



# Innovative Finance Inclusion

## Environmental Investment Center as an institution for practical implementation of sustainable finance policy in Estonia

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**Date: April 2022**

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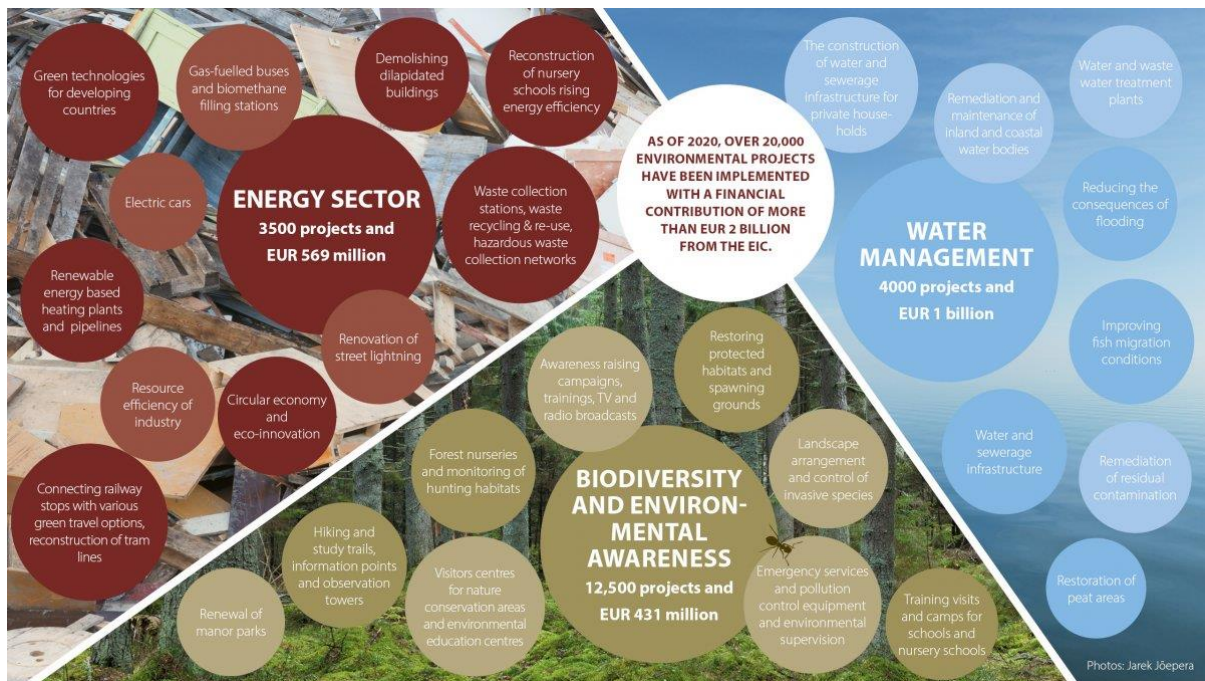
Co-funded by the  
Erasmus+ Programme  
of the European Union





## Abstract

The Environmental investment center (EIC) of Estonia is a foundation that contributes to sustainable finance development on the national level. Unlike many other organizations, the EIC started sustainable financing in 2000, when it was not mainstream and, as of 2020, over 20 000 environmental projects were implemented with a financial contribution of more than 2 billion EUR.



Distribution of EIC projects by types and finance volumes (Source <https://www.kik.ee/en/kik>)

The EIC was established in May 2000 and became the leading distributor of environmental assistance and investments to companies, educational institutions, private applicants, and other organizations. The EIC allocates the funds received from environmental exploitation (e.g., tax money, structural funds, revenue from the sale of Estonia’s CO2 allowances) into the development of environmental projects (see figure 1). The EIC is the implementing agency of the environmental projects of the European Regional Development Fund, the European Social Fund, and the Cohesion Fund of the European Union. The EIC also offers the possibility of applying for environmental loans to companies and organizations to develop environmental projects.

## Keywords

Structural Funds, Environmental Loans, Environmental Projects Financing, Sustainable Investments, Sustainable Finance.



# 1 Background

The EIC (<https://www.kik.ee/en/kik>) was founded in 2000, and for the last 20 years, it has served as one of the main financiers of environmental projects in Estonia. With the support of various sources of financing, the EIC has helped to implement activities within the scope of different ministries in Estonia.

The organization’s main task is to finance projects that are necessary to meet its statutory objectives. The statutory objectives include the reduction of environmental nuisances to the maximum extent possible to protect the environment, human health, well-being, property, and cultural heritage; the promotion of sustainable development to secure an environment that meets the health and well-being requirements of the present generation and future generations.

