

Greening SMEs in the EU Eastern Partnership Countries

POLICY HIGHLIGHTS

2016



EaPGREEN
Partnership for Environment and Growth



Environmental Policy Toolkit for Greening Small and Medium Enterprises in the EU Eastern Partnership Countries

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These Policy Highlights present the key findings of the *Environmental Policy Toolkit for SME Greening in the EU Eastern Partnership Countries* (OECD, 2016). It aims to help governments in the European Union's Eastern Partnership (EaP) countries (Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine) design and implement key instruments to promote environmental compliance and green business practices among SMEs using the experience of EU and other OECD countries.

The Toolkit covers three categories of environmental policy instruments:

- regulatory simplification and incentives;
- information-based tools (both offering advice and guidance to SMEs and information about their environmental performance for the public); and
- financial and economic incentives.

It draws on, among others, past OECD analysis of SME-related policies and the extensive work by the European Commission to implement the 2008 Small Business Act for Europe.

SME-specific challenges...

- Diversity and complexity of SMEs' activities
- Low awareness of environmental regulations and opportunities of green practices
- Limited capacity to consider environmental issues
- Distrust for environmental regulators and heavy reliance on professional surroundings (trade associations, suppliers, clients, accountants, etc.)
- Difficulty in accessing affordable finance.
- Concern about short-term financial profitability and reluctance to invest in green technologies.

... and opportunities

- Achieving and going beyond environmental compliance in both manufacturing and service sectors as part of greenin the economy
- SMEs driving eco-innovation and playing a key role in emerging green industries
- Potential costs savings and competitive advantage for SMEs as important suppliers of goods and services

Green practices among SMEs in Eastern Partnership countries: SME Surveys

Surveys conducted in 2014-15 in Armenia, Moldova, Georgia and Ukraine (Poltava region) of 400+ SMEs in each country covered the following sectors:

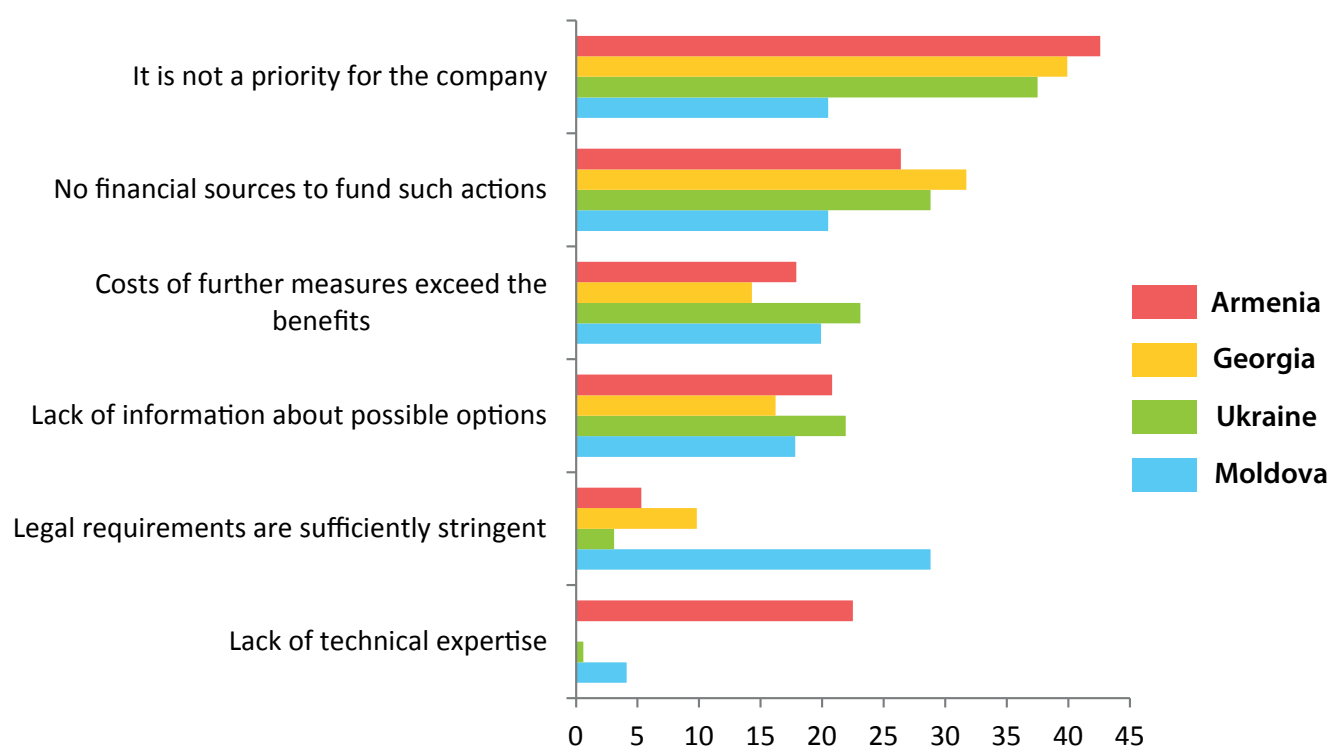
- Agriculture, fisheries and forestry
- Extractive industries (mining and quarrying)
- Food manufacturing
- Non-food manufacturing
- Construction
- Hotels and restaurants



