UNITED
NATIONS

EP

United Nations
Environment
Programme

Distr.
GENERAL

UNEP/OzL.Pro/ExCom/73/57
17 October 2014

ORIGINAL: ENGLISH

EXECUTIVE COMMITTEE OF
THE MULTILATERAL FUND FOR THE
IMPLEMENTATION OF THE MONTREAL PROTOCOL
Seventy-third Meeting
Paris, 9-13 November 2014

FUND TRANSFERS FROM THE TREASURER TO THE IMPLEMENTING AGENCIES (decision 72/42(b)(ii) and (iii))

Report on the Multilateral Fund on the issues of fund transfers to implementing agencies, fund surplus, interest earnings, investments and the efficient utilization of resources

Purpose

1. The Executive Committee's decision 72/42 in paragraph (b) (ii) requested the Treasurer to seek, in consultation with the Secretariat, expert views on the issue of fund transfers from the Treasurer to the implementing agencies and to report back to its 73rd meeting. Through paragraph (b) (iii) of the same decision, the Treasurer was requested to include in the next report on the accounts of the Multilateral Fund integrated information on the UNEP-wide standard on cash advances and the 20 per cent disbursement threshold for tranches of HCFC phase-out management plans to show clearly the relationship between the two issues, together with further information on the criteria used for the placement of funds to ensure risk reduction and the maximization of interest accrual.

2. The concerns about the excessive building up of surplus funds of the Multilateral Fund at various stages between the funds being contributed by the Parties to the time they are actually deployed in the activities for which they are intended have recently been expressed in the discussions of the Executive Committee's deliberations[1] and also from the 2011 UNEP Report of the United Nations Board of Auditors[2] (UNBOA). The Executive Committee also additionally pointed at the importance of maximizing the interest earning on these funds as they are being held.

3. The Treasurer appreciates the cooperation of the implementing agencies in their provision of information requested and the subsequent discussions with staff of their financial/accounting/investment departments.

[1] Several decisions of the Executive Committee sequentially: **decision 68/22 (a)** and **(b)** (based on UNEP/OzL.Pro/ExCom/68/24/Rev.1); **69/24 (b)** and **(c)** (based on UNEP/OzL.Pro/ExCom/69/35); **decision 70/20** (based on UNEP/OzL.Pro/ExCom/70/50); **decision 71/44** (based on UNEP/OzL.Pro/ExCom/71/58); **decision 71/46 (d)** and **(e)** (based on UNEP/OzL.Pro/ExCom/71/60); **decision 72/38** (based on UNEP/OzL.Pro/ExCom/72/38); and **decision 72/42** (based on NEP/OzL.Pro/ExCom/72/44).
[2] **A/67/5/Add.6 – Report of the Board of Auditors** on UNEP Financial report and audited financial statements for the biennium ended 31 December 2011.

Pre-session documents of the Executive Committee of the Multilateral Fund for the Implementation of the Montreal Protocol are without prejudice to any decision that the Executive Committee might take following issuance of the document.

Historical perspective

4. The Multilateral Fund was established as a trust fund of the United Nations in accordance with the financial regulations and rules of the United Nations and Executive Committee entrusted the responsibility to thus manage the trust fund to the Executive Director of the United Nations Environment Programme.

5. UNEP, being the UN department responsible for the promotion of environmental preservation, nurtured the inter-governmental processes for agreements on: (a) the Vienna Convention on the Protection of the Ozone Layer; and (b) the Montreal Protocol on the Protection of the Ozone Layer from Substances that Deplete the Ozone Layer. For both, the member states asked UNEP to host their common secretariat -the Ozone Secretariat-- and the latter agreed. UNEP was eventually also asked to take up the functions of Treasurer to the Multilateral Fund, which it accepted and went on to provide the services pro bono for some time until in 2004 when a new arrangement was agreed to with the Executive Committee and for which an annual fee became payable. Additionally to that the Parties decided to also collocate[3] the Secretariat of the Multilateral Fund with UNEP since the time of the establishment of the Multilateral Fund.

6. The Multilateral Fund financial mechanism operates on a three year cycle of replenishments and has adopted the use of a fixed exchange rate mechanism (FERM) for its Parties' payment of their contributions, in which those that qualify the established criteria can opt to use it in paying contributions in their national currency during the particular replenishment cycle agreed to. The Parties adopted this system fully aware that there would be exchange gains and losses and they agreed to absorb them within the fund. Also, the Multilateral Fund makes allowance for the qualifying Parties, to pay up to a maximum of twenty per cent of their contributions during a replenishment cycle in the form of bilateral technical assistance. Additionally to that, the Multilateral Fund also makes room for its qualifying Parties to pay their contributions through promissory notes which have to be established through an agreed upon format.

7. The issues under review have been raised in the context of constantly trying to find better ways of managing the resources of the Multilateral Fund. The end-of-year fund balances building up at various stages have necessitated looking for other ways that will maximize the returns from investment opportunities as an option of enhancing the returns to the fund.

Agreements

8. There are various agreements governing the Multilateral Fund's working modalities and these are between: (a) the Executive Committee and the Treasurer; (b) the Executive Committee and the implementing agencies; and (c) the Treasurer and the implementing agencies.