## 1.1 History of the EIC

In May 2000 Minister of Finance, Siim Kallas, signed the decision to establish the EIC. The institution was registered in the register of foundations and non-profit associations and already in June 2000 the EIC Council made the first decisions on the financing of environmental projects from the fees received from the use of the environment<sup>1</sup>.

In 2001 the EIC was appointed as the implementing unit for the implementation of the European Union's pre-structural fund ISPA (The Instrument for Structural Policies for Pre-Accession<sup>2</sup>) external assistance projects. Estonian Government signed an agreement with the Ministry of Finance to mediate loans taken from the Nordic Investment Bank for environmental projects.

In 2004–2006, the EIC was appointed as the implementing unit of the Cohesion Fund (CF) for the mediation of grants on environmental topics. Until now, projects financed from the ISPA budget have since been implemented with the rules and resources of the Cohesion

<sup>1</sup> Estonia has used economic instruments for environmental protection since the 1990s. Environmental taxes used <sup>1</sup> currently include the fuel excise duty, the excise duty on packaging and the heavy goods vehicle tax. An excise duty on electricity was established in 2008. The most important tool in achieving the objectives of environmental policy and the polluter/consumer-pays principle is environmental charges, which have also been implemented since 1991. The grounds for implementation of environmental charges and procedures for calculation and payment, rates and use of the state budget revenue from the charges are governed by the Environmental Charges Act and acts thereunder.

<https://www.eea.europa.eu/soer/2010/countries/ee/national-and-regional-story-estonia-flexibility>

<sup>2</sup> The Instrument for Structural Policies for Pre-Accession (ISPA) was designed to address environmental and transport <sup>2</sup> infrastructure priorities identified in the Accession Partnerships with the 10 applicant countries of Central and Eastern Europe. Its aim was to enhance economic and social cohesion in the applicant countries. It was replaced by the regional development component of the Instrument for Pre-accession Assistance (IPA) Search for available translations of the preceding in 2007.



Fund (CF). The granting of environmental loans started. In addition, the EIC was appointed as the implementing unit of the European Regional Development Fund (ERDF) for mediating grants from participants from Estonia.

In 2005 the Environmental Charges Act was adopted, based on which the money received from environmental charges are issued by the EIC.

In 2008 The EIC was named the implementing unit of the CF, the ERDF, and the European Social Fund (ESF) in the mediation of grants for the assistance period 2007–2013.

In 2009 the EIC and the Ministry of Finance signed a loan agreement, based on which the EIC received part of the loan money taken by the European Investment Bank (EIB) for on-lending.

In 2010 the EIC and the Ministry of the Environment entered into an administrative agreement under which the EIC must trade in CO2 emission units (AAUs) and implement the green investment scheme (RIS)<sup>3</sup>.

In 2013 The administrative agreement between the EIC and the Ministry of the Environment was supplemented with a clause that also enables the EIC to organize activities in the field of the environment itself, which contribute to the development of the field and increase the quality of submitted project applications. In the 2014–2020 funding period, the EIC will continue to distribute CF and ERDF grants as an implementing entity.

In 2015 the EIC Council approved the regulations for the organization of sectoral programs and the topic of the pilot study.

In 2016 the Ministry of Finance has opened an electronic application system for e-grants, which enables the submission of electronic applications for support from the European Union's structural funds. The EIC and Innove<sup>4</sup> first joined the pilot projects, opening the first rounds in the system.

<sup>3</sup> <https://www.mkm.ee/en/objectives-activities/foreign-financing/green-investment-schemes>

<sup>4</sup> Previously Innove (<https://www.innove.ee/>), foundation which provided state-commissioned services to children and young people, parents, adults, teachers and school leaders, educational institutions, as well as other institutions and organizations. As of the 1st of August 2020, all the activities of Foundation Innove will be transferred to a new state authority called the Education and Youth Authority (Haridus- ja Noorteamet). The Education and Youth Board (Harno) is a government agency of the Ministry of Education and Research that deals with the implementation of Estonian education and youth policy. The new authority is directly subordinate to the Ministry of Education and Research. <https://www.harno.ee/>



In 2017 an application round on ERDF<sup>5</sup> resource efficiency for companies was launched. For the first time, the EIC received a certificate of responsible entrepreneurship and a silver quality label<sup>6</sup>.

On 3 January 2019, the Government of the Estonia Republic decided to bring the EIC under the Ministry of the Environment. The decision entered into force retroactively from 1 January 2019.

### 1.2. Fields of activity and organizational structure

The EIC is a financial institution, mediating state budget funds (revenues from environmental charges), EU funds, funds from foreign aid programs and the Green Investment Scheme and granting loans for the implementation of environmental projects.

