AN INTERIM REPORT ON A REVISION OF THE FEE STRUCTURE
Recommended Council Decision

The Council, having reviewed document GEF/C.20/5, *An Interim Report on a Revision of the Fee Structure*, requests the GEF Secretariat, in consultation with the Implementing and Executing Agencies, to prepare a proposals for a revised fee structure for Council review and approval at its meeting in May 2003. In preparing the proposal, the Secretariat and the Implementing and Executing Agencies are requested to take into account the comments made by the Council at its meetings in May and October 2002, as well as any written comments submitted to the Secretariat by November 15, 2002. The revised fee proposal approved by the Council in May 2003 will apply to all GEF projects approved by the Council and the CEO beginning in FY04. Fees for projects approved by the Council and CEO in FY03 will be proposed in accordance with the current fee system, but subject to an overall ceiling of a fee to grant ratio no greater than that of the May 2002 work program.
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I. INTRODUCTION

1. This paper presents the interim results of (i) an analysis of GEF’s experience with its Fee-Based System during the period FY00-FY02; (ii) a review of the four fee options proposed by the independent review of the Fee-Based System; and (iii) consultations to-date between GEF Secretariat and the Implementing Agencies and executing agencies acting under expanded opportunities\(^1\) (Executing Agencies); as the basis for Council review and deliberation.

2. Council comment and guidance are sought on the resolution of the issues experienced and the finalization of the design of a revised fee structure for the GEF Fee-Based System, for the compensation of project implementation services that are to be provided by the three Implementing Agencies and seven Executing Agencies on GEF-funded projects, which are approved from July 1, 2003.

Background

3. The Fee-Based System was introduced in FY00 as a methodology for compensating the Implementing Agencies for the provision of project implementation management services on GEF-funded projects. To reinforce the implementation of the proposed fee structure, GEF Secretariat carried out a Benchmarking Review\(^2\) in 1999. During its third year of operation, in January - March 2002, an independent review of the Fee-Based System was carried out by the consulting firm of Deloitte & Touche. On discussing the outcome of this review\(^3\) at its meeting in May 2002, Council requested GEF Secretariat, in consultations with the Implementing Agencies and Executing Agencies, to (i) prepare a proposal for improving the fee structure, taking into account Council’s concerns over the rising trend in administrative fees and other comments that were made during the Council meeting, together with the findings and recommendations of the Consultant’s Report and the Second Overall Performance Study, and (ii) submit a paper to the Council for its consideration at its meeting in October 2002.

Council’s Concern over Continuing Increase in Project Fees

4. The Council also expressed its serious concern over the continuing rise of project management fees and agreed that this trend must be reversed. The Council expects that the fees for the October 2002 work program will be at a lower fee-to-grant ratio than those in the May 2002 work program. The Council also expects that the proposals for revising the fee system, which it will consider at its October 2002 meeting, will lead to agreement on a system that will result in a lower level of fee-to-grant ratio.

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\(^3\) “Consultant’s Report on an Independent Review of the Fee-Based System” GEF/C.19/12 dated April 19, 2002
II. CURRENT STRUCTURE OF THE FEE-BASED SYSTEM

Project Implementation Services

5. A fee is allocated to an agency for the provision of project implementation services in respect of a GEF-funded project. In summary, these services cover the management and administration of all project-cycle tasks and activities during all phases of a GEF project-cycle from concept to closure (i.e., development, preparation, appraisal, supervision and evaluation). These project-cycle tasks/activities are summarized, in general, in Annex 1.

Flat-Fee Structure

6. During FY00 - FY02, a “flat-fee” structure (summarized in Table 1 below), which established pre-determined fixed flat-fees for typical GEF projects within each GEF project-type, was applied to all GEF projects approved as from July 1, 1999. Premium and discount adjustments to the flat-fee were negotiated for specific projects, as appropriate, to account for the impact of a project being multi-country, multi-agency, innovative or replicative. Importantly, it is necessary to recognize and understand that the flat fee structure was established on the basis of (i) the typical project profile for each project type, i.e., grant size and duration; and (ii) the typical annual work program mix, that were current up until 1999.

