Inter-American Development Bank
Regional Policy Dialogue

Natural Disasters

INSTITUTIONAL BUDGETARY RESOURCES, SOURCES OF PUBLIC AND PRIVATE FUNDS FOR FINANCIAL PROTECTION AND RISK REDUCTION INCENTIVES

Situational Analysis

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OBSTACLES AND ADVANCES

- ✓ *Although significant changes have occurred over the last years in risk management legal and institutional frameworks, it is difficult to find cases of financial measures that sustain such changes in resource poor countries.*
- ✓ *This is a complicated situation given that although in many countries consciousness as regards the need for adequate institutional frameworks has partially increased, it is very worrying that there is little budgetary resource availability to support such changes.*

OBSTACLES AND ADVANCES

- ✓ *This situation is reflected in the fact that when we attempt to obtain information from institutions or from budgetary authorities as regards expenditures on risk management they are either non existent or are diffuse or unavailable except in a few cases.*
- ✓ *Investments in prevention and mitigation are many times mixed up with other non related investments, including normal development actions of the institutions.*

OBSTACLES AND ADVANCES

- ✓ *In general, information systems or agencies that collect and process information and establish the terms for the provision of information by institutions do not exist. The availability of information would allow the establishment of priorities and the allocation of resources to higher risk areas whilst at the same time permitting an adjustment of on going national and sub-national risk management programmes.*
- ✓ *In the countries there are not deep financial markets and a culture of insurance. This makes difficult the pooling of risks and using of the market mechanisms to transfer losses to specialized agents in the matter.*

Regular and exceptional financial mechanisms

- ✓ *Risk reduction activities are carried out in a majority of the countries using normal institutional budgetary allocations without the existence of specific allocations for these tasks. Regular operational resources are in general insufficient given the range of things to be done and these include, at times, diffusion, education and public information.*
- ✓ *Good practice would suggest the need for specific minimum budgetary allocations and indications as to their permitted use.*

International Cooperation

- ✓ *The high levels of dependency on external international resources for risk management activities may be creating a vicious circle in the long run. This dependency makes risk management unsustainable.*
- ✓ *This dependency and restrictions or directives on resource use by external agencies has been a major factor in explaining the lack of national policy frameworks in many countries that give coherence, order and meaning to the large quantity of projects that are executed.*

Special risk reduction funds

- *In general, funds for attending emergencies and for reconstruction have been established. But, similar funds do not exist in general for risk reduction. FOPREDEN is the exception.*

  This fund finances three basic areas :
- *Risk identification*
- *Risk mitigation or reduction*
- *Development of a risk prevention culture*

Budgetary decentralization and co-financing arrangements

- *The most adequate way of promoting risk management would be, on the one hand, to define a fixed value for conditioned intergovernmental transferences without institutional contributions and/or by means of subsidies or contributions with determined levels of institutional contribution.*
- *In order to promote risk reduction in a rational manner we need to recognise the existence of large differences in risk levels and available resources at the sub national scale.*
- *Fiscal decentralization is typified in most countries by a high concentration of resources in a few municipalities and departments. This leads to a high concentration of fiscal income.*

Budgetary decentralization and co-financing

- *The possibility exists of co-financing projects for risk reduction and covering the costs of responding to emergencies based on a categorization of municipalities. This can be done using a fixed percentage which would depend on the fiscal efforts made at the particular territorial level.*
- *It is important to identify investments coming from municipal resources and unspecified transferences from the national level such that there is some notion of the investment in risk management which has not been identified as such to date.*

Emergency and reconstruction funds

- *Reserve funds have in general been the most used financial mechanisms in the different countries. But it is obvious that the resources allocated to these funds have been insufficient.*
- *These reserve funds should accumulate resources in order to face up to the impacts of small disasters. Given that these are often recurrent in their incidence and systematically affect the same poor and vulnerable population, they require compensatory mechanisms to guard against the dramatic accumulative effects they may have on such population.*

Reconstruction

- *Many governments have had to support the losses associated with large disasters. In general, these losses have been compensated or covered with donations from foreign governments and international agencies, emergency loans given by international banks, the reallocation of existing loans, budgetary reallocations, taxes and insurance.*
- *A non permanent institutional structure established to deal with reconstruction does not have to be opposed to existing organizational set ups. Such an organization can appropriately coordinate a reconstruction process if it is given the right instruments and technical capacities in order to achieve its objectives within the existing organizational set up.*

Financing and risk transference

- *There is no precise data on the percentage of public buildings that are financially protected against disaster losses. But, it is generally accepted that this percentage is very low or moderate and that infrastructure is in general completely unprotected.*
- *In the majority of countries no calculation of probable losses is made as a permanent part of the budgetary process. Thus, information is lacking in order to evaluate alternatives for reducing or financing such losses. Moreover, this also contributes to the fact that risk reduction policies do not receive the attention they deserve and require.*

Financing and risk transference

- ✓ *It is vitally important that national and regional governments be aware of the need to adopt measures to diversify risk, especially those related to possible damage to physical infrastructure. Insurance allows a reduction of the fiscal burden once a disaster occurs.*
- ✓ *Protection mechanisms can be established once a definition of the State responsibility has been established and its fiscal capability determined. The State is basically responsible for infrastructure and public buildings as well as low income families who do not have resources to cover insurance.*

Summary of good practice

The best mechanisms identified in the region for improving the allocation and sustainability of risk management investments are :

- ✓ *The definition of a minimum budgetary allocation for sectorial and territorial agencies, accompanied by a clear specification of the types of use that may be given to these resources.*
- ✓ *The indication that a determined percentage of conditional budgetary transferences to territorial agencies must be dedicated to risk management. That is to say, a portion of general use resources would be given a specific use. Rules and regulations should exist as to the possible uses for such funds.*

Summary of good practice

- ✓ *To create or strengthen reserve and compensation funds for emergency response, rehabilitation, and reconstruction, establishing an optimum rate of accumulation and expenditure based on calculations of the probable impacts of low probability, high impact events.*
- ✓ *Specific funds or specific sub accounts to stimulate co-financing of risk reduction projects and programmes, differentiating these from the funds available for response, rehabilitation and reconstruction*

Summary of good practices

- ✓ *Mechanisms such as insurance and risk transference, perhaps subsidized by the State, which reduce the fiscal burden when disaster occurs.*
- ✓ *Instruments for financial protection could be gradually introduced with at first modest goals but which may be widened in the future according to improvements in the economic prosperity of the country and the development of an insurance culture in the private and public sectors.*