The EIC vision: *Efficient cooperation between EIC and its partners has reduced Estonia's ecological footprint.*

The EIC mission: *To ensure maximum efficiency by channeling every euro for the benefit of the Estonian people, a healthy living environment, and resource-efficient development of the country.*

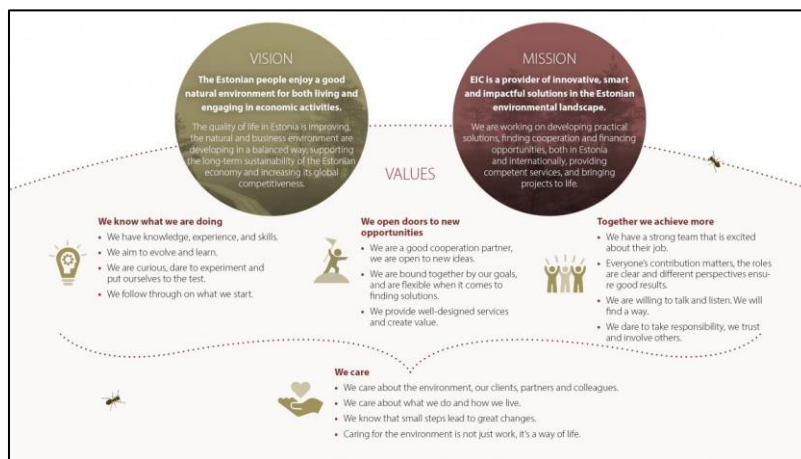


Figure 1. Values of the EIC (source <https://www.kik.ee/en/kik>)

<sup>5</sup> the European Regional Development Fund

<sup>6</sup> Estonian Responsible Business Index by the Responsible Business Forum <https://indeks.csr.ee/en/laureaadid/2017-en/>

To earn the Responsible Business Index Quality Label, companies must fill out an extensive application that consists of questions and principles based on the main social responsibility topics covered by the ISO 26000 standard, the global General Reporting Initiative (GRI) standard, recommendations for communicating responsibility topics, and the Estonian legal system. During the assessment, all companies were evaluated by their management methods and ethics as well as their actions towards the environment, the market, their employees, and their work environment. The companies are divided into two size-based categories for the evaluation: micro- and small enterprises comprised one category and medium and large enterprises the other



The EIC or in Estonian Keskkonnainvesteeringute Keskus (KIK) had a total of 63 employees in the 2nd quarter of 2021 and the organizational structure with several departments (see more in Figure 2), management board and Chamber of Development and Partnership.

The EIC is a state-owned foundation and performs tasks assigned by the state, based on various laws and administrative agreements, which mainly consist of the implementation of various support schemes in the field of environment. The activities of the EIC are public to the extent provided by law.

The organization’s main task is to finance projects that are necessary to meet its statutory<sup>7</sup> objectives. These objectives are:

- the reduction of environmental nuisances to the maximum extent possible in order to protect the environment, human health, well-being, property and cultural heritage;
- the promotion of sustainable development in order to secure an environment that meets the health and well-being requirements of the present generation and future generations;
- the preservation and protection of biodiversity;
- a healthy environment;
- the prevention and remedying of environmental damage.

<sup>7</sup> General Part of the Environmental Code Act, §1. [https://www.riigiteataja.ee/en/compare\\_original/524032015004](https://www.riigiteataja.ee/en/compare_original/524032015004) <sup>7</sup>

