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DU FONDS MULTILATÉRAL AUX FINS  
D'APPLICATION DU PROTOCOLE DE MONTRÉAL  
Trente-septième réunion  
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**EXAMEN DE LA POLITIQUE ET DE L'UTILISATION DES  
FRAIS ADMINISTRATIFS A LA BANQUE MONDIALE EN VERTU DU FONDS  
MULTILATERAL AUX FINS D'APPLICATION DU PROTOCOLE DE MONTREAL  
(SOU MIS PAR LA BANQUE MONDIALE)**

**Note du Secrétariat**

1. La Décision 36/47 demandait, entre autres, un rapport à la Banque mondiale sur les frais administratifs et leur utilisation, en particulier pour le secteur de la production de CFC du Programme de travail annuel de la Chine pour 2002 et, de façon générale, sur les plans sectoriels d'élimination.
2. La Banque mondiale a soumis ce rapport le 19 juin 2002, après que le Secrétariat ait affiché sur son site Internet la documentation sur les projets achevés avec soldes (UNEP/OzL.Pro/ExCom/37/9) et sur le secteur de la production (UNEP/OzL.Pro/ExCom/37/69).
3. Le Comité exécutif pourrait souhaiter examiner ce document dans son examen de la question des frais d'appui soulevée dans le contexte des projets achevés avec soldes pendant le Sous-comité de la surveillance, de l'évaluation et des finances, ainsi que les informations particulières relatives au secteur de la production en Chine et aux plans sectoriels d'élimination pendant le Sous-comité sur l'examen des projets.

**A Review of the Policy and Use of Administrative Fees at the World Bank  
under the Multilateral Fund for the Implementation of the Montreal Protocol**

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## Introduction

The 36<sup>th</sup> Executive Committee (Dec. 36/47) requested the World Bank to prepare a paper on how the administrative fee for the CFC production closure plan for China was to be used; how sectoral and national phase-out plans were implemented and how those related to administrative costs charged for other World Bank activities; and, what financial oversight was exercised over the technical assistance program. The 16<sup>th</sup> Sub-committee on Monitoring, Evaluation and Finance expressed an interest in seeing such a paper, in particular in regards to policies and procedures on support costs and options for their return to the Multilateral Fund (MLF).

The Executive Committee's request for information on the use of support costs by the Bank coincides with the Bank's recent decision to take stock of its portfolio of projects and the cost to deliver these projects in its role as an MLF Implementing Agency (IA). This assessment was spurred by the gradual change in the support cost regime in the last few years to accommodate larger projects and the growing impetus for support cost reporting. The paper will thus respond to the Executive Committee's request within the context of several general concerns:

*The increased emphasis by the MLF on de-linking individual projects from the IAs' overall portfolio of projects in terms of administrative fees and associated reporting at the same time that emphasis is being placed on delivering comprehensive programs consisting of investment and non-investment activities and technical and policy advice to assist both small and large consuming countries achieve compliance.*

- Leveraging funds under the fee-based system
- The Bank's mode and cost of operations
- Options for, and implications of the return of support costs

*A shift in the MLF's portfolio as a result of strategic planning for the compliance period from individual projects to comprehensive sector and national plans, and, the resulting affect of a varying administrative cost ratio on the Bank's approach to utilizing support costs.*

- Services provided for sector plans
- Services provided for national plans
- Traditional projects and new monitoring and evaluation requirements

*The recognition, based on historic data, characteristics of the Bank's current portfolio and likely trends, that support cost funding might not be sufficient to cover all future commitments.*

- Premises surrounding the adoption of a fee-based support cost system in 1995
- Project management cost outcomes and contribution to current administrative costs.

*The possible ways forward for the Bank to ensure fulfillment of its ongoing Montreal Protocol portfolio commitments to its client countries and the MLF Executive Committee.*

- Advantages of a fee-based support cost regime over a direct cost-based regime
- Experience of the GEF
- Variations on the fee-based support cost regime
- Conclusions on the possible way forward

In Part I of the paper, the Bank will provide a synopsis of findings and concerns as delineated above, and its conclusions. In Part II, the underpinnings of conclusions in Part I are presented by providing an overview of Bank operations and the project cycle, the evolution of the use of support costs at the Bank since the inception of the Montreal Protocol (MP) program within the context of overall Bank operations and corroborated data on the Bank's assessment of its use of administrative fees and the administrative fee policies over the last decade.

## **PART I – Findings and Conclusions on the Bank’s Experience with the MLF Support Cost Regime**

*There appears to be an increased emphasis under the MLF to treat administrative fees of individual projects separately from the IAs’ overall portfolio while encouraging development of more holistic projects.* In recent Executive Committee meetings, concerns have been expressed on the use of support costs in both sector and national plans and traditional projects to the degree that it has become a requirement to monitor and report on a project-by-project basis the use of support costs. Concomitantly, IAs have been encouraged to embrace new comprehensive programs in countries with various levels of ODS consumption and technical capacity which involve a host of unknowns in regards to costs of delivery, and which inherently demand flexibility in agencies’ use of support cost funding. This dichotomy mandates clarification by the Bank of its use of support costs in relation to its operations and understanding of its agreement with the Executive Committee.

- The World Bank has successfully demonstrated its ability to apportion its services according to need of individual countries. It is clearly understood that a country’s size, capacity, geographic location, economic situation and market structure will contribute to the cost of servicing that country. The past fee-based system has enabled the Bank to take advantage of its comparative advantage – the ability to identify specific client-country needs and the operational structure to allow it to adjust its services at the level required.
- The dissection of the costs needed to provide all services for individual, traditional projects is a task which is difficult under the Bank’s system of operation and also contradictory to the efficient use of support cost funds. Unlike the other IAs, the Bank operates under national execution which places emphasis on building ownership and local capacity in its client countries. In addition, national execution means that all approved project funding goes directly to the country which is not the case in other implementation modalities. The Bank’s approach is thus in line with the 1998 consultant paper on administrative costs which delineated what administrative fees were not eligible, including any costs charged to projects.<sup>1</sup> MLF project implementation is, in part, done by a country entity, the financial intermediary (FI), which is contracted by the Bank and the client country in the umbrella agreement at 3% of the project cost. The remaining support costs goes towards one, the Bank country team, which is most intimately involved in the project cycle and with the client – from project conceptualization to financial completion, and two, the coordination unit – the MLF liaison and policy promulgator.

The Bank has, historically, operated at a US \$4.5 to \$5.5 million budget based on a US \$50-\$60 million allocation with the coordination unit operating at a consistent \$1.4-1.6 million over the last decade. The variable in administrative costs has been the supervision cost, or the cost of the Bank country team. This again reflects variability in client countries, their private sector and the economic situation. For example, the average cost of supervision alone by Bank country teams in certain Latin American countries where there have been delays and other difficulties has averaged above 30% of project costs, whereas, in East Asia, it has averaged between 3-4%.

If one considers a US \$100,000 project with a duration of four years, the normal distribution of support cost funding at 13% of the project cost would be, for the first year, \$6,000 for upfront costs of the coordination unit and commitments to the FI, \$1,750 for supervision, and for each of the remaining three years \$1,750 for supervision. This is, essentially, the amount available from the project alone, for completing all required project implementation and monitoring and evaluation activities, including the trips to the country for supervision. (If delays or other

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<sup>1</sup> “Analysis of Options to Reducing the Level of Implementing Agencies’ Administrative Costs,” UNEP/OzL.Pro/ExCom/26/67, Twenty-sixth Meeting, Cairo, 11-13 November 1998.

problems which require more work by the IA and FI are factored into the equation, additional costs accrue quickly.)

Under national execution, MLF projects fall under larger umbrella agreements the Bank has with clients which lay out implementation arrangements and country obligations and requires that the FI enter into a “sub-grant agreement”(SGA) with the beneficiary enterprise. As soon as the SGA is signed, total MLF funds approved for that particular project are considered fully committed. This is also the case with the FI’s fee because as the Bank is contractually obligated to reimburse the FI with 3% of project costs, it cannot accept the liability associated with withholding administrative funds from the FI. In addition, similar to the manner the Bank leverages support cost funding to manage its entire portfolio, the FI is permitted to also leverage its 3% fee. This is crucial considering that most FIs are commercial banks yet must implement not only larger projects but also small projects with low funding levels. Under normal commercial practices, an end-date would be agreed upon with the FI in the agreement, however, because the end-date is basically set by the Executive Committee with its definition of project completion, FIs can be implicated in projects which suffer long delays, without the possibility of receiving support costs beyond the 3%.