9. The Treasurer's responsibilities which are covered in the Agreement between the Executive Committee and United Nations Environment Programme, as the Treasurer, are: to manage the Multilateral Fund as a United Nations trust fund and administering the contributions (including the bilateral cooperation assistance and the fixed exchange rate mechanism), managing the investments of the funds, remitting fund to the implementing agencies and its Secretariat as approved by the Executive Committee, reporting on the status of the fund and providing financial reports and reconciling of the Multilateral Fund accounts with those of implementing agencies, and supporting the work of the Executive Committee. An annual fee of USUS $500,000 is paid to the Treasurer for these services.

10. The Executive Committee has agreements with each of the implementing agencies in which the agencies - UNDP, UNEP, UNIDO and the World Bank- were asked to use their respective expertise in

[3] UNEP/OzL.Pro.2/3 Appendix IV D Paragraph 17 of the Report of the 2nd Meeting of the Parties to the Montreal Protocol.

the co-operation with the Executive Committee to assist the Article 5 Parties to facilitate compliance with the Montreal Protocol.

11. The Agreements required that each implementing agency establish a special/trust fund account for the receipt and management of the funds from the Multilateral Fund in accordance with their financial regulations and rules for the projects and activities approved by the Executive Committee; returning to the Multilateral Fund any earnings from investments of unutilized funds; providing periodic financial and substantive reports; and participation in the meetings of the Executive Committee.

12. While the initial agreements with the implementing agencies stipulated that the entirety of the funds for projects approved for them would be transferred to them by the Treasurer, amendments to them were introduced in 1998 to allow UNDP and UNIDO accept partial transfers of the funds for the approved projects subject to the balance being held by the Treasurer in promissory notes.

13. These agreements have worked smoothly over the Multilateral Fund's life time, and only minor amendments were introduced to accommodate the implementing agencies' recognition of promissory notes as resources they can count on as funds available to them for proceeding with their internal commitments for the project approvals granted by the Executive Committee. The other amendment was for updating the agreement of the Treasurer to include a fee payable for the services.

14. The Treasurer has over the period carried out the functions of transferring the resources to the implementing agencies, upon instructions from the Secretariat, in a timely manner and improvements have constantly been made based on the experience gained and as solutions found to overcome any difficulties encountered were worked out. The implementing agencies have expressed no problems with the resources transfers from the Treasurer and the Secretariat has closely monitored the resources given to the implementing agencies, how the resources are used in the projects and activities approved and enforcing good annual reporting on the progress achieved.

15. The Secretariat has, in fact been instrumental in introducing good practices in sound management of the Multilateral Fund resources including the tracking the substantive and financial implementation so as to have any fund balances in completed projects revert back. The Secretariat is also a very active participant in the annual reconciliation exercise of the accounts of the implementing agencies and the Treasurer to ensure correct reflection of the reported implementation reports with the financial reports.

Accumulation of surplus

16. The Treasurer is naturally the first point of accumulation as the funds being paid by the Parties are kept there until when the Executive Committee meets to review various proposals from Article 5 Parties. And only upon the approval of the Executive Committee and instructions from the Secretariat that the Treasurer would release the approved funds to the respective implementing agencies.

17. The second point of accumulation is at the level of implementing agencies which disburse to the beneficiary countries' projects in accordance with work plans and time tables agreed. And, the third point of accumulation, although this is only in a few cases, is by the implementing agencies to the beneficiary countries' intermediary institutions whose role is to facilitate the country in the implementation of projects.

18. UNEP confirmed that its last approval in the year includes funds for the compliance assistance programme (CAP) budget which constitutes about sixty per cent of the year's total resources from the Multilateral Fund, and that exaggerated the end-of-year balances significantly. The World Bank, UNDP and UNIDO expressed the same feelings that the year-end balances are unrealistically high figures to use as representative of the funds the agencies would be holding during the year.

19. During the time when three meetings were held in the year the last one was held towards the end of the year and the funds transferred to the implementing agencies for the approvals granted as the year was closing contributed to the higher amounts the implementing agencies held at the year end. But there were instances when the Treasurer only managed to transfer these funds at the beginning of the following year, and in these cases the year-end closing balances were at much lower levels.

20. The level of funds held by agencies fluctuates during the year as funds are being constantly used for the activities - some on-going from the previous years and others coming up as new approvals during the year. Thus, the agencies confirm that the average level of funds held during the year would definitely be lower than the end-of-year balances.

21. Over the lifetime of the Multilateral Fund[4] the end-of-year balances held by the implementing agencies grew steadily from US $5 million in 1991 to the highest level of US $325 million in 1999 and for the following seven years they stabilized at a slightly lower level of US $220 - US $280 million. During the same period the expenditures grew initially slowly and then picked up reaching about US $200 million in year 2000 before stabilizing at a slightly lower level of an average of about US $151 million for the following eight years. The fund balances and the expenditures both experienced a gradual decline during years 2006 to 2009 and then picked up slightly from 2010. The expenditures continued to grow all the way to the end of 2013 while the fund balances dipped slightly in both 2012 and 2013. The low level experienced in 2009 probably marked the end of CFC/CTC/Halon projects and then the growth of both fund balances and expenditures starting thereafter marked the onset of the multi-year agreement (MYA) HCFC projects covering sector-wide activities in stages.

22. Although the issue of fund balances held in 2011 by the implementing agencies, the beginning of the HCFC projects, was noted as being at an abnormally high ratio compared to the annual level of expenditures, such occurrences had been experienced at the very beginning of the Multilateral Fund and the contributing Parties noted it with concern in the Executive Committee's meetings, and in looking for solutions to it the introduction of promissory notes came into being. The promissory notes provided an option for Parties to make their contributions in time to the Treasurer but their encashment would be done at later dates based on several dates of the anticipated actual need of the funds[5].

