



Global Environment Facility

GEF/C.18/9

November 12, 2001

GEF Council
December 5-7, 2001
Agenda Item 11

**A PROPOSAL FOR AN INDEPENDENT REVIEW
OF THE FEE-BASED SYSTEM**

Recommended Council Decision

The Council having reviewed document GEF/C.18/9, *A Proposal for an Independent Review of the Fee-Based System*, approves the preparation of the proposed review, subject to the comments made during the Council meeting, and in accordance with the following:

- (a) the Terms of Reference proposed in document GEF/C.18/9;
- (b) the appointment of the consulting firm of Deloitte & Touche to carry out the review noting that the firm was selected through a competitive bid process administered by the World Bank's General Services Department; and
- (c) the associated budget to cover the fees payable to the consulting firm and the travel costs of involved GEF staff.

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1. This proposal seeks Council approval of the execution of an independent review of GEF's Fee-Based System, comprising:

- (a) the proposed Terms of Reference (Annex A);
- (b) the appointment of the consulting firm of Deloitte & Touche, which was selected through a competitive bid process administered by the World Bank's General Services Department; and
- (c) the associated budget to cover the fees payable to the consulting firm and the travel costs of involved GEF staff.

BACKGROUND

2. When the Fee-Based System was designed, it was agreed between the Implementing Agencies and GEF Secretariat, and later confirmed by the Council, that the fee structure would be reviewed after three years of experience. This was deemed as allowing sufficient time to gain experience with the operation of a Fee-Based System, and based on lessons learned, to determine if (a) a Fee-Based System should continue to be used; and (ii) the current fee structure should be revised. The current fiscal year is the third year of operation of the Fee-Based System. Any recommendations emanating from the review and approved by the Council could become applicable from July 1, 2002.

3. In approving the implementation of the Fee-Based System at its May 1999 meeting, Council requested GEF Secretariat to prepare "...*financial management reviews of the Implementing Agencies' costs...*" and to "...*organize an independent review of selected projects...*" Other critical work program priorities and a lack of resources have delayed these activities, which have not been carried out to date.

4. As the end of the three-year period is approaching, in order to commence the execution of such an independent review, GEF Secretariat has prepared a Terms of Reference (Annex A); and in consultation with the World Bank's General Services Department (GSD) initiated a competitive bid process, subject to the Bank's procurement policies and guidelines, for the selection of a consulting firm to carry out the review. A Selection Committee, comprising the GEF Corporate Finance Manager and representatives from each of the three Implementing Agencies, was established to technically evaluate the proposals presented by consulting firms interested in carrying out the independent review.

OBJECTIVE

5. The Review's objectives, which are intended to provide a sound and viable framework for the future application of a Fee-Based System, are:

- (a) an assessment of the impact of the Fee-Based System upon efficiency and effectiveness of project implementation and project cost management;

- (b) an evaluation of the current flat-fee structure and the respective Implementing Agency's primary driver components (i.e., project cycle staffweek coefficients, fully-loaded staffweek cost) used in the computation of their project implementation costs; and
- (c) a proposal for a revised fee structure/formula or enhancements to the current fee structure, as appropriate, to be applied to all GEF projects, approved from July 1, 2002, for which the Implementing Agencies and the Executing Agencies under the Expanded Opportunities initiative, provide project implementation services.

SCOPE

6. Organizationally, the Review will include the GEF Secretariat, the three Implementing Agencies (IAs) – IBRD, UNDP, UNEP - and the seven Executing Agencies under the Expanded Opportunities Initiative (EAs) – ADB, AfDB, EBRD, FAO, IADB, IFAD and UNIDO. The Review will encompass the following primary aspects of the Fee-Based System, addressing the component issues involved:

(i) The Modality of a Fee-Based System

- The appropriateness and applicability of a Fee-Based System as a modality for compensating project implementation services.
- The design and operation of the Fee-Based System.
- The impact and implications of the Fee-Based System upon GEF's operational and financial framework, e.g., corporate budget, project preparation grants, project grant allocations, executing agency fees, etc.
- The IAs' and EAs' policies and practices governing internal distribution, accounting and reporting of the fees received; including detailed reviews of at least 3 projects from each agency.

(ii) The Current Flat-Fee Structure

- The appropriateness and application of the current flat-fee structure.
- The construction and computation of the current flat-fee structure, e.g., fully-loaded staffweek cost, project cycle staffweek coefficients.

(iii) A Proposal for a Revised Fee Structure

- The implications of GEF's project portfolio and workprogram profile
- Identification of defined project implementation services by IAs and EAs.
- Definition of common standard project implementation services.