This policy on committed funds applies to the 3% FI support cost fee and the Bank’s cost as well. In cases where projects have been completed as planned but result in a savings, the Bank is obligated to compensate the FI for its 3% fixed cost, and has, under the support cost regime, and as understood when it agreed to apply the fee-based system in the mid-1990s, utilized the difference in savings where it was not sufficient in other projects.

- In the present support cost system arrangement as understood by the Bank, options for return of support costs present themselves in cases where projects are cancelled or project components are cancelled. However, depending on the stage of the project when it is cancelled, support cost return can vary and does not necessarily have a direct relationship to disbursement but rather to the level of funds committed (please recall the Bank’s contractual obligation to FIs) and the services provided at the time of cancellation.

The Executive Committee now appears to be moving towards considering support costs on a project-by-project basis which has, to date, entailed returning the same percentage of support cost received on any project savings. There are practical implications to this approach which bring to bear the original agreement with the Bank and the Executive Committee. It states that the Bank will make no commitments for financing in advance of receipt of financing and that it will be reimbursed annually in full for expenses incurred. Thus, if the MLF support cost regime is to require the return of proportional support costs on savings on a project-by-project basis, there must also be, simultaneously, a mechanism in place to compensate IAs on a project-by-project basis where support costs have exceeded the support cost allocation. This would not include the upfront expenditures already incurred for the FI and MP coordination unit. A mechanism would have to be put in place within the Bank to allow reimbursement to the FI as well in cases of overruns. In addition, it should be understood that the tracking and reporting of costs on an individual basis in order to return or claim support cost funding in proportion to project savings or expenses will result in a higher administrative fee transaction cost.

***The new strategic direction of the MLF and the increasing prevalence of multiyear, comprehensive sector and national plans, at the same time that traditional projects continue to be implemented and more closely monitored than ever before, present a diversification in the administrative functions of the IAs and also have resulted in an alteration of the fee-based support cost system to one of varying administrative cost ratios.***

- The work entailed in implementing and monitoring annual programs under sector plans is more significant than what appears to be the currently held conception. Experiences from the halon and CFC production sector plans show that considerable monitoring activities, and more importantly, close and continual policy and technical support to the NOU are required. Reporting and verification activities must be undertaken by the IAs in accordance with the new Executive Committee guidelines. Although the support cost ratio is decreased in sector plans, the Bank continues to contract FIs to assist in implementation at approximately the same rate as in other projects – 3% of the project cost. Coordination unit costs which have been proportionate to the FI fee are also constant. The performance and technical audit, is at approximately US \$100,000, about 1% of the annual tranche.

The 7% approved for the 2002 CFC production sector annual program thus makes up these three costs (FI fee, coordination unit cost and the audit), leaving no funds for the country team's cost. The 2001CFC production annual program, for which support costs were fixed at 9%, had, for example, an actual administrative cost of 9.2% of total project funding. (Please see Annex I for the list of administrative costs incurred by activity and by agent.)

The technical assistant (TA) component of the production sector plans is directed by Bank operational guidelines and monitored by several mechanisms. In China, the process begins with agreement on the terms of reference (TOR) for the TA prior to the submission of an annual program. A consultant is selected to carry out the TA, according to Bank procurement rules, and enters into an agreement with the government. The government will provide the Bank with quarterly reports which include disbursement information on the TA and the Bank, in turn, provides total disbursement information on the plan in its annual progress report. The Bank's disbursement to the government is linked to the implementation of TA activities. When the TA is completed after two to three years, a *performance* audit is done by a national agency selected by the government and the Bank, and a *financial* audit of both Bank and government accounts is performed. Finally, the Bank will conduct its own financial audit and contract an outside consultant to perform a *verification* audit which reviews and summarizes all activities and the assessment of performance by the country.

- Because the implementation of national plans has only begun, the type and level of IA support that will be required from year to year is not certain. However, with the knowledge that most remaining ODS consumption in countries that are advanced enough to receive funding for comprehensive and final phaseout efforts is in the more difficult sectors (small- and medium-sized enterprises (SMEs), residual, end-user), it is safe to assume that technical and policy support will be of a more intensive nature. Depending on the implementation modalities selected, it is expected that the first two years of a national plan will be administratively challenging as required implementation arrangements among stakeholders are set up and the Project Implementation Unit is created and launched. The process of, and resources for building capacity within the PIU and other concerned agencies to initiate and implement projects, develop policy, build public awareness, coordinate the overall program and manage financing will vary country to country.
- Amidst these new project developments remain a large number of traditional investment projects to implement and see to completion. (There will be new traditional investment projects as well). Unlike sector plans, the support cost approved is for the entire project cycle. Several papers have been presented to the Executive Committee that identify the administrative activities required of the IAs. The last detailed report was the 1998 administrative cost paper provided to the 26<sup>th</sup> Executive Committee in Cairo. One notable change in the activities since first delineated is in

regards to monitoring and evaluation. The Executive Committee has increased monitoring and evaluation responsibilities of the IAs to present at every meeting reports on delayed projects and completed projects with balances, PCRs (which have their own host of evolving data requirements) and any additional data and reviews required by the MLF Senior Monitoring and Evaluation Officer on an ad hoc basis. These reports require intensive stakeholder consultations.

In addition, the standard progress report has of late been amended to include more details, such as support cost expenditures on a project-by-project basis and current details and forecasts on multiyear projects. Positioned adjacent to projects suffering delays, these reporting activities do consume a large portion of support cost resources.

Thus, despite the gradual shift to country-driven programming, there are many factors to consider when assessing the costs to IAs for administering projects. The increased costs of monitoring traditional projects and the narrowing in of support costs in sector plans to the exact or lower amount required, has a real affect on the Bank's current portfolio and carries implications for operations in the near future.

***Based on historic data, characteristics of the Bank's current portfolio and likely trends, support cost funding, at its current level, might not be sufficient to cover all future commitments.*** Assessments of how to treat support cost funding and to determine the support cost ratios required in future sector and national annual plans under the current system, cannot be done without considering assumptions and understandings from the past on support costs.

- The transition by the Bank in 1995 from a cost-based system to a fee-based system was done on the understanding that the support cost funding received on projects receiving funding at the 18<sup>th</sup> Meeting and future projects would be utilized to cover administrative costs associated with the US\$180 million ongoing portfolio of projects at the time of the changeover. This condition was essential for the Bank, because by changing to the new support cost regime without requesting additional funds to cover ongoing projects, the Bank had to ensure that it would have sufficient funds to complete its ongoing commitments.

The second understanding when the Bank moved to a fee-based system was that any support cost savings at the end of the ODS program would be returned to the Fund. In order to determine the extent of the funding required to absorb costs of ongoing projects with future fees, the Bank performed an analysis of total approval, disbursement and support cost expenditure data for each of its 21 client countries which had ongoing projects 1996-2001. The Bank found that the average cost of implementing projects, although increasing progressively since 1997, resulted in 10% of project costs based on a simple analysis of total funds disbursed. Based on this percentage rate and the US\$137 million of undisbursed funds at the time of the transition to the fee-based system, the Bank estimates it has foregone US \$13.8 million in support costs.

- Extending the analysis to the Bank's current portfolio, it is seen that as of the end of 2001, required support costs associated with undisbursed funding of over US \$110 million would be US \$11.3 million based on the historic rate of 10%. The remaining total balance of support costs at the end of 2001 is US \$10.46 million demonstrating that there will be nearly a US \$1 million *shortfall*. However, in line with its agreement with the Executive Committee, the Bank understands that it must honor its commitments and complete implementation of the ongoing project portfolio within the remaining balance of funds.

With the assumption that the balance of support cost funds will be set aside to manage the Bank's remaining commitments, that all services required in project delivery over the last three years remain approximately the same and that the support cost rate for sector plans is reinstated at 9%

of project cost, the Bank believes it can continue operations based on a US \$52 million budget at an average 11% support cost rate. This is in spite of the current trends in new MLF project composition, projects with delays and the increased reporting requirements. However because of these very reasons, 11% cannot be guaranteed. Any rate below 11% appears to involve the risk that the Bank will not have sufficient funds for ongoing administrative and supervision activities. This burden cannot be assumed by the Bank according to its agreement with the Executive Committee.

*Considering the present situation, there are several possible ways forward in regards to administrative fees.* Clearly under the current, evolving support cost system of variable percentage rates and support cost returns for individual projects, there is increasing concern by the Bank in regards to having sufficient resources to be able to plan and budget funds in the immediate future in order to ensure staff and program continuity, honor its financial commitments to FIs and to complete the project cycle of all ongoing projects. At the same time, it is understood that the Executive Committee must be able to know with a sufficient level of confidence that administrative fees approved have been used in the most efficient manner possible. The Bank sees a need for adjusting the support cost regime to honor its project commitments in the most efficient and effective manner possible while providing the Executive Committee assurances that support cost expenditure is proportionate to project need. This conclusion is a result of investigating concerns expressed by Executive Committee members who requested more information on the use of administrative fees, in particular, in sector and national plans and in cases where there are project savings.

