forests and other alpine ecosystems are under threat from population growth, patterns of agricultural cultivation, livestock grazing and urbanization. Despite the small number of inhabitants in the HANAS region, population growth in the subsistence-based rural economy contributes directly to deforestation through the increased consumption of fuel wood. The area under cultivation is increasing with the most suitable land already under agriculture and the potential for additional allocations to agriculture is likely to be at the expense of the forests that lie immediately above the remote villages. About 90% of the rural households own livestock and their dependency on PAs, alpine meadows and surrounding forests for grazing livestock adversely affects the HANAS ecosystems. This is further compounded by the fact that alpine meadows – the traditional grazing grounds in the high mountain areas – are rapidly degrading and becoming infested with weeds, forcing herders to move their livestock into surrounding PAs, corridors and forests for grazing.

III. Global Environmental Objective(s)

The project development objective (PDO) is to improve the operational effectiveness and institutional sustainability of the Bhutan Trust Fund for Environment Conservation. The PDO is also the global environmental objective (GEO).

IV. Project Description

Component Name

Component 1: Enhancing the operational effectiveness and sustainability of BTFEC

Component 2: Improving conservation management of the high altitude northern areas (HANAS) landscape in Bhutan (including protected areas and associated methods, forests and agricultural systems)

Component 3: Mainstreaming of conservation and sustainable forest and natural resource management approaches in national policies, strategies and plans

V. Financing (*in USD Million*)

For Loans/Credits/Others	Amount
BORROWER/RECIPIENT	1.50
Global Environment Facility (GEF)	4.08
Local Communities	0.30
Total	5.88

VI. Implementation

The implementing agency for the proposed project is BTFEC. As previously stated, it was established with support from a GEF grant administered by the World Bank during 1992-97. The Fund has developed into a permanent and well-capitalized institution. It has made strides in the areas of conservation funding, financial management and grant-making. The proposed project will further enhance the implementation capacity of BTFEC through technical assistance, training and operational support to modernize its grant-making program. Such support would entail: (i) ensuring a transparent, open and competitive system for grant prioritization; (ii) strengthening BTFEC's capacity for M&E of the impact of its grants; (iii) improving investment management and performance evaluation; and (iv) enhancing civil society participation in grant prioritization and decision making. In addition to modernizing the grant award mechanism and administration and strengthening M&E capacity, revisions to various sections of the Operations Manual will be supported under Component 1 of the project. BTFEC will be fully responsible for financial management oversight, grant making and monitoring of project outcomes and impacts.

The review and approval of the proposals for HANAS under Component 2 will follow BTFEC's grant-making process. For the most part, the institutions within the Ministry of Agriculture and Forests (MOAF) will be responsible for the implementation of Component 2 activities within HANAS in cooperation with NGOs, local, district (dzongkhag) and sub-district (geog) administrations as well as local communities. The grants will be implemented largely by the departments of forestry, wildlife conservation, and livestock of MOAF, all of which have extensive experience working on World Bank and other donor-supported programs. Dzongkhag and geog administrative bodies, non-government organizations and local community organizations will participate in grant implementation.

The specific strategy and activities to be financed under Component 3 can be developed on the basis of lessons from and experiences with the implementation of Component 2 grants. The leading proponents for Component 3 will be MOAF's departments. The latter will prepare initiatives for funding that will be submitted to BTFEC, which in turn, will manage the selection, M&E of the precise set of activities that will be supported by BTFEC grants.

Project Components:

Component 1: Enhancing the operational effectiveness and sustainability of BTFEC (US\$0.8 million)

The objective of Component 1 is to support BTFEC in carrying out the update and implementation of the Strategic Plan by adopting more modern governance and business practices and ensuring the adequacy of its resources and tools going forward. With a view to greater operational effectiveness, BTFEC's Board has endorsed the following improvements: (i) increase and diversification of BTFEC Board representation; (ii) prioritization of interventions in the seven program areas of the Strategic Plan 2010-2015; (iii) preparation of a sustainable plan for the PA network; (iv) creation of a performance-based system to monitor and evaluate the impacts of BTFEC's grant program and institutional performance; (iv) modernization of the grant-making process towards efficiency, equity and transparency; and (v) review of options for BTFEC's future investment management.