- Computation of each respective IAs' and EAs' component cost drivers to be used in a revised fee structure.

EXECUTION

7. On October 5th, 2001, the World Bank's General Services Department (GSD) invited seven well established and internationally recognized consulting firms¹ to respond to a Request For Proposal (RFP) for an "Independent Review of GEF Fee-Based System" (the Review). Representatives from five firms² expressed initial interest by participating in a Pre-Proposal meeting chaired by GSD on October 17th, 2001. On October 29th, 2001, proposals were received from the firms of Arthur Andersen, Deloitte & Touche and KPMG Consulting. During the week of October 29th, 2001, with the guidance of GSD, the Selection Committee members³ technically evaluated the proposals received, based on a pre-determined set of evaluation criteria covering the firm's methodology, related experience and qualifications of assigned personnel. Based on the outcome of this evaluation, on November 7th, 2001, the firms were invited to make presentations of their proposals and respond to questions from the Selection Committee, on which they were further evaluated. On completion of the final scoring of the technical evaluation of these firms, GSD then independently evaluated the contract price proposals, which had been presented by the firms under separate cover. Consequently, based on the combined results of the technical and price evaluations, GSD informed the Selection Committee that the firm of Deloitte & Touche was selected as the proposed consulting firm to carry out the Review. The contract will be awarded to the selected firm only when Council has approved the independent review of the Fee-Based System.

8. Once the contract is awarded, it is expected that the Review will commence in mid-January 2002. The Review will, organizationally, involve the management and staff at the offices of GEF Secretariat, the three IAs and the seven newly designated EAs under the Expanded Opportunity initiative. During the Review, Deloitte & Touche will be accountable to the GEF Secretariat, through the Corporate Finance Manager, who will assume Task Manager responsibility. Deloitte & Touche's Lead Manager for the Review will have primary responsibility for managing the execution of the review and for preparing the final report.

9. GEF Secretariat and the IAs will provide to Deloitte & Touche, at the commencement of and during the review, all information, data and documents deemed essential and necessary to enable the firm to properly understand the organization and operations of the GEF. Relevant staff of the GEF Secretariat, IAs and EAs will also make themselves available at the commencement and throughout the review to address any queries and provide explanations. Deloitte & Touche will familiarize itself with all relevant policies, guidelines and processes pertaining to GEF project cycle; GEF financial management

¹ Arthur Andersen LLP, Boston Consulting Group, Ernst & Young, KPMG Consulting, McKinsey & Company, PriceWaterhouse Coopers LLP, and Deloitte & Touche LLP

² Arthur Andersen LLP, Boston Consulting Group, KPMG Consulting, PriceWaterhouse Coopers LLP, and Deloitte & Touche LLP

³ Comprising the GEF Corporate Finance Manager and a representative from each of the three IAs.

framework; project direct, implementation and execution responsibilities; and all related documents and material.

TIMETABLE

10. The Review's time-table is as follows:

Activity	Date
Issue of Request for Proposal	October 15, 2001
Proposal due date	October 29, 2001
Selection of successful firm	November 9, 2001
Council review and approval of TOR and budget	December 6-7, 2001
Contract award	mid-December, 2001
Expected commencement of Review	mid-January 2002
Discussions with GEF Secretariat, IAs, EAs	January 2002 – March 2002
Mid-review progress discussion	February 15 th 2002
Draft report due	March 26 th 2002
Final report due	April 9 th 2002
Council review of findings and recommendations	May 15-17, 2002

BUDGET

11. The total budgetary resources required for the Review will cover the fees of the consulting firm and the travel costs of involved GEF staff.

I. BACKGROUND

The Global Environment Facility

1. The Global Environment Facility (GEF) is a multilateral financial mechanism, created in 1991, to promote international cooperation and foster action to protect the global environment by addressing biodiversity, climate change, international waters, land degradation and ozone depletion, within the framework of sustainable development. GEF provides grants and concessional funds to complement traditional development assistance by covering the additional costs (also known as “agreed incremental costs”) incurred when a national, regional, or global development project incorporates global environmental objectives.