A review of past support cost policy papers and correspondences from the Secretariat and IAs, and the Global Environment Fund's own experience with support costs reveal several possible ways forward. Under the general rubric of administrative fee modalities, there are basically two that serve as a point of departure for tailored approaches – a fee-based system and direct cost system.

- The Bank began serving as an implementing agency under a direct cost approach, with the exception of the FI fee which was approved at 3% of the project cost. Although this system is perceived to provide a somewhat higher level of control for the Fund's custodians, it does involve a level of complexity that is not present in a fee-based system. All planned, eligible, but indirect administrative costs, such as training, would be itemized in an annual work plan, reviewed and cleared for funding. After the year is completed, depending on the expenses and the number of unforeseen developments, costs would be compensated or savings credited to the Fund. This approach would involve a higher administrative transaction cost, make predictability in administrative cost budgeting difficult year to year and reduce the level of comparability of cost of projects and IA performance.
- The GEF also abandoned this approach in 1999 when it too adopted a fee-based approach. The GEF's model is based on a flat fee according to four standard project types. However, the system allows for fee premium requests by IAs to be negotiated with the GEF Secretariat in cases where there is a higher level of project complexity or other project-specific issues, and to allow IAs to allocate support cost funds according to project need in their portfolios. It was determined in a recent consultant report<sup>2</sup> that the reliance on negotiations by stakeholders for each project with unique characteristics increases transaction costs and duration of the administrative fee process. The GEF is currently assessing the flat fee structure after three years of use for effectiveness of project implementation and cost management and to determine how to make the system more cost-effective. A result of this assessment may be a freeze on the support cost percentage across agencies.

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<sup>2</sup> "Consultant's Report on an Independent Review of the Fee-based System," GEF/C.19/12, April 19, 2002.



- The 1998 consultant report presented to the 26<sup>th</sup> Meeting of the Executive Committee similarly proposed, based on the consultants findings, that 11% of project costs would be a sufficient level of funding and that 10% might be feasible in the future assuming that MLF expenditures remain the same or increase and that national executing agencies are employed more gainfully.
- Excluding a direct-cost approach, which has been demonstrated to present more disadvantages than advantages both in the MLF and the GEF, the fee-based system appears to be the most attractive approach. There are, however, several feasible derivatives of a fee-based system. Advantages and disadvantages are outlined below.

**Table 1. Variations on a Fee-Based Administrative Cost Structure**

<b>Administrative Fee Modality</b>	<b>Description</b>	<b>Pros</b>	<b>Cons</b>	<b>Experience with this Approach</b>
Flat fee at a fixed rate for all projects and programs	One administrative cost ratio determined for all projects for a set allocation of project funds.	<ul style="list-style-type: none"> <li>• IA covers all its costs regardless if it exceeds the agreed rate on an individual project basis.</li> <li>• Fee is for full project cycle.</li> <li>• No liabilities to the MLF.</li> <li>• Project implementation not stalled due to insufficient funds.</li> <li>• Predictability of support cost funding required for financial management at the MLF level and at the IA level.</li> <li>• Provides incentive to develop innovative projects.</li> </ul>	<ul style="list-style-type: none"> <li>• Perceived lack of transparency by ExCom/ Secretariat.</li> <li>• Fee will not approximate real costs if total funding in portfolio decreases.</li> </ul>	Under the MLF's current system, and an allocation of US\$52 million, present and expected future costs average at 11%.
Combination of a fee-based approach with direct costing.	Fixed allocation for core unit [and FI]; Supervision funding given upfront with premiums/discounts negotiated in the context of a work program	<ul style="list-style-type: none"> <li>• Transparency in that support cost allocated for general groups of activities is known to ExCom/Secretariat.</li> </ul>	<ul style="list-style-type: none"> <li>• Higher admin. fee transaction cost</li> <li>• Longer admin. fee transaction process</li> <li>• Overall funding needed for support cost budgeting uncertain</li> <li>• Review process is more time consuming.</li> <li>• As business changes in sunset years, core unit funding needs might change.</li> </ul>	
Staggered fee (GEF)	A flat-fee is agreed upon depending on project type with possibility for negotiating premiums or discounts.	<ul style="list-style-type: none"> <li>• A degree of predictability in determining funding required for financial management at the GEF level.</li> <li>• Fee is for full project cycle.</li> </ul>	<ul style="list-style-type: none"> <li>• Higher admin. fee transaction cost</li> <li>• Longer admin. fee transaction process</li> <li>• Negotiating process reduces equity across IAs and EAs.</li> </ul>	GEF has utilized this approach for approximately 3 yrs yet is in the process of revising it.
13% fee-based system, adjusted, with direct-cost reporting (current approach under the MLF)	Basic premise is a 13% fee based-system which allows variable rates for sector and national plans and now requires project-by-project administrative fee costing and reporting.	<ul style="list-style-type: none"> <li>• The IA covers all its costs regardless if it exceeds the agreed rate on an individual project basis.</li> <li>• Increased transparency as exact support costs of projects with savings is reported.</li> </ul>	<ul style="list-style-type: none"> <li>• Uncertainty in ability of IA to fulfill project commitments</li> <li>• Liability to the Fund if fees are insufficient.</li> <li>• Project implementation stalled due to insufficient funds.</li> <li>• Increased transaction costs for tracking support cost expenditure.</li> </ul>	Since the 26 <sup>th</sup> ExCom Meeting, the variable rate approach is used to differentiate between high cost and/or negotiated projects. Support cost reporting was begun at the 35 <sup>th</sup> ExCom Meeting.

In conclusion, a decade of support cost expenditures provides a solid starting point for determining future need. There are undoubtedly still uncertainties in choosing support cost ratios for services provided in the future given the experience with sector plans, where the primary recipients of project funding were large ODS consumer and producer countries with straightforward ODS sector phaseout, the limited experience with national ODS phaseout plans and, in general, erratic project durations. Given the advantages of a flat-fee approach, however, the Bank believes it can operate at a fixed 11% project-support cost ratio based on the current allocation and under the following circumstances:

- A return to 9% support cost funding for the CFC production sector annual plans.
- The understanding that the current support cost balance with the Bank will be made to be sufficient for fulfilling all its remaining project commitments.
- Continuation of the Bank's approach to utilizing agency fees to manage its overall portfolio.

In this context, the Bank would like to reaffirm its commitment to the original agreement with the Executive Committee which states that any savings would be returned to the MLF at the end of the ODS programs.

## **PART II - Review of Policy and the Use of Administrative Fees at the World Bank**

The main issues influencing the Bank's conclusions on support costs are underpinned in the following text. In order to present committee members with corroborated data on the Bank's assessment of its use of administrative fees and the administrative fee policies over the last decade, the Bank has reviewed accounting and operational documentation, conducted a financial analysis of costs based on the project cycle and historic trends and referred to other policy papers on administrative fees, including the consultants report presented to the Executive Committee at the Cairo Meeting in 1998.

### **Background to Bank Operations**

Montreal Protocol operations at the Bank were incorporated into the Bank's overall operational policies, which is reflected in the agreement between the Executive Committee and the World Bank whereby the Bank will assist countries implement MLF projects by "following its rules and procedures [...]".<sup>3</sup> Thus, MP Operations at the Bank are based on guidelines and policies governing the implementation of large loans, many times of over US \$50 million.

A fundamental principle in Bank programs is national execution which gives client countries project ownership. This principle correspondingly led management to integrate MLF activities for a particular country into a comprehensive ODS phaseout program under one umbrella grant agreement. This type of arrangement was a result of streamlining normal loan procedures to be able to incorporate numerous small grant projects that were atypical to the Bank. National execution is now also pertinent to the MLF in light of the strategic planning exercise that focuses on country-driven approaches.

The implementation mechanism which is determined in an umbrella grant agreement, consists of the lead government agency as coordinating body, a local bank or consulting firm as the executing agency, or financial intermediary (FI), to conduct certain implementation duties in exchange for a fee, and, Bank staff to provide oversight, technical backstopping and guidance. All procurement and disbursement is based on Bank guidelines and the MP project cycle is supplemented by other Bank requirements such as project appraisal, a mechanism to reconfirm the financial viability of the enterprise and technical soundness of the project immediately after project funding is secured and before implementation begins.