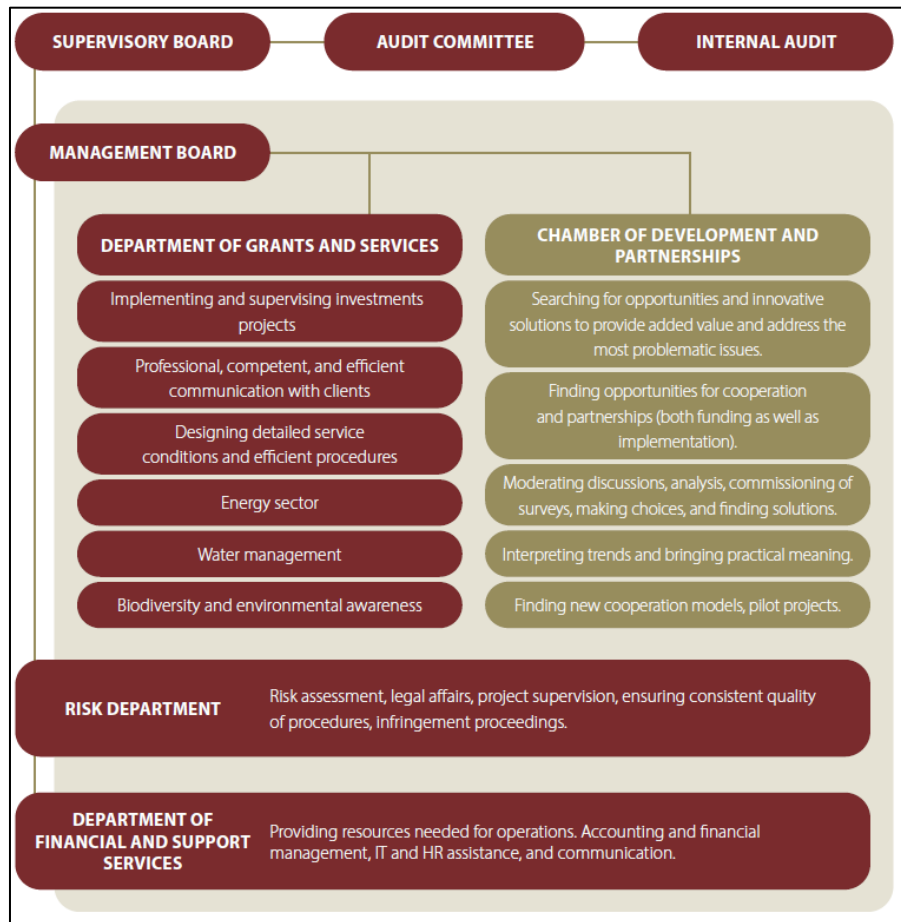


Figure 2. Functions and management of the Environmental Investments Centre (Source <https://www.kik.ee/en/kik> )

zField of activity of the EIC relates to following areas of projects' development and support, as well as measurement development:

- circular economy (resource efficiency and waste);
- energy, transport and building;
- biodiversity and nature-based solutions (conservation, forestry, fisheries, hunting, maritime);
- environmental education and awareness;
- green technologies and innovation;
- horizontal initiatives (smart city and community, climate change mitigation and adaption).

For each of the directions' the EIC provides grants for companies, institutions, or private persons with the aim to implement environmentally friendly and sustainable projects. From year-to-year priority directions change. As an example, in the year 2020 the activities supported by the EIC were divided into three areas<sup>8</sup>:

- Energy: atmospheric air protection, street lighting, resource efficiency, heat, waste, and recycling, biomethane production and consumption in the transport sector, energy efficiency in kindergarten buildings, electric vehicles, and hydrogen
- Nature and environmental awareness: fisheries, nature protection
- Water management: water infrastructure investments, marine environment, inland waterway remediation, flood risk management, achievement of climate policy objectives in developing countries.

In 2020, 508 project applications were submitted in the field of energy, of which 329 projects were funded for a total amount of EUR 62,138,855. A total of 832 applications were submitted in the field of environmental awareness and nature protection, of which 673 projects were funded in the total amount of 7,914,141 euros. 2,684 applications were submitted in the field of water management, of which 2,272 projects were funded in the total amount of 22,012,285 euros (see more in Figure 3).

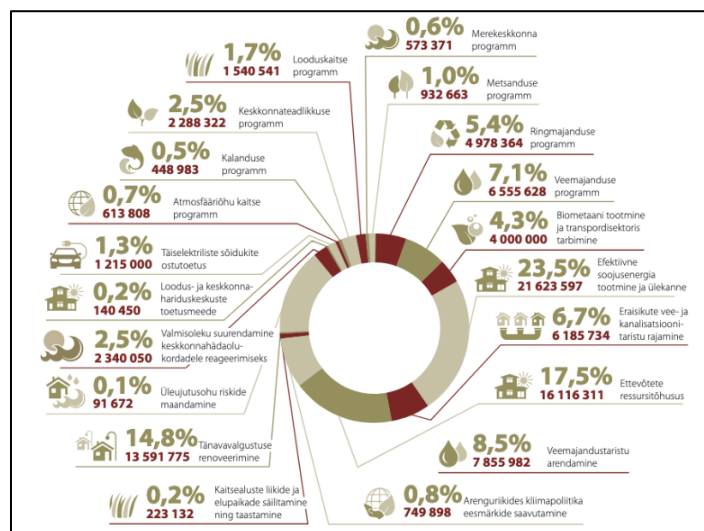


Figure 3. Amounts of projects for projects decided in 2020 by activity supported in euro. (23,5% efficient heat production and transmission, 17,5% resource efficiency of companies, 14,8% renovating street lighting, 8,5% development of water management infrastructure) (Source [Majandusaasta aruanne](#) (2020 Yearbook))