Table 1: Flat Fees for a Typical GEF Project

<table>
<thead>
<tr>
<th>Project-Type</th>
<th>INV</th>
<th>TA</th>
<th>MSP</th>
<th>EEA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Flat Fee</td>
<td>$942,000</td>
<td>$382,000</td>
<td>$146,000</td>
<td>$54,000</td>
</tr>
</tbody>
</table>

7. In brief, each project-type’s flat-fee was computed based on the weighted average (weighted by the number of approved projects) of the respective Implementing Agency’s estimated costs for managing the implementation of those project-types in which they have been involved (i.e., WB for investment projects; UNDP and UNEP for technical assistance projects; UNDP, UNEP and IBRD for expedited enabling activities and medium-sized projects).

Fee Components of Staff Week Cost and Project Staff Week Coefficient

8. The computation of a fee for each project-type is basically a function of two primary components – the “Project Staff Week Coefficients” for that project-type and the “Staff Week Cost” of a professional project staff. An agency’s Project Staff Week Coefficient is the number of week’s effort typically required by one professional staff person to perform the relevant activities in each of the four phases of the GEF project cycle (development, preparation, supervision, evaluation) in the complete delivery of the project’s outcome. An agency’s Staff Week Cost is the fully loaded cost of one week of that agency’s professional staff typically

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4 The GEF project cycle is discussed in greater details in the document GEF/C.16/Inf.7 “GEF Project Cycle”.
5 For financial/budgetary management purposes, all GEF projects are categorized as one of four standard GEF project-types: Investment (INV); Technical Assistance (TA); Medium-Size Projects (MSP) and Expedited Enabling Activities (EEA).
6 Based on total number of approved GEF projects as of December 31, 1998.
engaged on the implementation of its projects. Such “fully-loaded” cost would include all costs pertaining to, sustaining and supporting the staff person being fully operational; similar to a billing rate for a lawyer or consultant. These costs are categorized as follows:

(a) Staff Salaries and Benefits
(b) Consultants Salaries/Fees
(c) Staff/Consultant Mission Travel
(d) General Operating Costs
   (typically, support/temporary staff; general services - translation, communications, printing and publications, office equipment and supplies, etc.; contractual services; computing and information systems; and training)
(e) Institutional & Fixed Costs
   (typically, charge back services provided by the agency for administrative, personnel, accounting, auditing, legal, financial reporting, funds disbursement services and the use of office space/facilities)

Fee Ratio

9. Although the current fee structure is predicated upon the application of a flat fee for each of four identified project types, a “fee ratio” is computed for reporting purposes. The use of such a “fee ratio”, which is the fee expressed as a percentage of the underlying project grant value, provides a consistent basis for benchmarking:

(a) the reasonableness of the fee paid by GEF, compared to fees paid by other development agencies/organizations for similar project implementation services; and

(b) project fee performance and behavior between project types, fiscal years and implementing/executing agencies.

Many other funding and development organizations/agencies typically charge for their project implementation management services on the basis of an established percentage of the underlying project grant, as was determined in the Benchmarking Review of GEF’s implementation agency fees.

Agency’s Management and Accounting of Fees Received

10. Under the fee-based system, involved agencies have made significant efforts to enhance their project cost accounting capabilities in order to manage and account for the fees received, as was confirmed during the independent review. The Implementing Agencies have established guidelines and systems for allocating the fees received among their respective organization’s involved units, which provide the relevant project implementation services (e.g., consultants,
travel, etc.) over the duration of their respective projects. The Executing Agencies also have implemented or are developing systems for the accounting and allocation of their fees. The agencies’ management of the proper allocation, and the separate accounting thereof, of the fees provided by GEF is an important foundation for ensuring the adequacy of funds in the provision of the appropriate project implementation services for the successful completion and delivery GEF projects in their respective portfolios. More information on the management and allocation of fees by the three Implementing Agencies are provided in Annex 2.

II. Fee-Based System Experience (FY00 - FY02)

11. For the fiscal years FY00 - FY02, fees totaling US$ 125.2 million were paid in respect of 434 projects with a total grant value of US$ 1,372.1 million, as summarized in the following Table 1 (more detailed summaries are provided in Annex 3).