In Moldova and Ukraine, about half of respondents contemplate going beyond the requirements of environmental legislation. The willingness to engage in green practices is much lower in Georgia (19%) and Armenia (4%). The reasons not to go beyond compliance include the lack of information about potential green practices and, more importantly, the perception of their high cost and the lack of finance to cover it. This

demonstrates the inadequate appreciation among SMEs of the economic benefits of green practices. The lack of environmental skills is considered a less important gap: SMEs see themselves as technically competent to introduce green practices. (Figure 1). Other key obstacles to engaging in green practices noted by SMEs are different bureaucratic barriers such as complex procedures and obsolete technical requirements.

Figure 1: **Main reasons for not going beyond legal requirements, percentage of respondents**



Source : Based on various OECD (2015) and (2016) publications on pilot projects in Armenia, Georgia, Ukraine and Moldova.

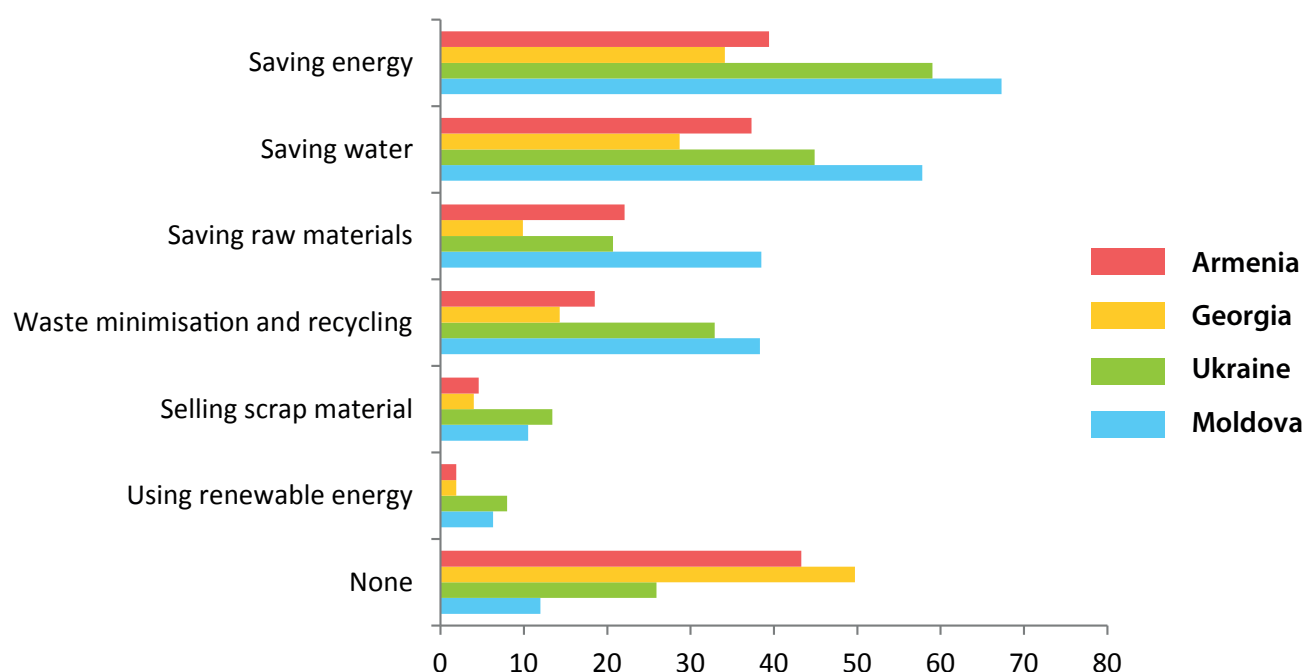


Progress and challenges in the region

A large share of SMEs in every surveyed country indicate that they are implementing energy and water efficiency measures. Actions to save raw materials and minimise

waste are also quite widespread in Moldova and, to a lesser degree, in Ukraine and Armenia (Figure 2).

Figure 2: **Current implementation of resource efficiency measures, percentage of respondents**