23. Indeed, in 1992, 1993 and 1994 the total end-of-year fund balances of the implementing agencies were at a very high level compared to the years' respective expenditures and the ratio stood at between 7.4 and 8.1- see Table 1 (and Figure 1) which includes a column showing these ratios. Of course, there were factors which could justify that at the beginning of the Multilateral Fund: (a) time was needed for working out policies and procedures on the programme's and projects' implementation, whose average was three years; (b) time was needed by member states and the implementing agencies to come up with and formulate project proposals; and (c) time was needed to sort out a myriad of other teething problems to get the programme off the ground.

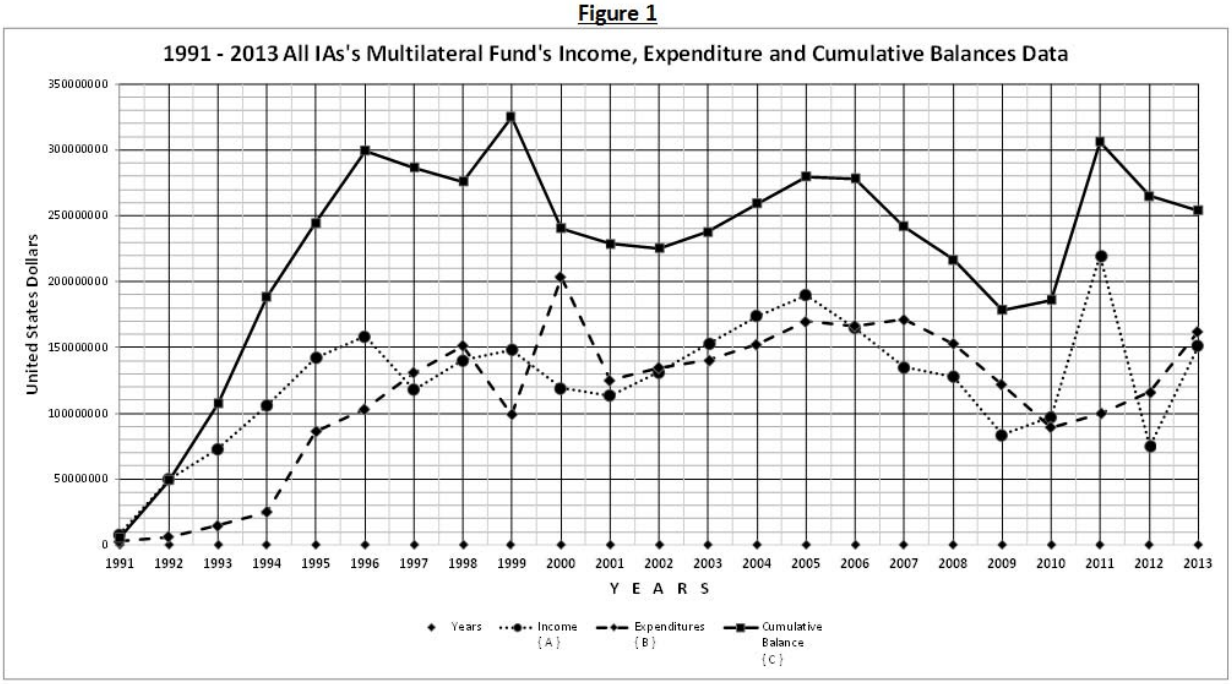
Table 1. All Implementing Agencies Aggregate Income, Expenditures and Cumulative Balances (US $)

Years	Income	Expenditures	Cumulative Balance	RATIO: Cumulative Balances Over Expenditures
	(a)	(b)	(c)	(d = c/b)
1991	8,079,633	2,669,480	5,410,153	2.0
1992	49,794,549	6,126,539	49,078,163	8.0
1993	72,839,402	14,700,485	107,217,080	7.3
1994	105,914,910	24,803,373	188,328,617	7.6

[4] See **Table 1** and **Figure 1** showing the 1991-2013 incomes, expenditures and fund balances from the implementing agencies compilations.
[5] **UNEP/OzL.Pro/ExCom/12/13** Annex **II** – Encashment Schedule for Promissory Notes.

Years	Income	Expenditures	Cumulative Balance	RATIO: Cumulative Balances Over Expenditures
	(a)	(b)	(c)	(d = c/b)
1995	142,039,048	85,957,718	244,409,947	2.8
1996	158,273,086	103,235,984	299,447,049	2.9
1997	117,781,554	130,564,334	286,664,269	2.2
1998	140,102,278	151,125,184	275,641,363	1.8
1999	147,912,976	98,697,039	324,857,300	3.3
2000	118,975,538	203,389,532	240,443,306	1.2
2001	113,289,029	125,086,276	228,646,058	1.8
2002	131,146,516	134,760,106	225,032,468	1.7
2003	152,819,461	140,100,414	237,751,515	1.7
2004	173,872,599	152,347,508	259,276,606	1.7
2005	189,760,780	169,685,639	279,351,747	1.6
2006	164,671,354	166,177,496	277,845,605	1.7
2007	134,839,293	171,120,151	241,564,747	1.4
2008	127,585,972	152,742,796	216,407,923	1.4
2009	83,554,938	121,741,057	178,221,804	1.5
2010	97,005,256	89,329,487	185,897,573	2.1
2011	219,531,817	99,538,227	305,891,163	3.1
2012	75,010,406	116,083,410	264,818,159	2.3
2013	151,198,791	162,111,924	253,905,026	1.6

Figure 1



24. In fact another high ratio of 3.3:1 for the implementing agencies fund balances relative to their total annual expenditures was experienced in 1999. Otherwise, outside these abnormal years at the beginning and in 1999 and 2011, for most of the remaining time of the Multilateral Fund this ratio

fluctuated below 3:1 and with the lowest of 1.2:1 experienced in 2000 -the average for those years stood at 1.9:1.