<table>
<thead>
<tr>
<th>Projects Nos.</th>
<th>Total Grant Value US$m</th>
<th>Total Fees US$m</th>
</tr>
</thead>
<tbody>
<tr>
<td>INV</td>
<td>71</td>
<td>742.56</td>
</tr>
<tr>
<td>TA</td>
<td>75</td>
<td>493.26</td>
</tr>
<tr>
<td>MSP</td>
<td>126</td>
<td>98.33</td>
</tr>
<tr>
<td>EA</td>
<td>162</td>
<td>38.00</td>
</tr>
<tr>
<td>TOTAL</td>
<td>434</td>
<td>1,372.14</td>
</tr>
</tbody>
</table>

Growth in Fee Ratio

12. For the fiscal years FY00 - FY02, an average Fee Ratio of 9.1% had been paid by the GEF to the Implementing Agencies for implementing GEF projects; compared to the range of 8% - 20% typically paid by other agencies/organizations, as confirmed during the 1999 benchmarking review, referred to above. However, over this period, the average overall Fee Ratio for GEF’s annual work program had grown from 7.9% in FY00 to 11.3% in FY02 – an increase of more than 43% - although the average project fee, particularly for the full-size projects, have declined (as summarized in Table 3).
Table 3: Growth of Annual Fee Ratio (FY00 - FY02)

<table>
<thead>
<tr>
<th></th>
<th>FY00 %</th>
<th>FY01 %</th>
<th>FY02 %</th>
<th>FY00-FY02 Average %</th>
<th>FY00-FY02 Growth %</th>
<th>FY00 $m</th>
<th>FY01 $m</th>
<th>FY02 $m</th>
</tr>
</thead>
<tbody>
<tr>
<td>INV</td>
<td>7.2</td>
<td>8.5</td>
<td>12.6</td>
<td>9.2</td>
<td>75.0</td>
<td>0.973</td>
<td>1.019</td>
<td>0.909</td>
</tr>
<tr>
<td>TA</td>
<td>6.4</td>
<td>7.2</td>
<td>6.3</td>
<td>6.7</td>
<td>-1.6</td>
<td>0.489</td>
<td>0.487</td>
<td>0.323</td>
</tr>
<tr>
<td>MSP</td>
<td>19.6</td>
<td>18.0</td>
<td>18.3</td>
<td>18.7</td>
<td>-6.6</td>
<td>0.147</td>
<td>0.145</td>
<td>0.145</td>
</tr>
<tr>
<td>EA</td>
<td>17.7</td>
<td>16.0</td>
<td>13.1</td>
<td>14.7</td>
<td>-26.0</td>
<td>0.037</td>
<td>0.028</td>
<td>0.037</td>
</tr>
<tr>
<td>Average</td>
<td>7.9</td>
<td>8.7</td>
<td>11.3</td>
<td>9.1</td>
<td>43.0</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
</tr>
</tbody>
</table>

13. As the dollar amount of the fee for a project is fixed, based on the flat-fee structure, this resultant growth in the Fee Ratio, over FY00 – FY02, reflects the overall impact of:

   (c) the changing mix of project-types in the annual work program among the different project types, which each have substantively differing grant and fee profiles;

   (d) the decline in the average project grant size, in particular, those of IBRD’s full size projects; and

   (e) an increase in the number of requests for and the average size of premium adjustments, particularly, on full-sized projects by UNDP.

The flat-fee structure, by its very nature, cannot readily accommodate such changes in project and work program project mix profiles.

14. The project and annual work program mix profiles have been impacted upon by a number of factors such as:

   (a) constrained level of available funding,

   (b) increased release of accumulated projects from the GEF Project Pipeline;

   (c) changes in the nature of projects;

   (d) implementing agencies’ operational strategy; and

   (e) introduction of the expanded opportunity executing agencies.

Impact of Changes in Project Profile and GEF Work program Project Mix

15. Change in Project Profile: The changes in overall project profile are reflected mainly in the average size of the project grants and the average duration of a GEF project, as demonstrated in Graph 1 below. The average GEF grant size has decreased because of the funding constraints, combined with an increasing number of projects flowing from a pipeline built up over several years. Thus, while FY02 had the lowest level of Council-approved work program in three years (23% less than FY00), there were 15% more full-sized projects in FY02 compared to FY00.
While the average project duration has declined, the costs of preparing and supervising projects do not decrease proportionately to the size of the project. The impact on the Fee Ratio of the decrease in the average grant size is, to some extent, mitigated by the discount adjustments on the flat fee to reflect the decline in average project duration.