There are thus two parallel project cycles, that of the umbrella grant agreement which follows the country<sup>4</sup> project cycle: project identification, preparation, appraisal, negotiations, implementation, monitoring and evaluation/supervision and post-evaluation; and that of the individual MLF "subproject" which is approved by the Executive Committee and falls under the grant agreement. The umbrella agreement reached with a country will include provisions which link government and FI actions to both Bank operational guidelines and Executive Committee decisions and all individual MLF projects are governed by the rules laid out in the agreement. The responsibilities of the FI are negotiated and included in the agreement. For individual MLF projects, the project cycle will include additional components that are specific to Executive Committee project requirements, such as certified equipment destruction and a project completion report (PCR).

In MLF project implementation at the World Bank, several actors are involved with distinct roles and responsibilities: the Bank Task Manager and country team (including legal, procurement and

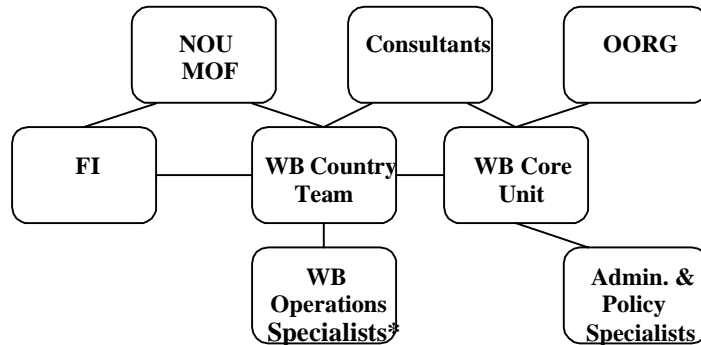
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<sup>3</sup> UNEP/OzL.Pro/ExCom/5/Inf.2 Section B: Operational Procedures.

<sup>4</sup> National execution means that the project cycle belongs to the country, which culminates when the project reaches the operative stage. In normal Bank projects, the goal is to have Initiation, Appraisal, Negotiation, Implementation and Monitoring and Evaluation as the country's responsibility and have Preparation, Negotiation, Supervision and Post-evaluation as the Bank's primary role.

disbursement specialists), the Bank MP coordination team (including budget and information officers, and environmental, legal and technical specialists), the FI, the country counterpart, consultants and an expert review body (Ozone Operations Resource Group – OORG). The implementation arrangement is depicted in Figure 1.

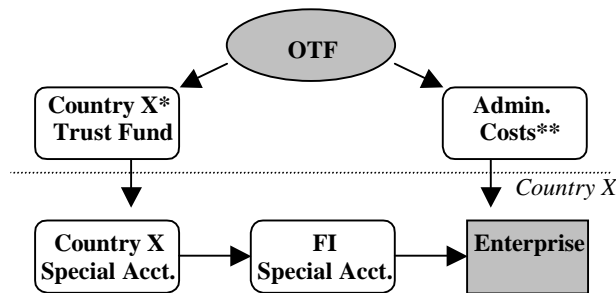
Figure 1.



\*Procurement, disbursement and legal advisors.

Similarly, there is a distinct arrangement for the financing of these MLF projects and their implementation services. Bank rules prevent it from disbursing funds directly to a private entity. In addition, because grant agreements are with the Governments, MLF funding is channeled through the Bank-situated Ozone Trust Fund (OTF) to a trust fund which is linked to a specific grant agreement with a country. Funding from this trust fund will be transferred to a special account that sits with a country ministry of finance, which in turn is disbursed into a special account of an FI (Figure 2). The return of unutilized funds under an umbrella grant agreement which will have several MLF projects is usually done when the project closes.

Figure 2.



\*Includes 3% FI fee

\*\*Includes 10% Agency Fee of total 13%

Although the number of individuals involved in both implementation and disbursement appears to be large, the overall aim is to build country capacity while creating a division of labor on the Bank side to ensure targeted and specialized assistance for various stages of the project cycle in a cost-effective manner. This structure, however, renders the support cost system and the associated use of the fees more complicated as described below under the overview of the Bank’s use of support costs. Please see Annex II for a complete list of responsibilities for Bank staff and consultants and the FI.

## Evolution of the Support Cost System

The support cost system adopted when the Bank became an Implementing Agency for the MLF in 1991 was based on a combination of a direct cost approach where each activity undertaken, including country programs, project preparation, and supervision/coordination costs, was charged back to the MLF and of a fee-based approach where a 3% fee on investment projects to compensate the Financial Intermediary per project was included in project approvals. The other three Implementing Agencies (IAs), all UN bodies, were utilizing a fee-based system.

Because the Executive Committee felt that a uniform support cost approach would facilitate comparability between the IAs, it requested the Bank to also adopt a fee-based system in 1995. A consulting company was hired in the mid-1990s to assess the cost of operations for the IAs and came to the conclusion that 13%, the rate utilized by the three UN agencies, was fairly accurate.

The Bank agreed to make the transition to the percentage fee-based system on the understanding that one, based on the assumption that ongoing projects in the existing portfolio from the previous system would cost an average of 11-12%, the 13% of *future* project approvals, including that of the projects funded at the 18<sup>th</sup> Meeting, would cover the expenses of those projects.<sup>5</sup> The Bank therefore did not ask the Executive Committee for additional support costs to cover the ongoing projects governed by the old support cost regime. Two, that when implementation of the MP portfolio was completed, any savings would be returned to the Fund. This latter understanding was a reiteration of the agreement between the Executive Committee and the Bank that states that the World Bank will hold unutilized resources in the OTF until all commitments and liabilities have been satisfied and project activities have been brought to a conclusion.

The 13% fee-based system was applied through 1998 when the consultant's report on administrative costs introduced several new concepts which resulted in the system's alteration. First, a graduated scale of rates was introduced based on project size in terms of the dollar value of projects. Second, the report defined administrative costs and the corresponding eligible items for compensation to allow for useful comparison and analysis between agencies. Finally, the paper concluded that administrative costs of the agencies averaged at 11% in 1997 and that in future years, it was not unreasonable to target 10%.

The Executive Committee began applying a graduated scale of rates (Dec. 26/41) with a delineation between projects below and above US\$500,000 and below and above US\$5 million:

- 13% on projects up to US \$500,000
- For projects over US \$500,000 and below US \$5,000,000, 13% on the first US \$500,000 and 11% on the balance
- For projects over US \$5,000,000, to assess their value on a case-by-case basis

As sector plans became more prominent and common under the MLF in the last few years, graduated rates for support costs have been replaced more and more by varying rates, because due to individual agreements between the Executive Committee and the beneficiary country, these can be negotiated on an annual basis for a particular sector or national plan. Support costs for sector plans, and more recently, national CFC phaseout plans, have ranged from 7% to 11%. The Bank, which leads IAs

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<sup>5</sup> On the existing \$180 million portfolio at the end of 1995, the Bank would limit administrative costs to 10.5%, including historical costs, FI fees approved for those projects, and 13% agency fee on the new approvals at the 18<sup>th</sup> Meeting of US \$34 million, and not request additional funds to complete supervision of the portfolio. With projections of an overall 11-12% average administrative cost for these ongoing projects, the Bank would apply a portion of the *future* 13% fee to cover expenses beyond the 10.5% received for that \$180 million portfolio.

in terms of the approved number of, and funding level for sector and national plans, has observed the evolution of the agency fee in sector and national plans particularly closely.

## **Overview of Bank's Use of Support Costs**

In order to demonstrate how the agency fee is utilized by the Bank, an outline of the structure of the Bank's administrative system for project implementation is provided, along with a cost analysis of various activities and parameters which affect use of funds, and an overview of the trends in support cost expenditures over the years. Before a useful analysis can be presented, however, the definition of administrative activities should be clarified.

The 1998 consultant's report on the administrative costs of implementing agencies proposed criteria to identify administrative costs which could be considered eligible. These were based on three major categories in project delivery: Project identification, formulation and approval; Project implementation and monitoring; and other activities, including business plan and progress report preparation, providing input to the Secretariat on policy and Executive Committee meeting attendance. The report listed as eligible the following costs:

Direct costs of the coordinating unit:

- Salaries and benefits to permanent and contractual staff
- Travel related MLF activities and monitoring of projects
- Office accommodation and equipment, supplies, telecommunications general expenses
- Contractual services related to activities of the coordinating unit

Fair cost allocation from central support services

- Human resources
- Accounting based on the volume of transactions generated
- Management information systems, based on the proportionate number of workstations and actual systems used by the coordination unit
- Procurement and legal, based on the volume of transactions generated
- General office and administrative services, based on the proportionate number of staff

Fair cost allocation of country or field office costs - Allocation made on the basis of financial activity (MLF spending vs. total agency spending)

Direct costs of the implementing arms – Costs would be established by a service contract and would exclude costs approved as part of the project budget.