<sup>8</sup> [Majandusaasta aruanne](#) (2020 Yearbook)





Considering the mission, vision, and goals of the EIC, which are aimed at maintaining a healthy living environment, EIC also want to be an example of an environmentally responsible organization. The EIC’s principles for their daily activities are the following:

- improve the resource efficiency of our operations and implement energy saving measures;
- introduce paperless delivery and more efficient use of paper;
- prevent the generation of waste and promote the separate collection of waste;
- purchase products and services (information and communication technology, paper, chemicals, office supplies, catering for information days, etc.) that have/are environmentally friendly, i.e., follow the green purchasing policy where possible;
- reduce the environmental impact of business trips and promote sustainable transport management;
- ensure a healthy and socially responsible work environment for our employees (ergonomic working conditions, opportunities to promote health, raising employees' awareness of health and social issues, etc.).

The EIC has a certificate of responsible entrepreneurship and a bronze level quality label by the Estonian Corporate Social Responsibility Forum, which is awarded to institutions that have a significant positive environmental and social impact, i.e., the footprint that the company leaves with its existence.

### 1.3. Activities, Partners and Clients

Based on its vision, the EIC’s activities could be divided into three strategic focus areas of development, the effectiveness of which can be measured, and which have a clear cause-and-effect connection between the EIC’s contribution as a fund allocation organization and the result.

Strategic objectives and target activities are:

1. Proactive development of measures (e.g., number of projects implemented, activities done)
2. Finding additional cooperation and funding opportunities for clients
3. Providing competent services in the fields of the environment and climate

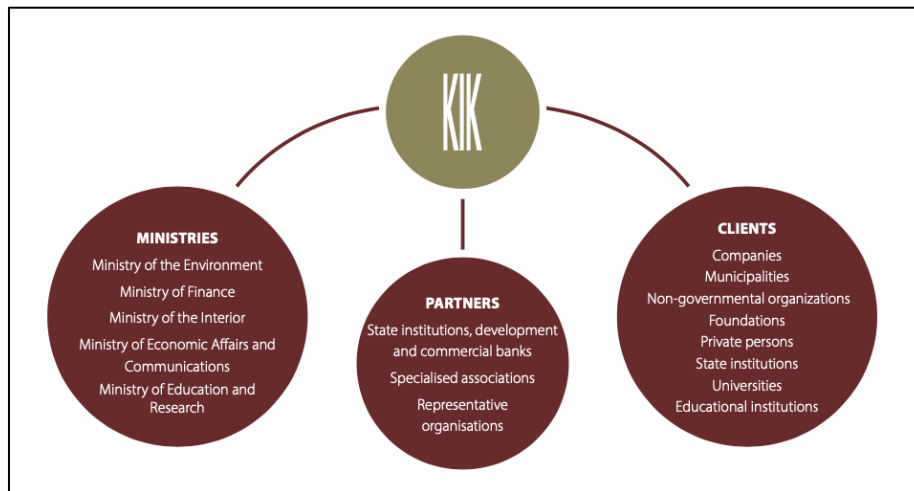


Figure 4. EIC’s current experience (target groups and partners) (Source <https://www.kik.ee/en/kik> )

The expectations of various stakeholders serve as the basis on which EIC’s activities are developed. The most important of these stakeholders’ expectations are<sup>9</sup>:

- the expectations of the Ministry of the Environment as the owner, which in large part overlap with the expectations of other ministries served (e.g., excellent understanding of the priorities and practical needs of the target group (clients), which allows for appropriate funding measures to be designed accordingly, while being logically consistent with all relevant actors in the field, and synergies to be found between the parties; becoming a center of competence for sustainable funding in our field, serving as a partner for the State, municipalities, and private businesses, etc.);
- the expectations of private and public partners, who play a key role in enabling effective solutions (e.g., capacity to implement pilot projects and new initiatives; flexibility to find solutions to different problems; excellent understanding of the public sector’s possibilities and the ability to negotiate agreements flexibly and promptly within the existing framework; clarity and consistency of the financing conditions, and proper risk management, etc.);
- the expectations of clients (target groups), whom it is important to motivate to carry out projects; and whose needs and interests are considered when designing the activities and services of the EIC (e.g., clarity and simplicity of agreements and procedures; clear and binding explanations of legislation (state aid, procurement conditions, financing regulations, etc.); full service: awareness raising, consultancy, information sharing, best practices, objective and clear answers, etc.).