Graph 1: Changes in Project Profiles

<table>
<thead>
<tr>
<th></th>
<th>Average Grant US $m</th>
<th>Average Duration Years</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>FY00</td>
<td>FY01</td>
</tr>
<tr>
<td>INV</td>
<td>13.46</td>
<td>11.99</td>
</tr>
<tr>
<td>TA</td>
<td>7.70</td>
<td>6.75</td>
</tr>
<tr>
<td>MSP</td>
<td>0.75</td>
<td>0.80</td>
</tr>
<tr>
<td>EA</td>
<td>0.21</td>
<td>0.18</td>
</tr>
<tr>
<td>OVERALL</td>
<td>4.36</td>
<td>3.15</td>
</tr>
</tbody>
</table>

16. Two distinctive trends, as summarized in the following Table 4, indicate a decrease of almost 42% in the average grant value of full-size Investment/Technical Assistance-type projects and an increase of 47% in the average grant value of enabling activities. In terms of impact upon the resulting average overall Fee Ratio, the decrease in the average/total grant values of full-size projects bears much greater significance than the increase in the average/total grant values of enabling activities because of the very substantial difference in the dollar value of their respective average grants.

Table 4: Changes in Project Profiles

17. Change in GEF Work program Project Mix: The effective operation of a flat fee structure was premised on the continued execution of a typical annual GEF work program volume and mix within each of and among the three Implementing Agencies. As quite different flat fees apply to each project type, any substantive change in a work program’s project mix would impact upon the total fees payable in relation to the total underlying project grants. This
results primary from (ii) the very much higher fee ratios accruing to Medium-Size Projects and Expedited Enabling Activities compared to the fee ratios for Full-Size Projects; and (ii) because of each agency’s respective comparative advantage concentration in implementing the different project types. The change in annual work program project mix over the period FY00 - FY02 is summarized in Table 5 below.

Table 5: Changes in GEF Work program Project Mix

<table>
<thead>
<tr>
<th></th>
<th>FY00 Projects Nos.</th>
<th>Grant US $m</th>
<th>FY01 Projects Nos.</th>
<th>Grant US $m</th>
<th>FY02 Projects Nos.</th>
<th>Grant US $m</th>
</tr>
</thead>
<tbody>
<tr>
<td>INV</td>
<td>20</td>
<td>269.24</td>
<td>22</td>
<td>263.88</td>
<td>29</td>
<td>209.44</td>
</tr>
<tr>
<td>TA</td>
<td>24</td>
<td>184.81</td>
<td>29</td>
<td>195.68</td>
<td>22</td>
<td>112.77</td>
</tr>
<tr>
<td>MSP</td>
<td>45</td>
<td>33.69</td>
<td>36</td>
<td>28.85</td>
<td>45</td>
<td>35.78</td>
</tr>
<tr>
<td>EA</td>
<td>24</td>
<td>4.94</td>
<td>72</td>
<td>12.70</td>
<td>66</td>
<td>20.35</td>
</tr>
<tr>
<td>Total</td>
<td>113</td>
<td>492.68</td>
<td>159</td>
<td>501.11</td>
<td>162</td>
<td>378.34</td>
</tr>
</tbody>
</table>

18. The two resulting trends with the most impact upon the overall average Fee Ratio is (i) *an increase in the number* of full-size projects but together with a very substantial *decrease in total grant value*; and (ii) a substantial *increase in the number* of enabling activities but with a much greater increase in the underlying total grant value. Since flat fees are paid on a per-project basis, these trends collectively have resulted in a greater increase in the total dollar value of fees relative to the total dollar value of the underlying grants.

19. Implementing Agencies’ Work program Project-Type and Volume Mix: GEF’s and the agencies’ average project-type and overall Fee Ratio, during FY00-02, as they are impacted upon by the project type and volume mix of their respective annual work program, are summarized in the following Table 6:

Table 6: Implementing Agencies Fee Ratio

<table>
<thead>
<tr>
<th></th>
<th>UNDP FY00 %</th>
<th>UNDP FY01 %</th>
<th>UNDP FY02 %</th>
<th>UNEP FY00 %</th>
<th>UNEP FY01 %</th>
<th>UNEP FY02 %</th>
<th>IBRD FY00 %</th>
<th>IBRD FY01 %</th>
<th>IBRD FY02 %</th>
<th>Executing Agencies FY00-02 %</th>
<th>Executing Agencies FY00-02 %</th>
<th>Total GEF FY00-02 %</th>
</tr>
</thead>
<tbody>
<tr>
<td>INV</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>7.2</td>
<td>8.5</td>
<td>12.6</td>
<td>9.3</td>
<td>9.6</td>
<td>18.7</td>
</tr>
<tr>
<td>TA</td>
<td>6.1</td>
<td>9.5</td>
<td>6.8</td>
<td>8.6</td>
<td>4.0</td>
<td>4.9</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>6.7</td>
</tr>
<tr>
<td>MSP</td>
<td>19.9</td>
<td>17.2</td>
<td>16.5</td>
<td>20.0</td>
<td>20.0</td>
<td>20.2</td>
<td>19.2</td>
<td>19.0</td>
<td>18.5</td>
<td>-</td>
<td>-</td>
<td>18.7</td>
</tr>
<tr>
<td>EA</td>
<td>17.4</td>
<td>14.9</td>
<td>13.4</td>
<td>-</td>
<td>18.3</td>
<td>16.6</td>
<td>19.3</td>
<td>18.3</td>
<td>31.8</td>
<td>11.1</td>
<td>14.7</td>
<td>9.1</td>
</tr>
<tr>
<td>Total</td>
<td>7.5</td>
<td>10.7</td>
<td>8.7</td>
<td>11.4</td>
<td>5.0</td>
<td>9.8</td>
<td>7.8</td>
<td>8.9</td>
<td>12.9</td>
<td>n/a</td>
<td>9.1</td>
<td></td>
</tr>
</tbody>
</table>

III. OBJECTIVES AND BENEFITS OF THE FEE-BASED SYSTEM

20. When the fee-based system was conceptualized and designed, certain objectives were recognized as critical to its implementation in order to strengthen financial management and
cost-efficiency efforts. Agencies would be encouraged to tend towards projects on which they have a comparative advantage in terms of operational and cost efficiencies. In the realization of GEF’s annual work program, a fee-based system would enhance ongoing financial management of project implementation by necessitating and ensuring:

(a) transparency of project-direct and corporate management costs through accurate definition, identification and categorization of all costs; and facilitating financial management of their respective differing budgetary and expenditure profiles and behavior patterns;

(b) accountability for project output and performance by establishing relationships between work program delivery costs and work program output; and promoting better understanding and management of the cost profiles, patterns and performance of the Implementing Agencies and GEF projects, through periodic fee analysis and revision; which requires and, thus, encourages improved monitoring and recording of operational and financial data;

(c) predictability and stability in the flow of GEF funds by establishing the total cost of each project at project approval and, thus, facilitating the provisioning of corresponding GEF funds; and

(d) comparability of project implementation cost performance among the Implementing Agencies and GEF projects; and, with external comparators (e.g., development/assistance agencies) through the use of benchmarking, performance indicators/standards, etc..

21. During its implementation over FY00-02, it was also determined that, quite importantly, to maintain the successful operation of a fee-based system, it should be perceived as providing reasonable, equitable and fair compensation to the agencies in the provision of adequate and successful project implementation services. At the same time, the fee-based system should ensure transparency and a clear understanding of the fee determination processes, and the ease and simplicity of operation; while limiting the transaction costs of any fee administration processes.

IV. **Fee-Based System Issues**

22. During the implementation of the fee-based system over FY00 - FY02, a number of important operational issues were identified and experienced. These issues, listed below, were also confirmed by the Independent Review in their discussions with the various implementing and executing agencies:

(a) the absence of clear definitions and distinctions between Investment-type and Technical Assistance-type projects as the relevant fee allocations are dependent upon proper categorization of such full-size projects,
(b) if the allocated fee is expected to enable an agency to fully recover the total costs of its implementation services or if the agency should also consider the operational and non-financial benefits and synergies that are obtained by both the agency and the project, as a result of the incidence of the GEF grant;

(c) the need to establish commonly agreed and defined project implementation services encompassing GEF’s project cycle phases and activities, as cross-referenced to each agency’s respective project cycle phases and activities; and clearly distinguished from executing agency activities covered by the project grant;

(d) the inability to determine clearly that the fee compensates only the additional project implementation services that are required by and resulting from the GEF component of a project;