25. In a system where the funds for the entire project life are given, the ratio of the fund balances to the expenditures has to be higher than 1:1 as the funds held include also funds for subsequent years. How much higher the optimal ratio should be depends on the average duration and the nature of the projects. The longer the duration of the average project the higher the ratio and may be the ratio of about 2:1 which is about what has been experienced by the Multilateral Fund for most of the time is an acceptable one.

Funds transfer mechanisms

26. At all the meetings of the Executive Committee, the Treasurer presents the report on the status of the Multilateral Fund in order to help the former's reviewing of proposals knowing how much funds are available and to eventually transfer to the implementing agencies based on the approved grants. At the completion of the meetings the Secretariat sends a formal request to the Treasurer to transfer the funds to the implementing agencies for their approvals, and if there were balances returned from completed or cancelled or adjusted projects, these would be offset against the funds transferred. Other elements taken into accounts in the funds to be transferred include: transfers of projects between implementing agencies, funds withheld subject to fulfilment of some aspects considered important and reported interest accruals.

27. The Treasurer normally transfers cash resources in which offsets for any reported interest accrued would have been included. Sometimes the Treasurer transferred or reserved promissory notes in lieu of cash resources for the approvals, but with an agreed arrangement with the implementing agency.

28. The existing arrangement of giving the full amount of resources to the implementing agencies is fully in accordance with the agreements and it leaves the implementing agencies fully responsible for the implementation of the projects and programmes approved to them. This definitely gives the implementing agencies the full flexibility of organizing themselves best on how to undertake their project implementation activities because there are no external risks of not receiving the cash whenever needed.

29. The World Bank does not make any commitments in advance of the receipt of financing in the Ozone Projects Trust Fund to finance commitments. In the cases of UNDP and UNIDO there is a little flexibility as they agreed in 1998 to amend their agreements to accommodate accepting partial payments in cash for projects approved for them as long as the other partial funds, in promissory notes, were held in trust by the Treasurer for them. However, all the implementing agencies indicated that there are increasing difficulties encountered in encashing promissory notes and for that reason they would prefer to receive cash transfers only for their approvals.

30. Not all financial mechanisms transfer funds in full to the implementing agencies upon approval of projects. For example, with regard to the Global Environment Facility (GEF), upon a project's approval a letter of commitment guaranteeing the funds for the project have been set aside and would be made available to the responsible implementing agency and the executing agencies under the expanded opportunities is given. The GEF portfolio is about seven times bigger than of the Multilateral Fund's and the duration of its medium sized projects and full sized projects is well above five years.

31. With each implementing agency and the executing agency under the expanded opportunities the trustee has an agreement for periodic cash transfers, normally quarterly or half yearly or yearly (depending on what has been agreed), for an amount the implementing agency and the executing agencies under the expanded opportunities deems sufficient for its needs for projects implementation, fees and budgets for special initiatives and administration. This arrangement has a very simplified process for the implementing agencies and the executing agencies under the expanded opportunities to use when asking for additional funds to ensure that they always remain liquid. The GEF has also devised a system for

continuously updating the financial information with regards to the interest earnings, cancellation of projects, changing needs of projects whether increasing or decreasing.

32. For the Multilateral Fund, the well-established approval and progress reporting process addresses the review and corrective measurements. The implementing agencies already provide disbursement estimates in their annual progress and financial reports and the Executive Committee monitors the extent to which implementing agencies achieve their disbursement target in the context of the evaluation of the performance of the implementing agencies[6].

Weighing the pros and cons of full or partial transfer of funds to the implementation agencies

33. Considering the option for the Multilateral Fund to adopt the system of **partially transferring of funds** to the implementing agencies the following **advantages** could be realized:

(a) The funds will be transferred to the implementing agencies closer to the time the funds would be needed for the activities in the planned period; and

(b) The existing systems in place within the Secretariat and the Treasurer need little adjusting to cope with the partial transfer of funds -additional to reviewing of the implementing agencies' projects implementation progress, and their annual disbursement plans.

34. However, the major **disadvantages** of the option of **partially transferring of funds** to the implementing agencies are:

(a) The existing arrangement will need to be revisited to ensure that all the necessary adjustments would be in place --- the World Bank's agreement with the Executive Committee will need amendments and the other implementing agencies will need to make amendments to theirs too to add cash withholding to the promissory notes allowance necessitated by the 1998 amendments;

(b) The adjustments to the implementing agencies' systems to recognize the resources being withheld by the Treasurer as belonging to them will need some negotiations and some time to agree to together; and

(c) The diversity of investments currently realized because each implementing agency invests the surplus funds held by the agency will be almost lost as the investment would largely be done by the Treasurer.