To ensure that BTFEC has the resources and tools for implementing change, its Board agreed on the following changes: (i) recruitment of additional staff to share the numerous operational responsibilities and tasks; (ii) engagement of short-term consultants for legal advice on changes to BTFEC's structure, preparation of a sustainable financing plan for the PA system and introduction of modern operating systems and processes; and (iii) development of new business lines to expand BTFEC's management of funding for conservation initiatives.

Specifically, Component 1 will finance training, technical assistance, equipment and data management systems and limited piloting for updates to the Royal Charter, introduction of bylaws, prioritization of grant selection on the basis of needs, risks and opportunities, modernizing grant-making, revision of the Operations Manual, review of options for future investment management, staff capacity improvements, and development of a fund-raising strategy.

Component 2: Improving conservation management of the high altitude northern areas (HANAS) landscape in Bhutan (including protected areas and associated methods, forests and agricultural systems) (US\$2.84 million)

This component aims to demonstrate BTFEC's conservation outcomes and enhance its grant-making operations. To that end, BTFEC will finance grants – on a competitive basis – that would improve conservation management in the high altitude northern area ecosystems. The conservation grants for the targeted areas will be processed and approved through BTFEC's existing grant management system. In accordance with BTFEC's grant award process, the maximum grant amount is US\$300,000 and grant proposals are considered and approved by BTFEC's Board twice a year.

Two types of grants will be provided under Component 2. The first type will support the testing and implementation of appropriate management strategies and proactive plans to anticipate and address

threats to the PA and biodiversity corridor complexes in HANAS. This would enable the conservation of broadleaf forests and other ecosystems within HANAS and help maintain their ecological integrity and the economic and ecological services they support. The activities to be supported would include: (i) review and update of existing management plans for PAs and zoning and enforcement of land-use regulations; (ii) monitoring of species of special concern, especially tigers and other charismatic species; (iii) research on critical species; (iv) engagement of local communities in habitat management and community stewardship and improved livelihoods and incomes; and (v) improved staff training and capacity for conservation. Hence, the grants would finance expert services (including community mobilization), training, workshops and equipment.

The second type of grants will support a range of community activities that aim to strengthen the adoption of: (i) sustainable agricultural land use and grazing management practices; (ii) co-management of forests and alpine meadows; and (iii) community-based ecotourism and value addition products. Grants of this type would finance goods, small works, community empowerment and training as well as other consultancies.

Component 3: Mainstreaming of conservation and sustainable forest and natural resource management approaches in national policies, strategies and plans (US\$0.44 million)

The lessons from the management of PAs and the HANAS landscape derived from the implementation of Component 2 will inform policies pertaining to key natural resource sectors, including watershed management, upland agriculture and livestock, forestry, wildlife conservation and also infrastructure development. Such learning and experience would contribute to the development and improvement of existing conservation and NRM guidelines, provide examples of good practices and support new models of integrating PAs, sustainable grazing and agricultural management approaches into sector and geog (sub-district) level planning to prevent the loss and fragmentation of forests and critical habitats. It will facilitate the replication of lessons and good practices more broadly throughout the country. The implementation of activities under this component will also be supported through BTFEC's competitive grant-making processes and systems.

At this stage of project preparation, the activities proposed for support under this component could include: (i) gap analysis of policies and guidelines on conservation management; (ii) high level exchange program with countries that implement high impact conservation policies; (iii) workshops for implementing agencies to share lessons and experiences; (iv) stakeholder meetings toward mainstreaming conservation and NRM into national policies; (v) local community consultations; and (vi) dissemination of good practices, results and outcomes stemming from the implementation of the grant-funded activities.

VII. Safeguard Policies (including public consultation)

Safeguard Policies Triggered by the Project	Yes	No
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04	x	
Forests OP/BP 4.36	x	
Pest Management OP 4.09	x	
Physical Cultural Resources OP/BP 4.11	x	
Indigenous Peoples OP/BP 4.10		x

Involuntary Resettlement OP/BP 4.12	x	
Safety of Dams OP/BP 4.37		x
Projects on International Waterways OP/BP 7.50		x
Projects in Disputed Areas OP/BP 7.60		x

VIII. Contact point

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