The consultant's report also listed items that could be considered *ineligible*, including any costs charged to projects and trips related to activities which are beyond the IA's role. The analysis utilized to generate supporting data on the cost of project delivery to the Bank in this report is based solely on these eligible administrative costs.

## **Structure of the Administrative System and Associated Procedures**

As mentioned above, the Bank uses national implementation, meaning that the Bank supervises the implementation process and a country-entity is responsible for certain implementation duties. Supervision is done by the Bank Task Manager and her or his country team with technical, financial and

policy guidance provided by the coordination, or core unit. The Bank therefore uses a decentralized approach to deliver services for support costs received which can be broken down into three groups: the financial intermediary, the Bank country team and the Bank coordination unit.

The Bank contracts a FI through an Art. 5 government to carry out the implementation, and the FI is paid a percentage of the project funds. The amount is normally a *fixed* 3% of the project cost and payment terms are agreed in the grant agreement with the country along with the actual conditions associated with the work of the FI. They reflect existing Executive Committee guidelines governing use of MLF funds and project implementation at the time the agreement is signed and are consistent with Bank general conditions for agreements. However, some flexibility in the language of the agreement has allowed FIs to absorb evolving Executive Committee requirements, such as additional reporting.

Although the FI performs some essential tasks in implementation, the Bank is responsible for ensuring that all work surrounding project delivery is carried out, in line with Bank and Executive Committee guidelines and that fiduciary responsibilities are met. Thus, the balance of support costs goes to the Bank to supervise and monitor implementation and to cover all other tasks involved in MLF project delivery, from development of new programs and policy to reporting and knowledge management to stakeholder dialogue and Government technical and policy guidance. The agency fee covers, in sum, staff weeks of the core unit, country teams, travel, supervision, reporting, hiring consultants, expert consultations (OORG), training workshops (for the FIs) and all indirect costs in accordance with eligible administrative costs.

When a project commences implementation (marked by the signing of the sub-grant agreement), the Bank's core unit takes an upfront fee (approximately 3% from a 7 to 13% agency fee) to support ongoing costs. Specific activities of the core unit linked to the upfront cost it receives are listed in Annex II. The size of the core unit has remained approximately the same since the inception of the MP program (a professional staff of 4-5, support staff of 1-2 and a budget officer), as has the cost to maintain core unit operations and activities.

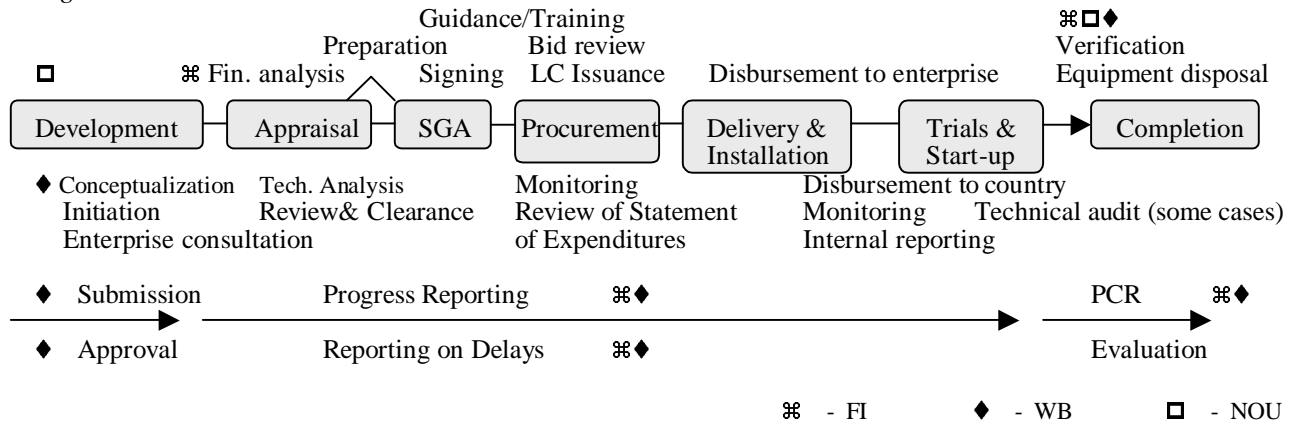
The remaining portion of support costs is reserved for supervision, meaning it is channeled to the Task Manager and the country team. Project supervision includes activities such as conceptualization and initiation of projects, consultations with enterprises, project financial and technical appraisals, site visits, review of statements of expense, procurement review, ongoing monitoring and technical support activities (consultant or Bank staff), commissioning and equipment disposal verification and PCR completion (please see Annex I). These activities are closely linked to the project cycle.

Each stage of the project cycle will thus incur a cost. For traditional investment projects under \$500,000 which involve a 13% agency fee, the first major cost is the appraisal, which is a funding safeguard required by the Bank to ensure that the new beneficiary still is financially viable and that all conditions are in place to facilitate absorption of the new technology and successful conversion. The country team, or a Bank consultant paid with agency fees, works closely with the enterprise during project preparation and after approval to secure all technical information needed to appraise the project. The FI will then conduct a desk review of company records and financial documents and compile the appraisal. The appraisal must be reviewed and cleared by the Bank before a sub-grant agreement can be signed. For this activity 1.5 to 2% of funds are disbursed to the FI, depending on the arrangement between the Government, the Bank and the FI. Once the appraisal has been approved by the Bank and the SGA has been signed, implementation begins and monitoring activities commence for both the FI and the Bank.

As the project progresses, an amount proportional to the agency fee breakdown between the Bank and the FI is taken by the Bank for parallel activities to the FI's activities. The number of site visits and exchanges on the project is proportional to the complexity and/or duration of the project, and

correspondingly, the amount of support costs required at different points in the project cycle. Figure 3 depicts the major milestones in implementation to which costs are associated.

Figure 3.



The tiered nature of the Bank’s administrative system in fact lends itself well to comprehensive financial oversight. Funding is filtered through the OTF to main accounts to country special accounts to the enterprises only when certain conditions are satisfied (please refer to Fig. 2). FIs cannot disburse until enterprises show documented proof of purchases. Their accounts, in turn, are replenished based on their projected disbursements for the year. Moreover, because the majority of the Bank’s FIs are banks, they have their own systems of accountability as well.

The treatment of support costs in comprehensive sector and national CFC phaseout plans is different than under traditional investment projects because disbursement of the MLF funds for the project is linked to the activities completed (i.e. performance based). The funding is basically provided after the disbursement conditions have been met, meaning that there must be funds ahead of time for the IA to perform annual activities, such as monitoring and reporting, which are part of the disbursement conditions. The minimum cost items for each annual production sector plan, in China for example, comprise of the following:

- FI Support Cost/Technical Assistance
- Preparation of the Annual Program
- Supervision Costs (plant site visits)
- Audits (Financial, technical and performance verification)
- PCR

The funding is thus disbursed in tranches which correspond to the first four activities. The last tranche will follow the audit which is presented mid-year (June or July) to the Sub-group on the Production Sector. Once conditions are satisfied, the government is given the go ahead by the Bank to draw down funds from its account. This process can take several weeks to a couple of months. Use of the support costs, including disbursement of the agreed fee to the national implementing agency (FI), is linked to each activity (see Annex I for a list of activities). The Bank will report on an annual basis on the disbursement of the annual tranche.

In sector and national plans, the Bank’s modality of operation remains is the same as in traditional investment projects. A direct cost for the Financial Intermediary is awarded at the level of investment projects (1-3%) because the rate is fixed in the legal agreement. Similarly, the overhead of the core unit is also fixed around 3% from the support cost allocation. This 4-6% is a cost which remains



constant and must be considered in the new climate of varying support cost rates for sector and national plans.

### Cost Analysis

Costs of project implementation for individual projects vary for a number of reasons, including duration, size of the project, size of the portfolio of projects, the technical complexity of the project and the sector it falls under. For these reasons, a useful analysis of cost to the Bank to deliver projects must be done on a larger scale.

The analysis focuses on ongoing projects and new approvals to the Bank from the time it shifted to the fee-based system (1996 to 2001) because prior to that time, work program costs were charged by year and accounts for the particular activities undertaken for projects were closed by the end of a calendar year. Total approvals, disbursement and average support cost expenditure for each of the 21 countries which received funding during this time were compared. Although expenditures on support costs is not directly linked to disbursement on a project-by-project basis, program-wide disbursement was utilized as reference point to provide a comparison to provide some understanding of the amount of support costs received and the level of actual expenses incurred. It was seen that the average cost as a percentage of total funds disbursed to the Bank was 10% which is also consistent with Bank financial statements. The budget for ongoing activities and staff has, since the early years of the MP program, been approximately US \$4.5 to \$5.5 million a year and based on an allocation of approximately US \$50-60 million. Over the years, the coordination unit has not changed much in composition and costs have remained about the same. The 3% FI fee is embedded in most grant agreements with the Bank's client countries and also does not vary.