35. On the other hand, the system which is currently in use of generally **transferring fully** to the implementing agencies **the funds** approved by the Executive Committee for their projects has the following **advantages**:

(a) The full amounts of funds being with the implementing agencies minimizes the risks of the funds being in another institutions' control and with this assurance proceeds with the implementation of the project activities within their full time framework with economies of doing so without any other intermittent other funds transfer costs;

[6] It should be further noted that all implementing agencies with investment projects met their performance targets for estimating fund disbursement in the 2013 evaluation as indicated in document UNEP/OzL.Pro/ExCom/73/16.

(b) The maintenance of the initial cooperation arrangement which has proven to have minimum hitches and with tested ability to mutually work on any difficulties encountered and getting solutions to them; and

(c) The investments by the implementing agencies provides some diversification and at the overall Multilateral Fund's level minimizes the risks of this being done largely by one institution.

36. The **disadvantage** of **fully transferring of funds** to the implementing agencies for the Executive Committee's approvals is the lack of guarantee that surplus funds will in future not build up again at the level of implementing agencies and remain unused for a considerable time.

UNEP-wide standard on cash advances, the 20 per cent disbursement threshold for tranches

37. The policy on cash advances of UNEP and the policy actions taken by the Executive Committee such as the requirement of at least 20 per cent of the funds from the previous tranche to have been disbursed before the following tranche's approval can be released is aimed at ensuring that progress on the implementation of the project is on course. The Secretariat would only instruct the Treasurer to transfer the funds to the implementing agencies when the Executive Committee would have been satisfied that, among others, the threshold disbursement conditions has been met by the implementing agencies. Additionally to this there is a requirement of completing HPMPs within one year's period after the last tranche approval and returning the remaining funds.

38. In essence, the above measures of: the UNEP policy on cash advances, the 20 per cent threshold for previous tranche's disbursements, and the enforcement of completion of the stage's projects and return the balances within a year after the last tranche's approval, have a common objective of trying to align the funding requirements with some tangible achievements in the implementation of the project. However, the second option has a potential for creating larger surpluses, especially if successive tranches are approved too close to one another.

39. The policy guidance on cash advances for UNEP, on its own programme activities away from the role of Treasurer to the Multilateral Fund, requires the implementing agency to, at the commencement, make an estimate of the fund requirements for the first six months and thereafter, upon furnishing satisfactory the quarterly year expenditure reports, cash advances are given for the following quarter based on the needs of the project. The UNEP-wide system is well designed for handling the cash advances and following up on the reporting on the implementation as the previous have to be cleared before the following period's requirements are approved and advanced.

40. However, it should be understood that UNEP's policy guidance for cash advance is tailored for giving resources to the executing agencies on the ground actually coordinating the implementation of the project activities. It is not for implementing agencies to a financial mechanism like the Multilateral Fund or the GEF the because the role of these agencies is that of agents helping member states with expertise in their formulation of projects, facilitating in the approval process and helping in the implementation of the projects with the management of funds and substantive activities until the projects come to completion.

41. UNEP's method is normally applied on a project-by-project basis instead of an agency portfolio basis and the controls sometimes delays the implementation of the projects due to the administrative work which takes time of both substantive and administrative staff in reviewing the reports. It should be noted that UNEP as Treasurer does not view the policy guidance for UNEP's projects to be applicable to fund transfers for portfolios.

42. The policy of not granting approvals and releasing funding for the tranches for a MYA following the first one unless 20 per cent of the preceding tranche(s)' funds have been disbursed could reduce the

balances held by implementing agencies[7]. It would reduce the automatic approval of tranches based solely on achieving a level of national consumption/production until 20 per cent of the first tranche had been disbursed. However, there remains the possibility of having a fund accumulation if tranche one remained with a low disbursement rate of say 20 per cent as well as similar levels for tranches two and the subsequent tranches. In the case of UNDP and the World Bank, as tranches are considered replenishment of funds instead of being treated for distinct projects as is the case of UNIDO, there could be accumulation of funds as described above. In the case of UNIDO, the accumulation of funds would depend largely on its ability to avoid project delays and the duration of project tranches.

43. In this regard, the Executive Committee's standard agreement for HPMPs requires that all HPMP stages are completed one year after the last tranche is approved and project fund balances at the end of each HPMP stage have to be returned. This standard clause in agreements which for non-LVCs have had durations of 5-6 years thus far should result in limited accumulation of balances during the phase-out of HCFCs. It is expected that this is going to result in less accumulation of funds as was as long as future stages of HPMPs for non-LVCs continue to have limited durations and the system of returning balances will continue at the end of each stage -as its effect will be to continuously mop up the excess fund balances.

44. Thus, the only relationship between the 20 per cent disbursement threshold for HPMP tranches and the UNEP-wide standard cash advance guidance is that both aim at releasing the funds for the implementation of projects in accordance with the requirements of the project. However, it should be noted that the UNEP projects are managed by executing agencies on the ground and are not really comparable to the HPMP which are portfolios and are manage by implementing agencies whose role is to assist member states in their preparation of and management of projects.

Investment policies

45. The Treasurer and the implementing agencies all do invest the funds not needed for immediate operations. They all broadly share the same investment objectives of <u>firstly</u> ensuring the preservation of the capital; <u>secondly</u> of ensuring that there would always be sufficient liquidity for the operational requirements and <u>thirdly</u> that the return on investment should be the optimal within the competitive market taking into account risks.