(e) the lack of transparency of the computation and determination of the flat-fee and associated premium/discount adjustments; with no clear rules governing the determination of premium and discounts; and the relatively time consuming fee negotiation and agreement processes;

(f) project cost accounting systems within many agencies are not set up to record and monitor specifically the costs of implementation services on individual GEF project components and, consequently, do not have substantive cost data readily available in respect of their GEF projects;

(g) expenses are incurred in advance by the Executing Agencies for the supervision of development and preparation of project proposals, which are only covered much later at the time of project approval (it is worth noting that the standing policy of many of the agencies do not allow expenses to be incurred without corresponding funding first being in place);

(h) the Executing Agencies would not be able to support a flat-fee structure that is dependent upon a work program or a portfolio for the recuperation of total costs, as would be possible with the three Implementing Agencies.

23. Also, to address execution issues which were experienced in implementing the fee-based system during FY00-02 and raised by the Independent Review, the design of a revised fee structure should take into account the following characteristics or conditionalities:

(a) fee should compensate the agencies on a project-by-project basis and not be dependent or conditional on the execution of an annual work program;

(b) fee determination/computation should be based on technical criteria and non-subjective;

(c) fee administration must be simple and, if possible, premium/discount negotiations should be completely eliminated;
(d) fee must demonstrate a relationship to or be reflective of the project’s grant value and duration;

V. EVALUATION OF FEE OPTIONS

24. The report of the Independent Review recommended that consideration be given to the following four options of fee approaches, while addressing the issues raised during the review:

(a) a flat fee structure (with or without adjustments) with agency specific levels based upon project type;

(b) a flat percentage of grant size (with or without adjustments and with or without audited percentage rates), utilizing agency specific rates;

(c) a parametric model (e.g., equation or premium schedule) approach that utilizes a limited number of project cost drivers; and

(d) project specific fees based upon project specific agency estimates.

25. In evaluating the appropriateness of each of these options, appropriate attention is paid to ensure that:

(a) the objectives and benefits of a fee-based system are maintained;

(b) the issues identified during the Independent Review are addressed; and

(c) the fee, while reflecting the circumstances of the project, should be referenced to the project-types and should not differ between agencies for the same project-type in order to maximize each agency’s respective comparative advantages.

26. It is important to note that, for the purpose of evaluating these options, analyses has been based on relevant empirical experience and quantitative data (i.e., project-type, grant value, duration, fees) pertaining to the GEF projects (i.e., investment, technical assistance, medium-sized, enabling activities) approved during the period FY00-02. In doing so, for the purposes of discussion, it is assumed that the flat-fee structure and the resulting fees allocated to the projects during FY00-02 represent fair and equitable compensation to the agencies for their project implementation services. These fee options are discussed further in the following paragraphs.

Flat-Fee Structure

27. As originally designed, under this option, a pre-established flat dollar-amount fee is allocated to a project type, irrespective of project-specific grant value or duration. Subsequently, during its implementation in FY00 - FY02, adjustments were made to the flat-fee structure to accommodate parameters such as grant value and project duration. The use of a flat-fee is very critically premised upon the execution of identified annual work programs and project profiles covering all involved agencies. Certain project-specific circumstances (e.g., untypical project duration, multi-agency, multi-country, innovative) may necessitate project-by-project
negotiations of appropriate premium/discount adjustments to the flat-fee. The flat-fee for each project-type is computed based on the weighted average (weighted by the number of approved projects) of the respective Implementing Agency’s cost estimate for those project-types in which they have been involved\(^7\). The formulas that would be utilized in the computation of such flat-fees are summarized in Table 7. The As was implemented during FY00-02, under this option, a pre-established flat dollar-amount fee is allocated to a project type, irrespective of project-specific grant value or duration.