<sup>9</sup> STRATEGY FOR 2020–2024 [https://www.kik.ee/sites/default/files/kik\\_strategiadokument\\_eng\\_2.pdf](https://www.kik.ee/sites/default/files/kik_strategiadokument_eng_2.pdf)



The EIC works with large variety of clients. An example of the EIC’s clients during the period 2000-2018 is shown in the Figure 5.

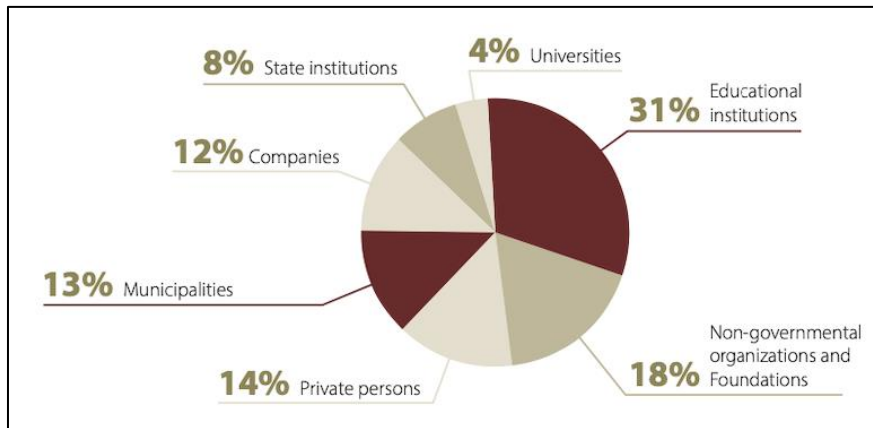


Figure 5. The EIC’s clients during the period 2000-2018 (Source STRATEGY FOR 2020–2024 [https://www.kik.ee/sites/default/files/kik\\_strategiadokument\\_eng\\_2.pdf](https://www.kik.ee/sites/default/files/kik_strategiadokument_eng_2.pdf) )

There are no direct competitors for the EIC in Estonia. Indirect ones are incubation and acceleration institutions, which promote support for green and sustainable projects.

In 2020 the EIC generated revenue around 4 million euros.

## 2 Institutional Solutions and Change

### 2.1. The EIC as an institutional solution

The EIC is case that explore changing metrics and incentives and explore innovative changes in finance models and structural platforms, as well as finance supply sources, bodies, and models’ case. Since the EIC was established in 2000, it influenced substantially to the development of environmental programs and their implementation in the country. Estonia has moved forward with a wide range of initiatives that have contributed to the sustainable development initiatives. Estonia is a country that has made considerable progress with sustainable development and green programs in a short period of time, considering that it emerged from a totalitarian regime<sup>10</sup> to establish a democratic government in the beginning of nineties.

<sup>10</sup> Totalitarianism is a form of government and a political system that prohibits all opposition parties, outlaws’ individual opposition to the state and its claims, and exercises an extremely high degree of control over public and private life. It is regarded as the most extreme and complete form of authoritarianism. In totalitarian states, political power is often held by



In 2011 EIC Yearbook was written<sup>11</sup>:

*“Environmental fee is one way of trying to see what nature would cost. Unfortunately, we cannot name everything nature can offer us not to mention trying to put a price tag on it. Try to put a price tag on peace of mind, hope, or even love – doesn’t work. Even though environmental fees and fines can cover only a fraction of these expenditures that were done on purpose or with carelessness to environment, fees and fines have their own role to let know people who pollute that they are the ones who have to pay. In order for funds from environmental use would get back to environmental improvement as investments and support there is a corresponding legislative guarantee and corresponding institution – Environmental Investment Centre (EIC).”*

The EIC implemented a large variety of environmental projects and programs during its history. Firstly, areas funded the most were water protection and waste management (e.g., in 2010 the number of projects were 124 with total funding of 20 million euros). The most troublesome areas for Estonia were drinking water issues, sewage, and waste management, as well as other areas like forestry, fishery, nature protection, and environmental awareness. The EIC became a leading supporter of environmental projects and implementer of environmental investments and support, institutional solution and started changing green projects landscape in Estonia.

To illustrate, program priorities in 2010 were environmental awareness, water management, regional projects implemented in Estonia regions (figure 6). The number of projects that were financed by those priorities in more detail are following: preservation of natural diversity (54), development of infrastructure of water supply systems and water management (14), extended use of renewable energy sources for the generation of energy and reconstruction of district heating networks (21).

autocrats, such as dictators and absolute monarchs, who employ all-encompassing campaigns in which propaganda is broadcast by state-controlled mass media in order to control the citizenry. The Estonian Soviet Socialist Republic (Estonian SSR or ESSR) was a republic of the Soviet Union. The ESSR was initially established on the territory of the Republic of Estonia on 21 July 1940, following the occupation of Soviet troops on 17 June 1940 and the installation of a communist government backed by the Soviet Union, which declared Estonia a Soviet constituency. More details can be found [here](#).