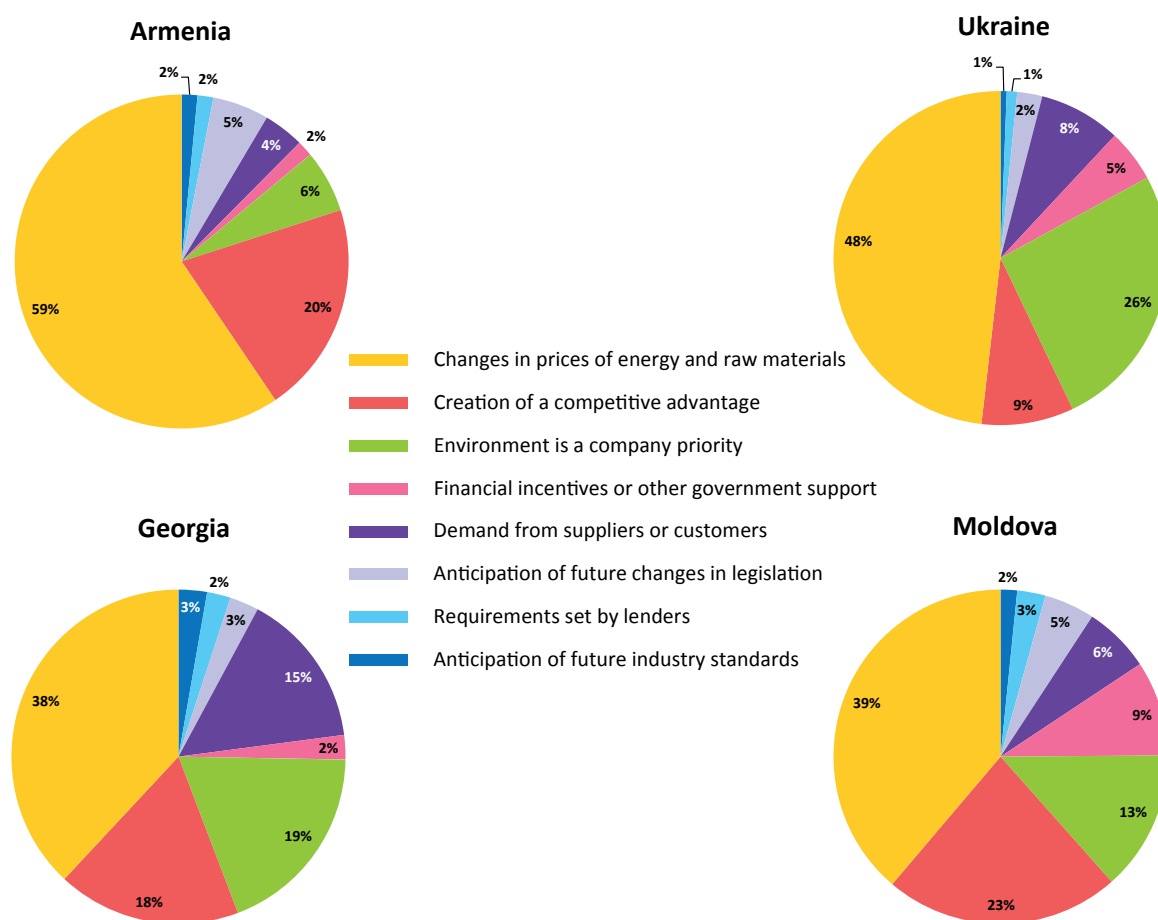


Source : Based on various OECD (2015) and (2016) publications on pilot projects in Armenia, Georgia, Ukraine and Moldova.

The current resource efficiency practices are largely driven by the growing prices of energy, water, and raw materials (as reported by an overwhelming majority of surveyed SMEs in Moldova and Armenia). A significant share of