**Table 7: Flat Fee Computation**

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<th>Project Type</th>
<th>Flat-Fee Formula</th>
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<tr>
<td>INV</td>
<td>(ADB Cost Estimate(^8) x no. of projects) + (IBRD Cost Estimate x no. of projects) Total No. of ADB + IBRD Projects</td>
</tr>
<tr>
<td>TA</td>
<td>(UNDP Cost Estimate x no. of projects) + (UNEP Cost Estimate x no. of projects) Total No. of UNDP + UNEP Projects</td>
</tr>
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<td>MSP</td>
<td>(UNDP Cost Estimate x no. of projects) + (UNEP Cost Estimate x no. of projects) + (WB Cost Estimate x no. of projects) Total No. of UNDP + UNEP + WB Projects</td>
</tr>
<tr>
<td>EEA</td>
<td>(UNDP Cost Estimate x no. of projects) + (UNEP Cost Estimate x no. of projects) + (WB Cost Estimate x no. of projects) Total No. of UNDP + UNEP + WB + UNIDO Projects</td>
</tr>
</tbody>
</table>

28. The main difficulties experienced with the use of a flat-fee structure were absence of definitions between Investment-type and Technical Assistance-type projects; the inability of the fee structure to adjust readily to address evolving agency work program mix and project profiles; the absence of clear guidelines/parameters for premium/discount adjustments; and the sometimes involved negotiations needed to agree premium/discount adjustments on certain projects. A flat fee structure enables an agency to reasonably recuperate its annual expenditures only if it has a substantive work program in terms of the number of projects; and if both its project profile and annual work program are assured. The continued use of a flat-fee structure may no longer optimal because of the more dynamic evolution and nature of GEF’s work program and project profiles as a result of a less predictable funding situation, a more diversified strategically-oriented work program, the introduction of seven additional agencies and inadequate identifiable parameters or empirical data for determining premium/discount adjustments.

**Flat Percentage of Grant Size**

29. This option establishes the fee for a specific project by applying a pre-established fixed percentage to the grant value of that project. During the above-mentioned Benchmarking Review of GEF’s project implementation costs, it was determined that most of the development funding agencies and organizations provided compensation for project implementation services in terms of a pre-established fixed percentage of the grant value, without any identification, categorization or classification between project types. One organization utilized a graduated scale of compensation percentages based on the size of the grant value. However, none of these agencies/organizations could explain the calculation or determination of the fixed percentage.

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\(^7\) Specifically, IBRD and ADB for Investment-type projects; UNDP and UNEP for Technical Assistance-type projects; UNDP, UNEP, UNIDO and IBRD for expedited enabling activities and medium-sized projects.

\(^8\) Each agency’s estimated costs for a project-type is a function of its total project “Staff Week-coefficient” and its “Staff Week-cost”. 
applied and/or if such a percentage did fairly and adequately cover the costs of their implementing agencies.

30. By being computed on a percentage basis referenced to a project’s grant value, an assumption is made that the resulting fee would have intrinsically taken into account the project’s complexity and duration, which should be reflected in the amount of the project grant. On this premise, the use of such a pre-established fixed percentage should then eliminate any need for subsequent negotiations for premium/discount adjustments to factor for individual projects circumstances. However, given that certain implementation services do not increase in direct proportion to the grant value, a graduated scale of fixed fee percentages based on a project’s grant value may be more appropriate. If implemented strictly, this option is efficient and non-subjective in the determination of fees; and acknowledges a fee percentage “ceiling” for each project-type, but not a dollar-value ceiling. Under this method, clear definitions have to be established and appropriate percentages computed for each respective project-type. It must be recognized, however, that the relative numbers of approved projects in each project-type will impact upon the overall GEF Fee Ratio, which was 9.1% for FY00-02.

**Parametric Model**

31. A parametric model is based on the use of an established formula to compute the fee of each project by factoring for certain identified project-specific parameters, such as grant size, project duration, etc. In FY01, when it became apparent that sufficient data was not readily available to provide an empirical basis for establishing flat-fee premium/discount parameters for Full-Size Projects, GEF Secretariat developed a parametric fee formula for Investment-type and Technical Assistance-type projects as a model for exploratory consultations, analysis and evaluation with the Implementing Agencies. This “test” formula was simplistically based on an assumption that a project’s primary cost drivers are its (i) grant value (as a proxy for project complexity) and (ii) duration (as an indication of required supervision effort). Also, the formula was developed utilizing the following available data:

(a) GEF’s FY00 approved work program for project grant-size, duration and allocated fee profiles for Full-Size projects; and

(b) each Implementing Agency’s Staff Week costs and project Staff Week coefficients.