<sup>11</sup> [2001 aastaraamat \(Yearbook\)](#)

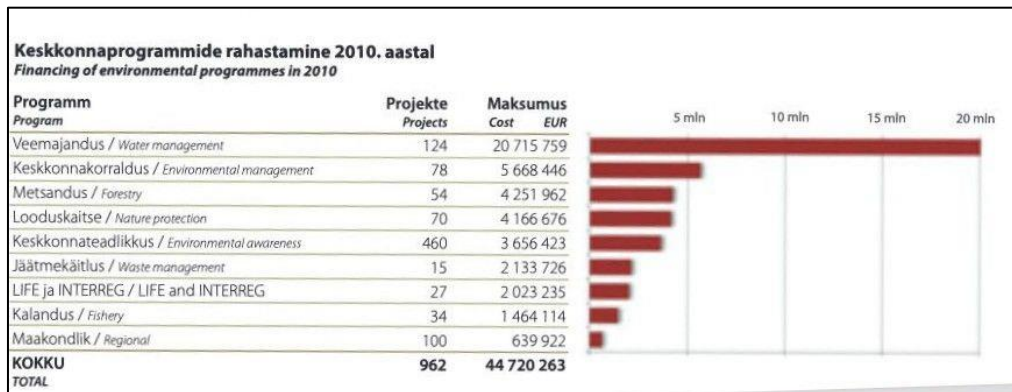


Figure 6. Financing of environmental programs in 2010 (Source [2010 aastaraamat](#) (Yearbook))



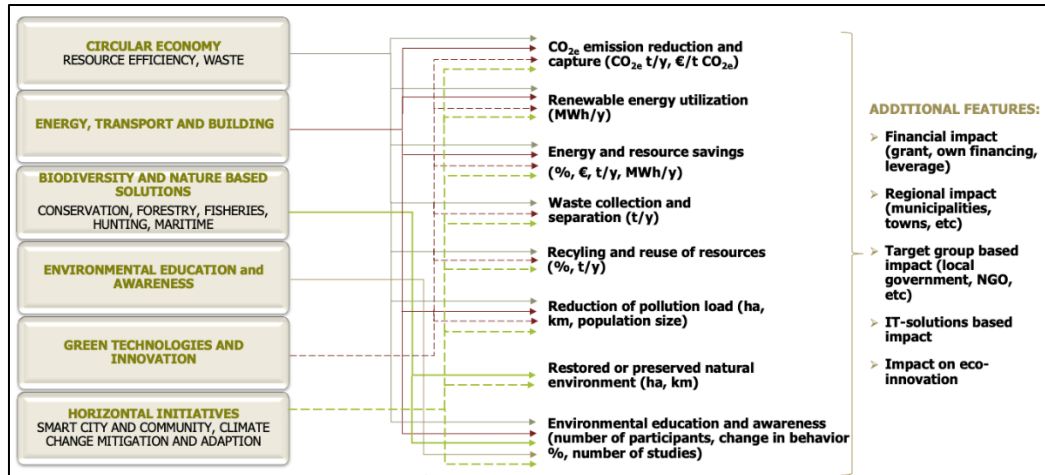
Figure 7. Financing of environmental projects in 2010 (Source [2010 aastaraamat](#) (Yearbook))

The priorities change from field to field and covering more and more topics, that provide multilateral approach towards sustainability topic. At present the distribution of projects are following: 23,5% efficient heat production and transmission, 17,5% resource



efficiency of companies, 14,8% renovating street lighting, 8,5% development of water management infrastructure.

To give finance and spread grants between participants and applicants, the EIC developed the system of their own parameters in the field of green finance.



Picture 8. Fields and metrics, developed by EIC to evaluate projects (Source – developed by the EIC representatives)

EIC's sources of financing are:

- the environmental fees of the Republic of Estonia;
- European Union structural funds;
- revenue from the sale of Estonia's CO2 allowances.

In addition to financing environmental projects, EIC offers the possibility to apply for a special purpose loan for their implementation.

The EIC has provided loans since 2002. The EIC not competing with commercial banks but is trying to develop environmental projects with longer pay-back periods and find funds for self-financing of projects supported by the EIC.

Two of the most important and equally large customer groups, based on loan amounts, are local governments and water undertakings. The advantages of taking a loan from the EIC are a longer pay-back period (up to 20 years), an affordable interest rate, and the possibility of a flexible payment break at the time when the project is being implemented or about to take off.