2. GEF is the designated financial mechanism for two international treaties: the Convention on Biological Diversity (CBD) and the United Nations Framework Convention on Climate Change (UNFCCC). GEF is also expected to be the financial mechanism for the Stockholm Convention on Persistent Organic Pollutants (POPs). In its capacity as financial mechanism, GEF receives guidance from the Conference of the Parties to these Conventions and is accountable to them. GEF also supports the objectives of the UN Convention to Combat Desertification (UNCCD) to address land degradation. Although the GEF is not a financial mechanism for the Montreal Protocol, GEF operational policies concerning ozone layer depletion are consistent with those of the Montreal Protocol and its amendments. For international waters, GEF operational policies take into account numerous relevant international treaties and conventions.

3. The GEF was first initiated as a Pilot Phase in 1991. The Restructured Global Environment Facility became operational in 1994, with a pledged core fund of US\$2 billion. At the Second Replenishment in 1998, US\$2.75 billion was pledged for the next replenishment period. To date, with a membership of 168 governments, the GEF's mandate continues to evolve, with increasing additional attention to desertification, deforestation and persistent organic pollutants. Since its creation, and as of June 30, 2000, GEF has committed \$3.42 billion in grants to over 900 projects in 156 developing countries and transitional economies.

4. The GEF is governed by a Council, which consists of 32 Members representing constituencies from developing and developed countries, and countries in transition. Organizationally, GEF comprises six functional units. The GEF Secretariat (GEF Secretariat) provides central corporate management of institutional relations, program development and coordination, outreach and communications, financial management and monitoring and evaluation. The GEF Trust Fund Trustee responsibilities are assumed by The World Bank. The Scientific and Technical Advisory Panel (STAP), is an advisory body providing scientific and technical advice. Three Implementing Agencies (Implementing Agencies) - the

United Nations Development Programme (UNDP), the United Nations Environment Programme (UNEP) and the World Bank (IBRD) – implement projects funded by GEF project grants. Recently, in FY00, the Council approved an initiative that allowed other multi-lateral banks and development agencies, which met certain established organizational and operational criteria to provide implementation services on GEF-funded projects. Such agencies (EAs) under the “Expanded Opportunity Initiative” include the Asian Development Bank (ADB), the African Development Bank (AfDB), the European Bank for Reconstruction and Development (EBRD), the Inter-American Development Bank (IADB), the International Fund for Agricultural Development (IFAD), the U.N. Food and Agriculture Organization (FAO), and the U.N. Industrial Development Organization (UNIDO).

The Implementation of a Fee-Based System

5. GEF-funded projects are implemented by any of the three Implementing Agencies and the seven EAs, individually or jointly. On a per-project basis, each agency is compensated for its performance of project cycle implementation services, as summarized in Attachment 1. Previously, the Implementing Agencies’ costs of implementing GEF projects were provided for and approved annually both as project-direct and project-indirect costs in GEF’s annual Corporate Budget. In May 1999, the Council approved the introduction of a Fee-Based System for the compensation of Implementing Agencies for their implementation of GEF projects (see http://www.gefweb.org/COUNCIL/GEF_C13/doc/C13_11.doc Council document GEF/C.13/11: *Proposal for a Fee-Based System for Funding GEF Project Implementation*). Under the Fee-Based System, on Council/CEO approval of a project, an IA would be assigned a project implementation fee that is intended to cover the implementation costs of that project over the life-time of the project (most projects are implemented over several years). This fee is based on a flat-fee structure that recognizes four standard GEF project types (i.e., full-size investment, full-size technical assistance, and medium-sized projects, and enabling activities). The approved Fee-Based System became effective July 1, 1999 and was applied to all GEF projects from FY00.

6. When approving the Fee-Based System, Council requested GEF Secretariat to carry out a benchmarking review of GEF’s fee structure against the project implementation costs of comparable development agencies, including regional development banks, aid and development agencies, multilateral funds, and non-governmental organizations. The primary objectives were to determine: (a) the reasonableness and appropriateness of GEF’s flat-fee structure; and, (b) the efficiency and effectiveness of GEF’s financial management of its project implementation costs. This was completed in August and September 1999; and the findings were provided to Council in May 2000 (see http://www.gefweb.org/COUNCIL/GEF_C15/GEF_C15_Inf.7.doc Council document GEF/C/15/Inf.7: *Report on a Benchmarking Review of Implementing Agency Fees*). The review confirmed that GEF’s project cost management practices were adequately and effectively methodical, rigorous and demanding; and, that GEF’s flat-fee structure is neither unreasonable nor inappropriate.