Country team costs, however, have varied. In 1996, the first year of the new support cost system, the average percentage of supervision expenditure to project cost dipped from earlier years to 6% and reached its lowest rate in 1998. However, it has steadily climbed since 1997, reaching a new high in 2000 and decreasing only slightly in 2001. Projects with delays, the mature stages of some country portfolios, the complexity of projects and increased administrative functions, such as reporting are attributable. These are discussed in detail below. When considered at the country level, average supervision costs vary extensively with one South Asia and several countries in Latin America ranging from 27 to 37% and others, such as in East Asia, coming out with low costs around 4%.

At the time of the Bank's shift to a fee-based system, a number of projects were ongoing, with nearly US \$137 million not disbursed. Administrative fees needed for these ongoing projects were calculated by an aggregate figure based on disbursement. By changing over to this system and utilizing the average cost calculated above to complete a project, the Bank estimates a total of US \$13.8 million in support costs foregone. In line with the assumptions made by the Bank before the 18<sup>th</sup> Executive Committee Meeting when it agreed to adopt the fee-based system, however, it was expected that administrative activities for ongoing projects would be subsidized with support costs from future project approvals. This included the 13% agency fee awarded to the Bank for 19 projects, cleared for approval at the 17<sup>th</sup> Executive Committee Meeting and new project approvals of the 18<sup>th</sup> Meeting (a total of US \$3.79 million), as well as subsequent approvals.

As of the end of 2001, undisbursed funding was over US \$110 million. Required support costs associated with this undisbursed funding would be US \$11.3 million based on the historic rate of 10%. The remaining balance of support costs at the end of 2001 is nearly US \$10.5 million which demonstrates there will be a shortfall. The affect of support costs foregone from early years, in combination with project implementation variables is marked.

Plainly, the ability for the Bank to cover its existing funding commitments would rest with the support costs from the sector plans. However, under the approach currently used by the Executive Committee, the agency fee will change from year to year depending on the approval amount for the annual program making long-term administrative planning unpredictable. In the production sector, funding will decrease proportionally to the increased phaseout accomplished annually. Costs of standard monitoring and reporting requirements such as the audit and preparation of the annual program will, however, not decrease (and could increase slightly) yet they will have to be completed each year. The support costs received today might be needed to subsidize these annual requirements in the future, including the PCR if support costs tomorrow are insufficient. For the MAC sector and 2001 CFC production sector annual plan, it is already evident that support costs were not sufficient to conduct all supervision and reporting activities.

### *Variables Affecting Costs*

The average cost to the Bank to deliver projects over the years must be considered in parallel with the evolution of the type and number of activities associated with the delivery of projects as well as the nature of the projects themselves. Although costs have remained the same on average, parameters surrounding project delivery are much different than in the early years of the Fund. Since the time of the 1998 consultant's report which listed activities eligible for reimbursement with administrative fees, monitoring and evaluation responsibilities of the IAs have been expanded. The PCR has become an important tool for the MLF Senior Monitoring and Evaluation Officer, and with its increased import has come evolving requirements for detailed cost and production information, a rigorous equipment disposal process and multiple stakeholder review and input. Sector evaluations often will, however, require more information and IAs have readily provided this on an ongoing basis.

In addition, in its mission to understand and remedy implementation delays and to untie funds from completed projects for future programming, the Executive Committee has added two new reporting requirements for review at each meeting. These reports, in particular that on project implementation delays, have proven to be quite resource intensive as much stakeholder consultation is required. Finally, the most recent changes have been to the annual progress report which in addition to past data, now requires details on support cost funding, on current and future multiyear agreements, on past business plan information, and on projects which have been or are on the list of project implementation delays. In terms of reporting, the Bank's emphasis on national execution increases the number of actors involved in collecting and reporting data.

Under the direct-cost approach, the Bank was compensated for costs of training workshops and expert meeting separately. All these types of activities are now covered by the support cost allocation. The need for these activities has not diminished as the Executive Committee's body of decisions continues to grow. Financial Intermediaries must be continuously informed of new guidelines and how these impact day-to-day operations. Applying guidelines to ongoing projects is particularly challenging as the set of assumptions agreed upon by all stakeholders is modified during implementation which requires resources and time for all stakeholders to accept, understand and adopt.

The most obvious variable in the cost of project implementation is the nature of the project. The 1998 paper on administrative costs already encapsulated the accepted fact that larger projects will cost less to implement than smaller projects. A large project (in terms of funding) will not always translate in a cheaper project to implement, however. SMEs are the largest number of enterprises left to convert around the world. Umbrella projects may capture a large number of these enterprises, yet all project implementation and monitoring requirements still exist.

Projects which are technically complex, involve new implementation modalities or innovative financing may involve higher administrative costs in certain stages of the project cycle. This is again demonstrated by umbrella projects for SMEs. In its issue paper on support costs, the Secretariat provided a similar conclusion – the definition of a small project should go beyond the project budget to look at the effort required in administering different types of projects<sup>6</sup>. Interesting enough, the two variables of project size and type and of technical complexity, are the determining factors for support cost allocation under the GEF’s flat-fee system.

Duration of projects has proven to be a variable that all IAs underestimated in the early years in terms of the impact on administrative costs. Two major regions of the world were hit by economic difficulties in the late 1990s which have delayed some projects significantly. Supervision duties (and expenses) continue until a project is completed, despite the additional years the project might last.

Conversely, there are a small number of projects in the Bank’s portfolio which, for a combination of reasons, will be completed with little difficulties and delays, and may also incur savings in project costs because of effective implementation. In these cases, the only savings which might occur in support costs and which is seen on a case-by-case basis, is in the supervision component, because the Bank has a contractual agreement with FIs to pay the 3% and because of the coordination unit’s upfront costs. If the Bank were to return support costs for activities already paid for, it would quickly be operating at a loss. The small amount of savings resulting from the 7% supervision component is, however, quickly absorbed by projects which have exceeded the 13% because of delays, isolation, size, etc. Again, the use of support cost in this manner is completely acceptable based on the agreement that the Bank has with the Executive Committee and the understanding it had when agreeing to the 13% fee-based system.

Services which *are not* provided result in a savings in support costs which *are* returned to the MLF. This is seen in cancelled projects or projects with a cancellation in a component of the project. Because of fixed costs in the Bank’s support cost arrangement, it will return funds depending on the stage of implementation (according to the project cycle followed by the Bank) when the project is cancelled.

## **Conclusion**

The World Bank sees three factors influencing its decision to take stock of the support cost system at this time: a shift in the MLF’s portfolio development as a result of strategic planning and the compliance period; the recognition, based on characteristics of the Bank’s current portfolio and likely trends, that support cost funding might not be sufficient to cover all future commitments; and, the increased emphasis by the MLF on de-linking individual projects from the Agencies’ overall portfolio of projects in terms of administrative fees and associated reporting at the same time that emphasis is being placed on delivering comprehensive programs consisting of investment and non-investment activities and technical and policy advice to assist individual countries achieve compliance.

In view of the analysis of historical data on support costs and the current trends, the World Bank’s main concern is that, in line with the agreement between the Bank and the Executive Committee, all costs associated with project implementation are covered. Historical and current data demonstrate that the remaining support cost funds are all required to cover the Bank’s existing project commitments. Further, it is seen that the Bank can operate on a 11% fee based on a US \$50 million allocation provided that it is permitted to utilize its existing pool of support cost funding to meet its commitments and that the

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<sup>6</sup> “An Issue Paper on Support Costs: Follow-up to Decision 34/65,” UNEP/OzL.Pro/ExCom/35/64, 2 November 2001.

level of administrative fees for the production sector projects are commensurate to expenditures for supervision, the FI fee and the Bank's coordination unit.

Any adjustment to the current support cost system should reflect the experience of the Bank and other IAs in maximizing the effectiveness of the agency fee to deliver on their respective project commitments. The administrative cost system itself should not involve transaction costs which diminish the overall advantages of the system, nor create disincentives for developing innovative, and inherently riskier, projects.

With the compliance period upon us and the additional diligence it entails, the Bank believes it is crucial that services provided to ensure development of sound and pertinent projects, and smooth and successful project implementation in both traditional projects and sector and national plans are assured through an equitable, consistent and efficient support cost regime.