46. Across the board, these investments tend to be in a variety of securities like bank deposits, commercial paper, and securities of supranational, governments and government agencies. The tendency of these instruments is to have them for not long term investments and with the ability to be easily convertible to cash.

47. UNEP, as the Treasurer and an implementing agency, being a department of the United Nations, has its investments done by the UN Secretariat's Treasury in the UN Controller's office where there is an investment team whose strategy is guided by the three above objectives and uses the strategy of pooling all the funds managed by the United Nations headquarters so that its size attracts some preferential rates. The different programmes, including the Multilateral Fund, whose funds are pooled, share the earnings in prorated calculations.

48. UNDP's investment strategy is to invest the various programmes' balances as pooled funds consistent with UNDP's investment policy aimed at maximizing returns, while broadly observing the three objectives above. The investment guidelines adopted by the organization follow a conservative approach to investment and annual interest rate is based on the portfolio balance of UNDP managed funds

[7] This issue was discussed in the Overview of Issues arising from Project Review in document UNEP/OzL.Pro/ExCom/72/38 and decision 72/24 requires a further analysis to be presented to the 73rd and 74th meetings.

that are pooled and held in investment/bank accounts and through it the Multilateral Fund benefits from the preferential interest rates secured, especially as it is the second largest trust fund.

49. UNIDO's investment strategy governs all the funds of the organization whereby UNIDO pools all funds available for investments and manages the portfolio. Thus, the funds from the Multilateral Fund enjoy the preferential rates obtained by UNIDO on the overall fund balances kept by UNIDO, including the diversification of its funds held for future use and thus, has a significantly reduced risk exposure. The annual interest rate is not a function of the year-end balance of funds held for the Multilateral Fund but rather the current size of the total UNIDO investment portfolio throughout the year, the preferential rates and other market conditions. Interest earned is based on varying amounts held/invested and the rate is an average for the organization's investments. The investment team looks at the yearly requirements and uses average figures in undertaking investments.

50. The World Bank's investment strategy is to pool the funds of the Multilateral Fund with others across several donor-funded programs and the co-mingled funds and invested by the Bank's Treasury Department. The investment income of each fund consists of the trust fund's allocated share of the following: interest income earned by the pool, realized gains/losses from sales of securities and unrealized gains/losses resulting from recording the assets held by the pool at fair value. The rate of return on investment is for the pool as a whole not specific to any fund alone. The rate of return is calculated on annual basis for the investment earnings[8]. There a few cases where the Bank serves as a trustee and donors have asked to increase the risk profile of their investments with explicit instructions to the trustee.

Interest earnings

51. Interest earnings and investment incomes are normally done on the basis of the rates calculated on the daily balances in the accounts or rates at which investments have been locked for a designated period of time but normally calculated on a daily basis and the reporting is done either daily or at the designated points of reporting. Thus, the interest accounted for in the accounts does not necessarily reflect all the earnings for the period reported as the posting of some of these might be at some future point or might even include some for previous periods during which the same was not reported. Looking at the year's interest earning based on the surpluses of any point of time in the year or even the average surpluses held during the year serves to give only a very indicative figure for comparing without any exactitude.

52. The interest income to the Multilateral Fund has been a very important component of the mechanism and over time has contributed to US $211[9] million as at the 72nd meeting of the Executive Committee.

53. The interest earnings and rates of the implementing agencies fluctuated a lot as pointed in the paragraph below and indicated[10] in Table 2 and Figure 2. For the sake of having some comparability between the implementing agencies the rates have been calculated using the interest earnings as a percentage of the average yearly fund balances -the average yearly fund balance calculated as an average of the beginning and ending balances.

[8] As a financial institution, the Bank uses a standard formula to calculating rates of return from its investment portfolio, including the trust fund portfolio which includes the OTF balance. Eligible investments are highly rated fixed income securities rated AA- or better for governments and agencies, and AAA for corporates and asset-backed securities.

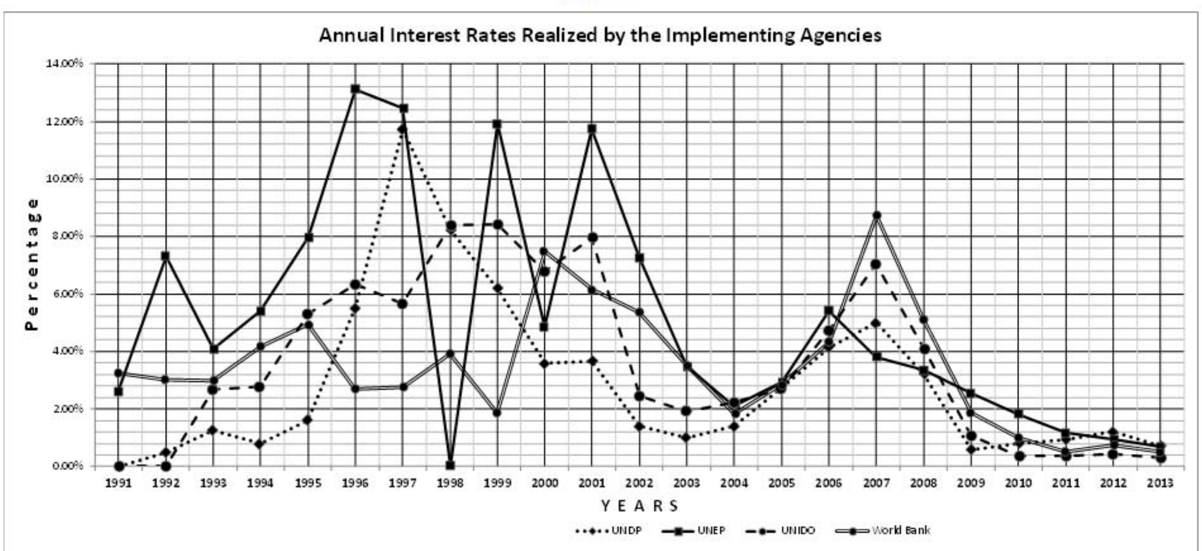
[9] **UNEP/OzL.Pro/ExCom/72/47** Annex I page 1 of the Treasurer's the Status of the Multilateral Fund Report.