small business are starting to realise that green practices can lead to a competitive advantage. However, the regulatory and financial incentives for SME greening are very weak (Figure 3).

Figure 3: **Key reasons for implementing resource efficiency measures, percentage of respondents**



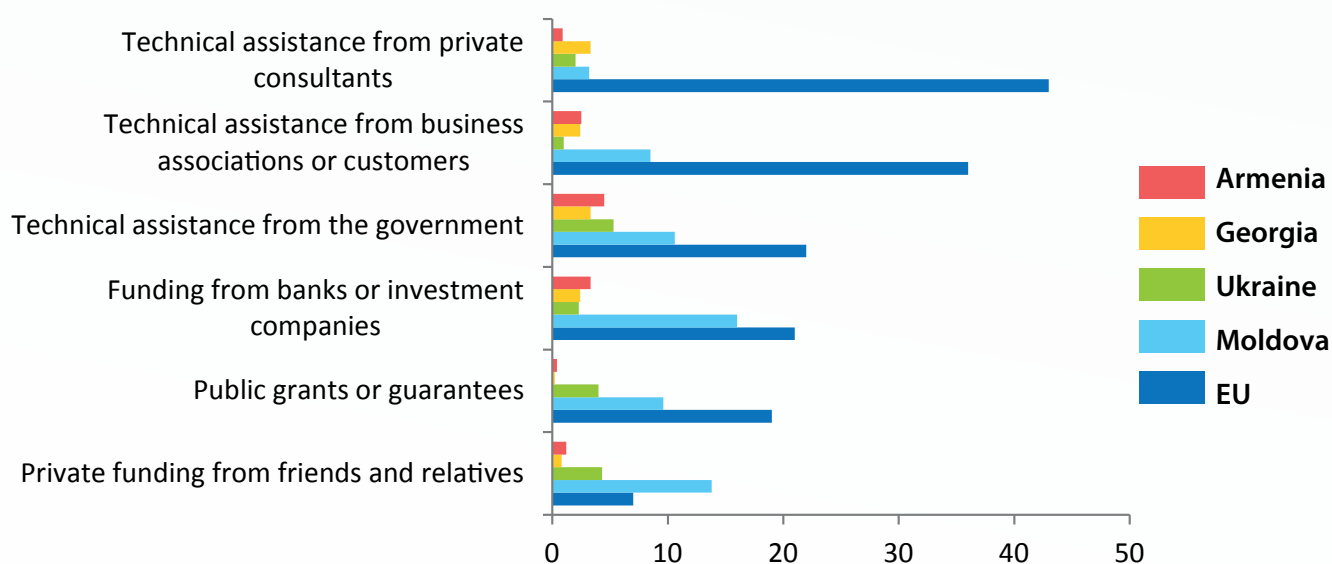
Source : Based on various OECD (2015) and (2016) publications on pilot projects in Armenia, Georgia, Ukraine and Moldova.