**Annex I**  
**Use of the Administrative Fee under Sector Plans\***

<b>Task</b>	<b>NOU</b>	<b>Financial Intermediary</b>	<b>Bank Country Task Team</b>
<b>Support costs</b>	<b>1 ½%</b>	<b>1 ½%</b>	<b>~ 4%</b>
Prepare sector plan	SEPA team prepares sector proposal		Assist SEPA in preparation
Prepare Project Implementation	SEPA prepare project implementation manual		
Selection of Domestic Implementation Agency (DIA or FI)	<ul style="list-style-type: none"> <li>• TOR for DIA</li> <li>• Bid invitation</li> <li>• Selection of DIA</li> </ul>	Sign agreement with SEPA	<ul style="list-style-type: none"> <li>• Bank review and clearance</li> <li>• Bank clearance</li> <li>• Bank no Objection</li> </ul>
Preparation of Annual Plan	Draft proposal		Review of draft proposal Prepare final proposal to be agreed with NOU
Implementation of Annual Program			Monitor implementation of overall Annual Program
Selection of beneficiary enterprises	Prepare invitation for proposal from beneficiaries	Assist NOU in the tasks	Review and no objection to the procedures
	Conduct training for enterprises	Assist NOU	Clear TOR for training TA
		Review of proposals and recommendation of beneficiaries to NOU	Review and no objection
	Review bid/proposals and select beneficiary enterprises	Verify enterprise information and confirm eligibility	Verify eligibility and other information through plant visits as per ExCom agreements
Technical assistance activities	Prepare initial proposals		Review and clear
	Prepare TOR for agreed TA activities		Review and provide a no objection
	Selection of TA contractor		Bank No objection
	CTA contract		Monitored by Bank
Contract with beneficiary enterprises	Sign contract	Co-sign contracts	
Implementation of contracts		Receive report from beneficiaries	Review quarterly reports
	Monitor implementation of contract	Assist NOU	Monitor through plant visits
	Commissioning	Assist NOU	
	Completion report	Assist NOU	Verify information and no objection
Review of Annual Program Implementation Status	Review quarterly reports		Review quarterly reports and perform random plant visits during three missions per year
Bank Financial Audit			World Bank audits all accounts in China
Chinese Performance Audit	SEPA contract Audit Bureau to do a performance verification of all activities		World Bank reviews the audit and accepts the Chinese performance audit report as a condition for the last disbursement
Bank Independent Performance verification			World Bank hires independent verification team to verify through plant visits that annual targets have been met.

\*Please refer to Annex II for the list of activities of the Coordination Unit.

## Annex II

### World Bank Montreal Protocol Operations: Roles and Responsibilities

#### **Financial Intermediary**

Provides detailed information on enterprises and subproject eligibility

Prepares appraisal containing:

- Proposal & Revised Budget table,
- Financial Analysis & Appraisal,
- Basic Financing Plan,
- Procurement procedures,
- Disbursement Schedule,
- Audit & Reporting Requirements,
- Equipment Disposal Plan

Prepares and signs SGA with beneficiary

Verifies expenditures and disburses funding from trust fund account

Monitors and supervises projects for compliance with Bank procurement procedures, ExCom rules and policies, and provisions of the SGA

Keeps all project records

Assists enterprise in/or prepares draft PCR

Reports on project progress biannually

Provides data for ExCom reporting requirements (reports on progress, completed projects with balances and implementation delays) at least three times a year and for all follow-up requests of the MLF

Secretariat

Responds to ad hoc information requests by the Bank and NOU, such as information for MLF Senior M&E Officer evaluations, Bank project audits and quality assurance reviews, etc.)

#### **World Bank Country Task Manager**

Leads umbrella grant agreement preparation, amendments, extensions

Works with Government to initiate projects

Administration of funds (preparation and finalization of legal documents, disbursement, record keeping and audits)

Prepares project proposals or engages the use of consultants

Reviews and clears project appraisal reports

Provides “no objection” to sub-grant agreements

Supervises projects and FI and consultant activities through:

- A minimum of two country missions a year (if not already situated in the country)
- Review of statements of expense
- Review of procurement
- Ongoing monitoring and technical support activities, including through site visits
- Commissioning and equipment disposal verification, PCR completion.
- Drafting Back to Office Reports and Aide Memoires

Completes internal Project Status Reports

Provides NOU policy guidance

Provides FI Bank operational policy guidance

Completes Implementation Completion Report on umbrella grant agreement

Liaises between Bank coordination unit and FI

Provides data to coordination unit for policy papers, responses to the Secretariat, etc.

## **World Bank Coordination Unit**

Liaises with MLF Secretariat and Task Managers

Submits projects

Attends Executive Committee meetings

Prepares policy papers and responses to the ExCom and/or Secretariat

Provides technical and policy advice to TMs and FIs

Conducts FI training through annual workshops

Attends international meetings and workshops (UNEP network meetings, OEWG, etc.)

Coordinates and executes M&E requirements:

- Reports on progress, implementation delays, completed projects with balances

- Reviews, finalizes and submits PCRs

- Provides additional data requested for MLF evaluations and Secretariat policy papers

Business Planning and annual work programs

Budgeting and fiduciary management

Administration of funds (Review of expenses, fund allocation, cash flow management for donors)

Recruit experts and consultants

Direct and lead MP knowledge management (database development and maintenance, website, information pieces – internal/external, publications, information dissemination to FIs, NOUs and general public, library maintenance)

## **Other Bank Roles**

Procurement Officer

- Provides procurement advice to TMs

- Reviews procurement documents

Disbursement Officer

Legal – Country and Environment Lawyers

- Provides legal advice to TMs and Coordination Unit on:

  - Grant agreements

  - ExCom decisions

  - International conventions

  - Bank operational and business policies

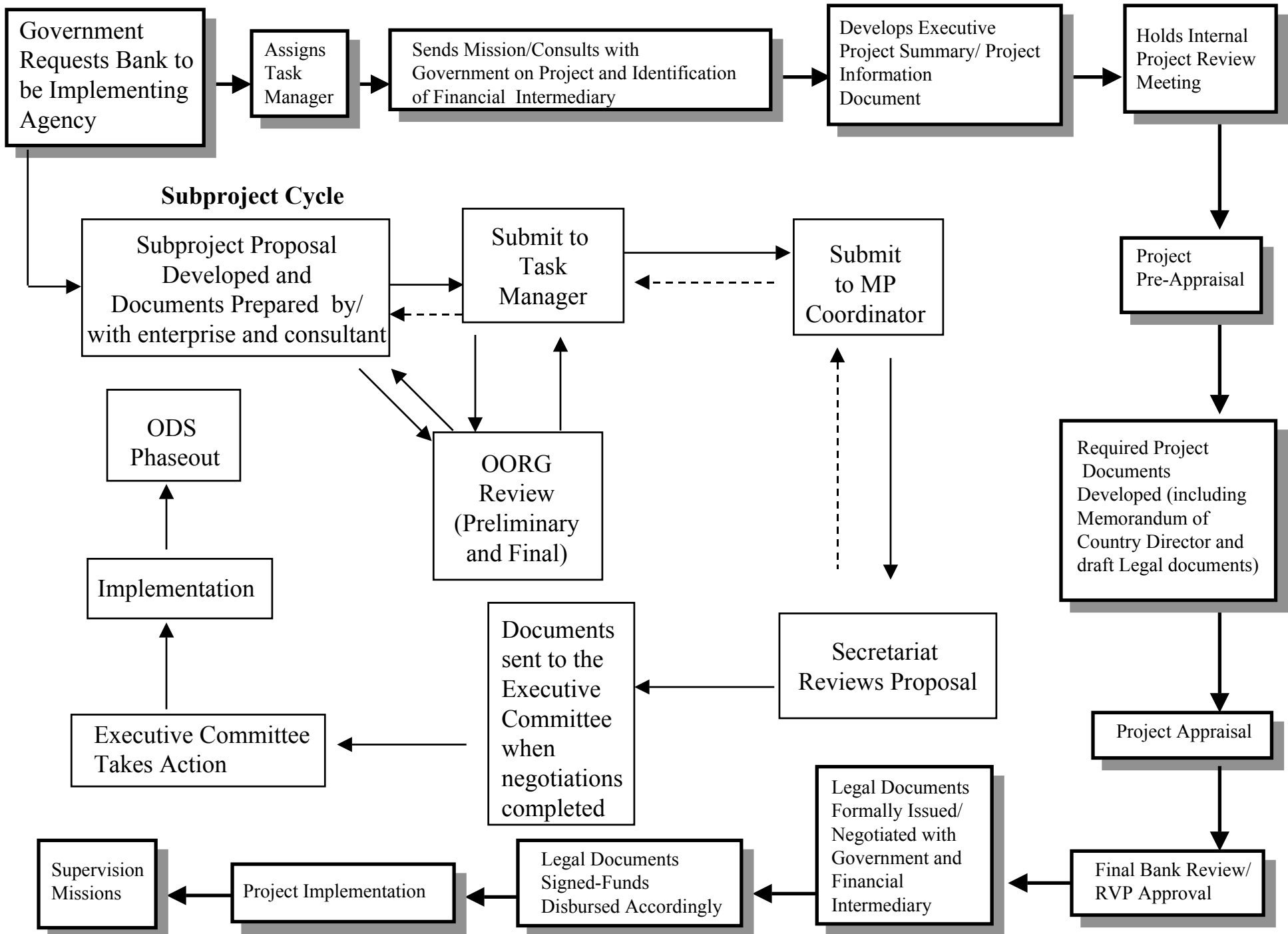
- Proposes legal instruments for projects with new mechanisms (such as concessional lending, performance-based implementation, new multilateral partners or funds, etc.)