[10] **1991-2013 Interest Rates** realized by the implementing agencies, calculated using interest earning based on the average fund balance determined as the average of the beginning and ending fund balance, for purposes of comparability **Table 2** and **Figure 2**.

Table 2. Implementing Agencies Interest Earnings and Interest Rates

Year	UNDP			UNEP			UNIDO			World Bank		
	Average Yearly Balances (US$)	Interest Earnings (US$)	Annual Rate %age	Average Yearly Balances (US$)	Interest Earnings (US$)	Annual Rate %age	Average Yearly Balances (US$)	Interest Earnings (US$)	Annual Rate %age	Average Yearly Balances (US$)	Interest Earnings (US$)	Annual Rate %age
1991	872,957	0	0.00	927,782	24,172	2.61				3,609,414	116,741	3.23
1992	5,256,884	25,937	0.49	1,036,947	75,848	7.31				20,950,328	630,569	3.01
1993	14,072,529	176,914	1.26	2,877,856	117,320	4.08	3,109,457	82,813	2.66	58,087,780	1,736,608	2.99
1994	45,384,911	357,010	0.79	5,477,051	296,439	5.41	21,529,345	597,192	2.77	75,381,543	3,143,566	4.17
1995	72,117,790	1,166,045	1.62	4,269,074	339,902	7.96	46,905,003	2,486,948	5.30	93,077,415	4,588,362	4.93
1996	76,779,412	4,220,730	5.50	2,329,205	305,567	13.12	56,117,277	3,550,981	6.33	136,702,605	3,674,684	2.69
1997	83,001,559	9,734,082	11.73	2,309,288	288,029	12.47	55,471,350	3,147,059	5.67	152,273,463	4,202,532	2.76
1998	91,167,908	7,512,267	8.24	2,757,604	615	0.02	52,538,547	4,403,236	8.38	134,688,757	5,280,746	3.92
1999	96,866,644	5,999,096	6.19	7,017,582	835,769	11.91	45,885,713	3,860,135	8.41	150,479,393	2,820,239	1.87
2000	84,854,151	3,039,689	3.58	8,585,622	417,490	4.86	35,820,206	2,431,724	6.79	153,390,325	11,491,927	7.49
2001	72,622,299	2,664,073	3.67	5,436,585	638,344	11.74	29,016,041	2,308,795	7.96	127,469,757	7,835,561	6.15
2002	74,318,455	1,038,314	1.40	8,728,304	632,720	7.25	27,878,780	682,967	2.45	115,913,725	6,206,417	5.35
2003	77,973,971	783,950	1.01	11,814,764	410,315	3.47	30,299,560	581,257	1.92	111,303,697	3,892,206	3.50
2004	82,787,987	1,155,846	1.40	15,702,533	330,448	2.10	36,497,987	813,953	2.23	113,525,555	2,083,040	1.83
2005	95,465,803	2,608,285	2.73	20,158,227	589,730	2.93	55,056,988	1,488,686	2.70	98,633,159	2,804,319	2.84
2006	100,319,164	4,163,160	4.15	19,595,546	1,061,640	5.42	61,144,290	2,887,492	4.72	97,539,677	4,233,849	4.34
2007	91,620,854	4,572,673	4.99	20,926,138	797,549	3.81	48,809,495	3,438,100	7.04	98,348,690	8,590,765	8.74
2008	86,329,509	2,773,842	3.21	23,215,102	776,656	3.35	50,773,596	2,069,908	4.08	68,668,129	3,513,094	5.12
2009	72,432,571	416,843	0.58	22,804,846	582,958	2.56	52,053,121	559,162	1.07	50,024,326	937,060	1.87
2010	58,590,949	467,358	0.80	22,147,757	403,171	1.82	62,151,319	226,429	0.36	39,169,664	387,337	0.99
2011	72,258,612	671,101	0.93	22,999,018	271,314	1.18	102,367,954	369,007	0.36	48,268,785	244,055	0.51
2012	87,068,918	1,051,278	1.21	26,480,873	252,063	0.95	108,454,344	465,222	0.43	63,350,527	462,598	0.73
2013	84,726,302	600,000	0.71	31,409,310	215,731	0.69	82,788,648	248,761	0.30	60,437,332	303,250	0.50

Figure 2



54. Over the time the interest earnings of each implementing agency were highest in absolute terms in the late 1990's and early 2000's and then decreased to their lowest in about 2004 and then started growing to another high, of less magnitude than the earlier highest, in 2007 and thereafter the annual earnings have been going down. Definitely, the years of 2010 to 2013, and stretching into 2014, have been the lowest in interest earnings for the Multilateral Fund. This is typically a reflection of the diminished global opportunities and it is not limited to the Multilateral Fund only. Even the GEF[11] experienced seriously falling annual investment return rates from 2.9 per cent in 2010 to 0.10 per cent to in 2013. The trend in the interest earnings for the next triennium is more likely to remain at about the low levels of what is being currently experienced and if it goes up it will not be by much.