An additional convenience is that the customer only must communicate with the EIC, not separately with the granter of the aid and the lender. The favorable terms of loans taken from the EIC enable local governments to implement other important and topical investments



and better manage their finances. The payment discipline of customers has been excellent so far.

The main loan products (as for 2013) are:

- loan portfolio of the European Investment Bank (EIB) – aimed at covering self-financing of the water management projects supported from the Cohesion Fund; the volume of the loan portfolio is EUR 130 million, of which EUR 99.7 million is in use.
- loan portfolio of the EIC’s own funds – aimed at funding projects whose objectives tally with the directions of the EIC under its articles of association<sup>12</sup>; the volume of the loan portfolio is EUR 15 million, of which EUR 10 million is in use.

As an implementing unit for EU support, the task of the EIC in mediating structural aid has been related to counselling recipients and monitoring their activity. The control system has two levels. The first control is carried out by project coordinators (who mostly counselling for applicants) and the second, selective level, by the specialists of the Supervision Unit. The Supervision Unit also handles violations, in addition to selection-based control.

Violations, or mistakes in observing the requirements of the structural aid rules, mainly occur due to inexperience or unawareness on the part of the recipients, especially when organizing tenders. A violation results in a financial correction or reduction in the amount of aid.

The EIC has structured its work so that the main emphasis is on the counselling of aid recipients, with control activities carried out in as early a stage as possible. This type of system, based on counselling and prevention, enables mistakes or errors to be avoided and reduced, and has proven itself useful. The most important contribution to achieving a good result has been given by project coordinators because they are the main staff counselling the recipients of aid.

## 2.2. The new EU Taxonomy for environmentally sustainable economic activities

The EU taxonomy is a classification system, establishing a list of environmentally sustainable economic activities. It could play an important role help the EU scale up sustainable investment and implement the European Green Deal<sup>13</sup>. The EU taxonomy would provide companies, investors, and policymakers with appropriate definitions for which economic activities can be considered environmentally sustainable. In this way, it should

<sup>12</sup> [https://www.kik.ee/sites/default/files/kik\\_pohikiri\\_10.02.2020\\_0.pdf](https://www.kik.ee/sites/default/files/kik_pohikiri_10.02.2020_0.pdf)

<sup>13</sup> [https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal\\_en](https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en)



create security for investors, protect private investors from greenwashing, help companies to become more climate-friendly, mitigate market fragmentation and help shift investments where they are most needed.

The Taxonomy Regulation was published in the Official Journal of the European Union on 22 June 2020 and entered into force on 12 July 2020<sup>14</sup>. It establishes the basis for the EU taxonomy by setting out four overarching conditions that an economic activity must meet in order to qualify as environmentally sustainable. Four overarching conditions are: 1) Climate Change Mitigation (2) Climate Change Adaptation (3) Sustainable Use and Protection of Maritime Resources (4) Transition to a Circular Economy<sup>15</sup>. The EIC has its own developed methodology to assess projects and make decision of financing. Now the EIC faces task to find ways to integrate Taxonomy and its own criteria. This task is planned for a year 2021 and will be accomplished by the EIC staff. In general, it would not influence on customers and grant holders, and will require internal research and work towards alignment.

<sup>14</sup> [https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities\\_en](https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities_en)

<sup>15</sup> [https://ec.europa.eu/info/sites/default/files/business\\_economy\\_euro/banking\\_and\\_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy\\_en.pdf](https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy_en.pdf)





### 3 Conclusion

The Environmental Investment Centre is Estonia’s leading agency when it comes to distributing environmental grants and investments. Thousands of useful and helpful projects are implemented with the support of the EIC every year, helping to preserve the state of Estonia’s environment, remedy environmental damage, and reproduce natural resources.

As a financial institution, the EIC made a great contribution to sustainable finance development in Estonia and is a good example of innovative changes in finance models and structural platforms, as well as organization which developed metrics for green finance support in its field of application.

Proposed example demonstrates connection between finance and sustainability on a national level. Used material could be used to demonstrate sustainable finance from the macro-perspective.

Task based on the case study is to reflect on proposed questions and discuss in groups:

- In your opinion, are state support financial institutions like the EIC effective instrument to promote sustainability? Discuss pros and cons of these type of agencies.
- Are there any country specifics for agencies like the EIC, or this instrument is universal and could be adopted in any country? What supportive mechanisms for implementation should exist in the country/region for that?
- Find another country-specific example of similar agencies, discuss, and compare their efficiency.



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