## **Annex III**

### **The Project Cycle under MP Operations at the World Bank**



# Montreal Protocol Project and Subproject Cycle



## Annex IV

### Agreement between the Executive Committee of the Interim Multilateral Fund for the Implementation of the Montreal Protocol and the International Bank for Reconstruction and Development

The Executive Committee and the World Bank signed an agreement on 9 July 1991. Under this agreement:

The World Bank will co-operate with the Executive Committee and assist it in accordance with these arrangements in administering and managing the programme under the authority of the Parties to finance the agreed incremental costs of Parties operating under paragraph 1 of Article 5 of the Protocol. In performing its functions under these arrangements, the World Bank will act through the Ozone Projects Trust Fund (OTF) and will apply only those considerations relevant to effective and economically efficient programmes and projects which are consistent with criteria adopted by the Parties and guidelines adopted by the Executive Committee (UNEP/OzL Proc/Ex-Com/3/Inf.2, Section A, *Scope of Co-operation*).

The World Bank will prepare a work programme in co-operation with recipient countries, UNEP and UNDP, for its activities under these arrangements, including a budget, for approval by the Executive Committee on an annual basis. The work programme as approved by the Executive Committee will be consistent with the relevant decisions of the Parties and guidelines adopted by the Executive Committee regarding project eligibility and the implementation of activities supported by the Fund.

The World Bank will co-operate with the Parties, UNEP, UNDP, and the Executive Committee through the Secretariat of the Fund, to provide information on funding available for relevant projects, to secure the necessary contacts, and to co-ordinate, when requested by the interested Party, projects financed from other sources with activities financed under the Protocol.

The World Bank will co-operate with the Parties operating under paragraph 1 of Article 5 of the Protocol and assist them, as requested by them and in accordance with the approved work programme referred to in paragraph 2, in developing each Party's country programme (CP) as envisaged in the Terms of Reference of the Fund, as well as projects to facilitate compliance with the Protocol.

The World Bank will review each CP in respect of which it will perform its functions under these arrangements, and submit its views to the Executive Committee. Upon approval of the CP by the Executive Committee, the World Bank will assist the party to implement the projects contained in it. The World Bank will do so by following its rules and procedures and in accordance with the approved work programmes in co-operation with UNEP and UNDP. The World Bank may approve a request for financing by the Party of a project or projects pursuant to the approved CP if the agreed incremental costs are less than US \$500,000. Additional financing from the Fund for unforeseen increases in expenditure for any project will be subject to approval by the World Bank, except that if the additional financing would cause the total expenditure for the project to exceed US \$500,000, the financing will be subject to approval by the Executive Committee as adjustment to the current, or part of the next, work programme. For projects where the agreed incremental cost exceeds US \$500,000 financing by the World Bank is subject to the approval of the Executive Committee as part of a CP.

Any disagreement by a Party operating under paragraph 1 of Article 5 with any decisions taken with regard to a request for financing by that Party of a project or projects where the agreed incremental costs are less than US \$500,000 may, at the request of the Party, be referred to the Executive Committee for review.

Pending the preparation of country programmes, the procedures in above two paragraphs will apply also as appropriate to projects consistent with the ozone layer protection policies of Parties operating under paragraph 1 of Article 5 of the Protocol, which the Executive Committee finds in compliance with the control measures of the Protocol.

(UNEP/OzL Proc/Ex-Com/3/Inf.2, Section B, *Operational Procedures*)

The Bank will hold and administer funds provided to the Bank pursuant to this agreement in trust, together with any other assets and receipts of the OTF, for the benefit of the Parties in accordance with the decision by the World Bank to provide for the establishment of the OTF and these arrangements.

The Executive Committee will arrange for the transfer of funds contributed by the Parties and allocated by the Executive Committee to the OTF for expenses incurred or to be incurred by the World Bank for the activities it undertakes pursuant to these arrangements and for the implementation of approved country programmes and projects, as soon as the funds become available. The transfer will be made in cash in United States dollars or at the request of the Executive Committee by the deposit of notes or similar obligations denominated in United States dollars and issued by the government of a Party or the depository designed by such Party, which shall be

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non-negotiable, non-interest bearing and payable in United States dollars at their par value on demand to the OTF or in accordance with a schedule of encashment agreed by the World Bank, provided that in exceptional cases and as administratively feasible on the basis of appropriate arrangements, as determined by the World Bank, contributions may be made also in other currencies.

Funds held in the OTF will be invested pending disbursement in accordance with the regular practice of the Bank, and the income of investment will be added to the resources of the OTF.

The World Bank will be reimbursed annually in full for the expenses incurred by it for the activities it undertakes pursuant to these arrangements. The reimbursement will be made on the basis of estimated costs, subject to adjustment as of the end of the Bank's financial year, and will be charged against the resources of the OTF.

The World Bank will present to the Executive Committee detailed annual financial statements expressed in United States dollars, externally audited, as part of its annual report.

The World Bank will make no commitments for financing under these arrangements in advance of the receipt of financing in the OTF to finance the commitments.

The Executive Committee will notify the World Bank through the Secretariat if a shortfall in resources for the approved work programme is anticipated or if the work programme needs to be adjusted for this reason.

The World Bank may agree to co-financing arrangements with Parties and others for the purpose of these arrangements.

The World Bank will provide financing from the OTF in the form of grants denominated in United States dollars.

The World Bank will continue to hold all unutilised resources in the OTF until all commitments and liabilities under these arrangements have been satisfied, project activities have been brought to an orderly conclusion and reimbursement under paragraph 11 has been made, after which any remaining resources will be transferred as the Executive Committee may determine. If the unutilised resources prove insufficient to meet such commitments, liabilities and reimbursement, the World Bank will consult with the Executive Committee on the manner in which such commitments, liabilities and reimbursement may be satisfied.

*(UNEP Del. Proc/ExCom/5/Inf.2, Section C: Financial Provisions)*

The President of the World Bank, or his representative, will participate in meetings of the Executive Committee in order to report and consult on the World Bank's activities under these arrangements.

*(UNEP Del. Proc/ExCom/5/Inf.2, Section D: Participation in Meetings)*

The World Bank will provide to the Executive Committee through the Secretariat semi-annual progress reports and an annual report on implementation by the World Bank of previously approved work programmes and activities related to country programmes and projects, including co-ordination with UNEP and UNDP under these arrangements. The financial statements will be attached to the annual report.

The reports will include proposals if necessary to revise the current year's budget; provide for the work programme, including a budget, for the following year, and describe any disagreement by a Party operating under paragraph 1 of Article 5 of the Protocol with any decision taken by the World Bank with regard to a request for financing by that Party of a project or projects where the agreed incremental costs are less than US \$500,000. After the OTF shall have been fully used, the World Bank will present a final report on the operations financed under these arrangements.

*(UNEP Del. Proc/ExCom/5/Inf.2, Section E: Reporting by the World Bank)*

These arrangements may be amended by agreement of the Executive Committee and the World Bank in writing at any time.

*(UNEP Del. Proc/ExCom/5/Inf.2, Section F: Amendments)*

These arrangements will terminate thirty days after either the Executive Committee or the World Bank may have given notice in writing to the other party of its decision to terminate them, in which event the World Bank will take all necessary action for the expeditious and orderly winding up of its activities under these arrangements pursuant to paragraph 17.

*(UNEP Del. Proc/ExCom/5/Inf.2, Section G: Termination)*

This Agreement entered into force on 9 July 1991 (date of its signature).

*(UNEP Del. Proc/ExCom/5/Inf.2, Section H: Effective Date of Agreement)*

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