55. The aggregate view of the totality of the implementing agencies (Table 3) mirrors the above story whereby the interest earnings grew steadily along with the interest rates of a little less than 3 per cent from the beginning to the level of US $17 million in 1997 and a rate of 6 per cent and remained at that high level for five years during which a dip to US $13.5 million was experienced in 1999 during which the interest rate was at 4.5 per cent. Thereafter there was a decline in both the earnings and rates from 2001 to the lowest in 2004 with the earnings of US $4.3 million and rate of 1.76 per cent. From that low there was a rise to the 2007 short peak earnings of US $17.4 million and rate of 6.7 per cent which was followed by a continuous decline to the low earnings of US $1.3 million and rate of 0.53 per cent in 2013.

Table 3. Total Implementing Agencies Annual Average Fund Balances, Interest Earnings and Rates

Year	Annual Average Fund Balances (US$)	Annual Interest Earnings (US $)	Annual Interest Rates (%age)
1991	5,410,153	140,913	2.60
1992	27,244,158	732,354	2.69
1993	78,147,622	2,113,655	2.70
1994	147,772,849	4,394,207	2.97
1995	216,369,282	8,581,257	3.97
1996	271,928,498	11,751,962	4.32
1997	293,055,659	17,371,702	5.93
1998	281,152,816	17,196,864	6.12
1999	300,249,331	13,515,239	4.50
2000	282,650,303	17,380,830	6.15
2001	234,544,682	13,446,773	5.73
2002	226,839,263	8,560,418	3.77
2003	231,391,992	5,667,728	2.45
2004	248,514,061	4,383,287	1.76
2005	269,314,176	7,491,020	2.78
2006	278,598,676	12,346,141	4.43
2007	259,705,176	17,399,087	6.70
2008	228,986,335	9,133,500	3.99
2009	197,314,863	2,496,023	1.26
2010	182,059,688	1,484,295	0.82
2011	245,894,368	1,555,477	0.63
2012	285,354,661	2,231,161	0.78
2013	259,361,592	1,367,742	0.53

56. The possibility of pursuing the option of letting the implementing agency which is more likely to realize the best returns do it for all the others is more likely not possible because of the difficulties of any implementing agency keeping up with not only constantly re-evaluating the surplus amount available for passing to the other entity but also the difficulties of getting these resources back in a timely way.

[11] **GEF/R.6/Inf.8** – Third Meeting for the Sixth Replenishment of the **GEF** Trust Fund, Page 8 – Investment Returns Graph.

57. The World Bank has categorically indicated that the trouble to take up such an assignment is not worth it unless it is asked to take up the role of trustee altogether. The other implementing agencies share similar sentiments with regard to the additional work and the Treasurer will similarly experience the same difficulties if the surplus funds were to be passed to another institution for investment.

58. With regard to tracking interest income at the beneficiary level or country level the implementing agencies have different policies. UNDP keeps its operations to three months cash advance for items it cannot disburse for directly and as a result the amounts involves are too small to attract any interest income of material significance. UNIDO works in a centralized manner handling most of the procurements and disbursing directly and it too does not have a policy of tracking interest earnings by beneficiaries. The World Bank’s policy is to have the interest income accounted for and audited but it considers it to belong to the beneficiary country and to be re-ploughed into the project. UNEP is the only one where cash advances to beneficiaries require interest income to be reported and it captures this element in its accounts of interest earned reported.

Recommendations

59. The Executive Committee may wish to:

(a) Note the report on Fund Transfers from the Treasurer to the Implementing Agencies (decision 72/42(b)(ii) and (iii)) contained in document UNEP/OzL.Pro/ExCom/73/57;

(b) To commend and encourage the Secretariat to continue with its constant quest for ensuring that all possible measures of efficiently using the funds of the Multilateral Fund are deployed at all times as this contributes a lot to maximizing the achievements of the Multilateral Fund;

(c) To review the advantages and disadvantages of either the transferring full funds to the implementing agencies for the approvals it grants or the transferring to the implementing agencies partial funds based on their periodic needs and decide which option it wishes to go forward with;

(d) To consider, in case the Executive Committee decides to move ahead with the partial transfer of funds as serving the interests of the Multilateral Fund best, introducing it for an initial period of say two years and at the end of which an evaluation on its feasibility of going on with it would be made for its decision;

(e) To note that interest earnings are a product of the implementing agencies prudence in their management of the resources of the Multilateral Fund and that higher realizations tend to be during the times the global investment returns are good;

(f) To note the lack of comparable relationship between the 20 per cent disbursement threshold for HPMP tranches and the UNEP-wide standard cash advance guidance except for the underlying intention of both being intended to prudently manage the resources for projects implementation. But the UNEP guidance is targeted to specifically project activities by executing agencies and not to implementing agencies managing a portfolio of projects; and

(g) To note that although there have also been other times when the Multilateral Fund experienced high ratios of 3:1 and above, of the surplus fund balance relative to the expenditures in the year, for a lot more years the average of this ratio averaged at about 2:1.