Less than a quarter of SMEs in Moldova, Ukraine and Georgia (and as low as 12% in Armenia) that undertake resource efficiency measures receive any technical or financial support. The larger the enterprise, the more

likely it is to receive some support, which almost never reaches micro-businesses. The lack of government support appears to represent the biggest gap, in stark contrast with the extent of public support activities in the EU¹. (Figure 4)

¹ EC (2013), SMEs, Resource Efficiency and Green Markets, Flash Eurobarometer 381, conducted by TNS Political & Social at the request of the Directorate-General Enterprise and Industry, European Commission, Brussels.

Figure 4: **Percentage of SMEs receiving support for resource efficiency actions**



Source : Based on various OECD (2015) and (2016) publications on pilot projects in Armenia, Georgia, Ukraine and Moldova.



Governments in EaP countries increasingly realise the importance of SME support policies in the context of greening the economy. Ministries of Economy in both Moldova and Armenia have introduced environmental considerations into their strategic documents on SME support activities but have not yet started the development of specific policy measures.

Environmental regulatory regimes (such as permitting and inspections) are only starting to be more flexible based on the enterprises' level of environmental risk, still leaving a heavy administrative burden for SMEs.

Environment ministries and their associate institutions provide **regulatory information** to business. Specialised environmental information centres provide assistance in understanding environmental requirements through telephone advice, workshops, and guidelines. However, these information services rarely reach smaller businesses.

EaP country governments should play a more active role in **promoting environmental sustainability and best practices**. Ministries of economy in several EaP countries (notably in Georgia) implement various information and training programmes for small businesses, but they rarely get institutionalised. Environmental authorities lack capacity to develop and implement sector-specific policies and are not engaging in environmental compliance promotion activities.

The existing **business organisations**, such as chambers of commerce and industry and employers' associations, are dominated by larger companies and do not give priority to serving the needs of small businesses. They also have little knowledge of sustainable production issues. There are very few sector-specific trade associations, and their SME membership is quite limited. This makes it much harder for the government to reach out to individual SMEs.

International donor-sponsored initiatives to promote SME green development play a substantial role in improving access to finance and know-how for SMEs in the region. While they contribute to building social and environmental responsibility in private banks, they are not sustainable in the long term.

Recommendations

There is a great variety of strategies and instruments that should be used as part of a policy mix to promote environmental compliance and green business practices, including:

- **Regulatory tools:** simplification of regulatory requirements for SMEs through standardised permits or general binding rules as well as other better regulation initiatives; offering regulatory incentives for the establishment of environmental management systems; moving towards sector-specific strategies for compliance assurance;
- **Information-based instruments:** advising individual businesses directly or disseminating guidance on environmental compliance and good

practices to a wide audience in the printed and, increasingly, electronic form; introducing sector-specific certifications and eco-labels as well as other environmental recognition awards;

- **Economic incentives:** grants, low-interest loans and tax incentives for businesses willing to go beyond compliance and invest in greener technologies; encouraging supply chain pressure from larger companies and exerting it through green public procurement.

Making regulatory tools smarter

There is a marked trend in OECD countries to simplify environmental regulatory requirements for SMEs that are characterised by a low level of environmental risk. This simplification generally involves **replacing bespoke environmental permitting with standardised requirements (e.g. general binding rules) for specific activities with low environmental risk** that are practised by a large number of operators and employ similar technologies. Rules that require operators to notify, or register with, the competent environmental authority before engaging in an activity are preferable in terms of the regulator's knowledge of the regulated community and control over its potential environmental impacts.

Another way to reduce the administrative burden on SMEs is to ensure collaboration between environmental and non-environmental regulators to identify

opportunities to reduce duplication in paperwork and conduct joint or delegated inspections in selected sectors. **Introducing elements of compliance self-assessment by operators of low-risk facilities** (e.g. as part of an environmental management system) would not only contribute to the reduction of the administrative burden but also improve the efficiency of compliance monitoring.