7. In May 2000, GEF Secretariat also reported to Council on the first-year experience with the implementation of the Fee-Based System. The report discussed the primary issues encountered and presents proposals with the objective of enhancing and reinforcing the Fee-Based System as the primary mechanism for reimbursing an Implementing Agency's project implementation costs (see http://www.gefweb.org/COUNCIL/GEF_C15/GEF_C15_6.doc Council document GEF/C/15/6: *Report on the Implementation of the Fee-Based System*). It was decided to continue operation of the Fee-Based System in its existing form to gain more experience; and to revise it, if appropriate, after three years of experience, as agreed on initial implementation of a fee structure.

8. The Fee-Based System was originally applied to the three Implementing Agencies (i.e., IBRD, UNDP, UNEP). With the recent introduction of the EAs, it is anticipated that these will also be compensated under the same Fee-Based System as the Implementing Agencies, for performing project implementation services on GEF projects

II. PROPOSED INDEPENDENT REVIEW OF THE FEE-BASED SYSTEM

9. When the Fee-Based System was designed, it was agreed between the Implementing Agencies and GEF Secretariat, and later confirmed by Council approval, that the fee structure would be reviewed after three years of experience. This was deemed as allowing sufficient experience with the operation of a Fee-Based System; and, based on lessons learned, to determine if (a) a Fee-Based System will continue to be used; and (ii) the current fee structure will need to be revised. The current fiscal year is the third year of operation of the Fee-Based System. Based on this review, if appropriate, a revised fee structure would become applicable from July 1, 2002.

10. In approving the implementation of the Fee-Based System at its May 2000 meeting, Council requested GEF Secretariat to prepare "...financial management reviews of the Implementing Agencies' costs..." and to "...organize an independent review of selected projects..." Other critical workprogram priorities and a lack of resources have delayed these, which have not yet been carried out to date.

11. These Terms of Reference establish the objective, scope and execution of an independent review of GEF's Fee-Based System (the Fee Review).

Objective of Fee Review

12. The Fee Review should achieve the following objectives that would provide a sound and viable framework for the future application of a Fee-Based System, taking into account the experience so far and the recent introduction of the EAs:

- a) an assessment of the impact of the Fee-Based System upon efficiency and effectiveness of project implementation and project cost management;

- b) a validation of the current flat-fee structure and the respective IA's primary driver components (i.e., project cycle staffweek coefficients, fully-loaded staffweek cost) used in the computation of their project implementation costs; and
- c) a proposal for a revised fee structure/formula or enhancements to the current fee structure, if necessary, to be applied to all GEF projects, approved from July 1, 2002, for which the Implementing Agencies and EAs provide project implementation services.

Scope of the Fee Review

13. The Fee Review will address the following primary aspects of the Fee-Based System, addressing the component issues involved:

- i. The Modality of a Fee-Based System
 - (a) The appropriateness and applicability of a Fee-Based System as a modality for compensating project implementation services.
 - (b) The design and operation of the Fee-Based System.
 - (c) The impact and implications of the Fee-Based System upon GEF's operational and financial framework, e.g., corporate budget, project preparation grants, project grant allocations, executing agency fees, etc.
 - (d) The Implementing Agencies' and EAs' policies and practices governing internal distribution, accounting and reporting of the fees received; including detailed reviews of at least 3 projects from each agency.
- ii. The Current Flat-Fee Structure
 - (a) The appropriateness and application of the current flat-fee structure.
 - (b) The construction and computation of the current flat-fee structure, e.g., fully-loaded staffweek cost, project cycle staffweek coefficients.
- iii. Proposal for a Revised Fee Structure
 - (a) The implications of GEF's project portfolio and workprogram profile
 - (b) Identification of defined project implementation services by Implementing Agencies and EAs.

- (c) Definition of common standard project implementation services.
- (d) Computation of each respective Implementing Agencies' and EAs' component cost drivers to be used in a revised fee structure

Conclusions, Findings and Recommendations of Fee Review

14. The Fee Review will prepare a comprehensive and detailed report addressing the objectives and scope outlined above, and discussing the issues and outcome of the review. The report should also present general conclusions, specific findings and recommendations to the GEF.