Efforts to promote compliance with environmental regulations should generally be sector-based because businesses, particularly SMEs, respond primarily to messages adapted to their sector. The sectoral approach to outreach is part of a larger customer service perspective that environmental regulators should adopt in their relationship with small businesses. Environmental enforcement authorities should work to strengthen their own staff's capacity to regulate and advise small businesses in specific sectors.

Providing information, advice and guidance

The government's environmental outreach to SMEs includes compliance promotion and larger efforts to encourage green business practices. While in the long term web-based guidance is likely to become the primary source of support for SMEs, in the short and medium term **online tools need to be complemented by other, more traditional instruments such as paper and electronic mailings, brochures and workshops.**

Packaging the information and formulating the right message is crucial for the effectiveness of communication tools. **Business benefits of improved environmental performance should be the main "selling point" of environmental outreach to SMEs.** Government bodies, including ministries of economy and environment, should work in partnership with trade associations and business support organisations to elaborate and disseminate environmental guidance, which would add to its credibility.

The instruments of environmental outreach should be carefully tailored to the nature and needs of small businesses. **Guidance should be concise and clearly distinguish between legal requirements and good practices** in order to avoid excessive efforts by small businesses to achieve compliance. It should contain a simple message about the problem, its solution and where to go for more information.

Recognising green practices

Small businesses face serious obstacles in implementing environmental management systems (EMSs), including a lack of resources, knowledge and technical capacity, high upfront costs, and low public visibility. **It is important to focus on simple, accessible improvements in management practices.** EMSs with varying degrees of complexity and low on paperwork as well as sectoral green label schemes are more likely to be attractive to small businesses than formal ISO 14001 certification. Sector-specific green certification (of business practices) and eco-label schemes (for products) also contribute to an increased demand for green business practices.



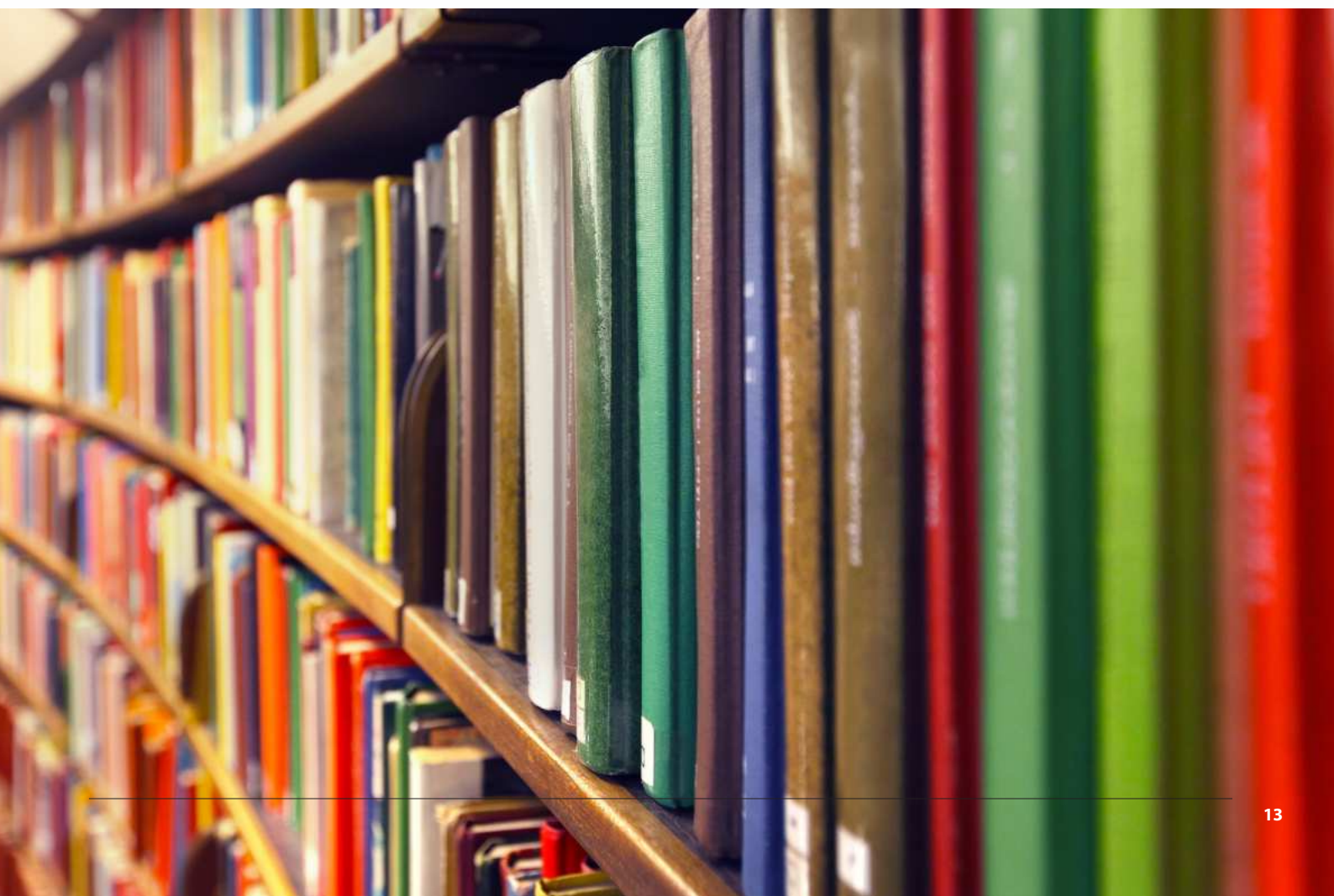
Offering financial incentives

Governments may **introduce tax privileges** (accelerated amortisation, reduced property or corporate taxes) and **favourable loan policies through public financial institutions to SMEs willing to invest in green technologies**. However, governments should not provide subsidies to businesses for achieving compliance with environmental requirements.

Government authorities should encourage private banks and insurance companies to provide incentives for good environmental performance of small businesses. Banks may require an environmental checklist

for loan approval, and insurers may demand a statement of environmental risk identification and control. Banks and insurers can also offer better loan or insurance policy conditions to businesses with green credentials.

Direct subsidies and free technical assistance to SMEs help to increase their awareness and secure their initial engagement in green practices. However, given the limited availability of public funding for promoting compliance and green business practices, a gradual transition toward a fee-based system for technical assistance would improve its long-term sustainability.





Sending the right market signals

Governments should exert direct supply chain pressure by **developing and implementing green public procurement policies** as a way to encourage potential SME suppliers to offer environmentally friendly goods and services.

Governments should also encourage larger firms to form partnerships with smaller suppliers on improving their environmental performance and provide public recognition to those who do so.

Building institutional partnerships

Environmental authorities have regulatory competency over only part of the SME community, and they are not the primary interlocutors of small businesses. However, in OECD countries they often co-ordinate the efforts of other public and private actors to promote green behaviour of SMEs. In EaP countries, this role is increasingly being assumed by ministries of economy. **It is important that a national government body take the lead in establishing a network of actors engaged in helping SMEs improve their environmental performance.**

Once such a network has been created, its member institutions should perform the **crucial “signposting” function** of providing businesses with references to direct

operators of multiple governmental and non-governmental programmes promoting different aspects of green business.

Working in partnership with business groups can be particularly useful as many SMEs do not respond to outreach activities conducted by government agencies due to suspicion of a hidden regulatory agenda. Feedback from businesses groups is extremely useful in developing and improving compliance assistance programmes. Business associations can help small businesses to improve profitability through environmental management, e.g. by developing marketing and promotional materials which a business could use to display to its customers its “green credentials” and practices.

Further reading

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The OECD implements the EaP GREEN project within the framework of the EAP Task Force which has, for over twenty years, been helping countries in Eastern Europe, Caucasus and Central Asia (EECCA) to integrate environmental considerations into the processes of economic, social and political reform. This policy brief has been produced with the financial assistance of the government of the Netherlands.

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