Proposed Timetable

15. The Fee Review's schedule is referenced to the award of the Fee Review contract after the December 2001 Council meeting and to the May 2002 Council discussion of its findings and recommendations; as follows:

Activity	Date
Commencement of Review, initial briefings	mid-January 2002
Meetings and discussions with GEF Secretariat, Implementing Agencies, EAs	January 2002 – March 2002
Mid-Review Progress Discussion	February 15 th 2002
Draft report	March 26 th 2002
Final Report	April 9 th 2002

Importantly, it should be noted that the review has to maintain the above schedule, which has an inflexible deadline. Specifically, the final outcome of the Fee Review has to be ready and complete for presentation to Council for discussion and approval at its May 15th – 17th, 2002 meeting so that any proposed revised fee structure, if accepted, can be applied to GEF projects approved in FY03 (i.e. from July 1, 2002)

Execution of Fee Review

16. An independent consulting firm (the Firm) will be selected to carry out the Fee Review. The Firm will be appointed by a committee comprising of the GEF Assistant CEO, the GEF Corporate Finance Manager and representatives from the Implementing Agencies; in accordance with the Terms of Reference approved by the GEF Council and in consultation with the GEF CEO/Chairman. During the Fee Review, the Firm will be accountable to the GEF Secretariat, through the Corporate Finance Manager. The Fee Review will, organizationally, encompass GEF Secretariat, the GEF Implementing Agencies and the newly designated Expanded Opportunity Agencies.

17. GEF Secretariat will provide to the Firm, at the commencement of the review, all additional information, data and documents deemed essential and necessary to enable the Firm to properly understand the organization and operations of the GEF. The Firm will familiarize itself with all relevant policies, guidelines and processes pertaining to GEF project cycle; GEF financial management framework; project direct, implementation and execution responsibilities; and all related documents and material. Relevant staff of the GEF Secretariat and Implementing Agencies will also make themselves available at the commencement and throughout the review to address any queries and provide any explanations. The Firm will be expected to visit and to meet with involved management and staff of GEF Secretariat, the three Implementing Agencies and the seven EAs; specifically, IBRD/IFC (Washington DC), UNDP (New York), UNEP (Nairobi), EBRD (London), IADB (Washington DC), ADB (Manila), AfDB (Abidjan), FAO (Rome), IFAD (Rome), and UNIDO (Vienna).

18. The Firm's Project Manager of the Fee Review will have primary responsibility for managing the Fee Review and for preparing and drafting the final report. She/he should have strong experience in leading a team as she/he is responsible for operationalizing and implementing the review. She/he must have excellent knowledge and understanding of financial, budgetary and cost management principles and practices; project management and finance; and organizational structures and accountabilities.

19. The Firm's Fee Review Members will also have a sound knowledge and understanding of financial, budgetary and cost management principles and practices; and experience with project management and project finance. The following minimum qualifications and expertise are required from each team member:

- Masters degree or higher in financial, budgetary or business management;
- a minimum of 10 years of experience in finance, management, auditing and cost management;
- excellent analytical skills;
- experience with multilateral or national development programs;
- capacity to work effectively work in a team;
- excellent writing and communication skills in English; and
- ability and readiness to work in multicultural environments and to travel internationally.

20. The Firm's Project Manager will have primary responsibility for and will be expected to carry out the core substantive discussions, deliberations and analyses. For performing any required data analyses at the offices of the Implementing Agencies and EAs referred to in Paragraph 17, the Firm is encouraged to optimally utilize appropriately qualified and experienced staff from their organization's relevant local and regional offices.

PROJECT IMPLEMENTATION SERVICES

An Implementation Fee is assigned to an agency for the provision of implementation management services in respect of a GEF-funded project. These services cover the management and administration of all project-cycle tasks and activities during all phases of a Project from concept to closure (i.e., development, preparation, appraisal, supervision and evaluation). The GEF project cycle is discussed in greater details in the document GEF/C.16/Inf.7 “GEF Project Cycle”; the project-cycle tasks/activities are summarized generally below.

Development

- development of project concept (*with or without PDF funds*)
- presentation for Pipeline Entry
- Preparation
- preparation of detailed feasibility study and project design, which are presented in a project proposal, the Project Brief (*typically with PDF funds*)
- presentation of Project Brief for CEO approval (Medium-Sized Projects, Expedited Enabling Activities) or Workprogram inclusion for Council approval (Full-Sized Projects)

Appraisal

- finalization of the project’s design, implementation plan/time-table, detailed budget/cost estimates, in-country negotiations, etc.
- preparation of project appraisal and relevant legal documents
- presentation of project appraisal and final project proposal for CEO endorsement; and negotiation/agreement of Implementation Service Fee (*release of grant and implementation fees*)

Supervision

- supervision of the project implementation (including procurement/disbursements)
- project cost-management and reporting
- project progress review and reporting
- preparation of appropriate interim evaluations and reviews, in accordance with agency’s operational policy/practice
- preparation of annual Project Implementation Review (PIR)

Completion and Evaluation

preparation of project completion report and/or project completion/termination evaluation, in accordance with agency’s operational policy/practice.