32. The “test” formula was expressed as “Project Fee” = (Gr x Pm x Sw$) + (Yr x Sm x Sw$) + (Em x Sw$), where:

(a) (Gr) a project’s grant value and (Yr) its duration would provide the **project-specific variables** in the computation of a project’s fee

(b) Pm (Preparation/Development Multiplier): the number of Staff Weeks required per $1.0 million of grant, as a proxy for complexity and scope

(c) Sm (Annual Supervision Multiplier): the number of Staff Weeks required for supervision of each year of the project’s life
(d) \( E_m \) (Evaluation Multiplier): the number of Staff Weeks required for ICR, audits, etc.; and

(e) \( SwS = \) the fully loaded Staff Week cost\(^9\).

Essentially, the formula’s components of \((Gr \times Pm \times SwS)\), \((Yr \times Sm \times SwS)\) and \((Em \times SwS)\) represent the fee components covering an agency’s project implementation services for a project’s “development/preparation”, “supervision” and “evaluation” phases respectively. The “evaluation” effort was deemed to be quite consistent across projects and, therefore, did not require a project-specific variable.

33. The use of a parametric model establishes a fee computation formula that mechanistically determines a project’s fee by factoring for the project-specific parameters of \( grant-value \) and \( duration \). As with the Flat Percentage option, each respective GEF project-type have to be clearly defined and appropriate multipliers have to be identified and agreed upon for incorporation into the established formula for each project-type. In application, this option would be more suitable for full-size Investment-type and Technical Assistance-type projects, whose project-specific characteristics can vary quite substantially between projects than for Medium-Sized Projects and Enabling Activities, which have more consistent characteristics. This option avoids any need for negotiations of fee adjustments to accommodate project-unique circumstances and, therefore, is efficient and non-subjective in its operation.

**Project Specific Fees**

34. This option requires an agency, for its project implementation services on each individual project, to prepare and provide quite detailed project-specific implementation plan and estimates for all cost categories to be incurred under each of the four GEF project cycle phases for that project. This option would also require GEF Secretariat, individually for each project, to then review and evaluate these project-specific plans and estimates and to subsequently engage in negotiations with the respective agencies in order to agree upon the fee to be allocated for that project.

35. In practice, this option to determining a project’s fee would require (i) very substantive involvement of both GEF Secretariat and agency staff resources to prepare and review the estimates; and (ii) a very lengthy lead time before each work program submission to review and agree on the estimates. To better appreciate the magnitude of effort and lead-time that could be involved, it should be noted that, each year on average, a total of about 150 projects are reviewed and submitted for work program approval, including about 50 Full-Size projects.

**Consideration of Possible Variations of Proposed Fee Options**

36. Although the Fee-Based System was initially based on the foundational premise of a fee based on each GEF project-type to be applied consistently to all agencies, the exercise of some flexibility from this premise could obtain certain cost efficiencies and advantages, depending on each respective agency’s organizational and operational structure. In addition to the above

\[^9\] The Staff Week cost could be adjusted annually to account for inflation/price increases.
options proposed by the Independent Review, for the purpose of providing a different perspective, the following variations were also considered while, importantly, assuring the maintenance of comparative advantage between the agencies in implementing GEF projects.

(a) Fees for all project-types for all agencies based on a single pre-established fixed percentage of a project’s grant-value.

(b) Fees for all project-types based on a pre-established fixed percentage of a project’s grant-value for each respective agency (i.e., each agency may have a different percentage, which is dependent upon the total value of their respective annual work program); the management and allocation of fees between the different projects and project-types being the responsibility of each agency.

(c) Fees for all project-types based on a fee option that is deemed most appropriate and relevant to each respective agency (i.e., agencies do not all necessarily have to determine their fees using the same option).

VI. PROPOSED PLAN OF ACTION

37. The input provided by the three Implementing Agencies, the seven Executing Agencies and GEF Secretariat during their substantive involvement in the Independent Review and their comments on an earlier draft of this report have been taken into account in the preparation of this Interim Report on a Revision of the Fee Structure. On the basis of Council comments and guidance received at this October 2002 meeting, GEF Secretariat, in further consultation and collaboration with the three Implementing and seven Executing Agencies, will:

(a) prepare quantitative analyses of the proposed fee options as a basis for more detailed review, discussion and evaluation (November – December 2002);

(b) finalize the design of a revised fee structure for GEF’s Fee-Based System (January - March 2003); and

(c) prepare and present to Council for its review and approval, at its meeting in May 2003, a Proposal for a Revised Fee Structure, which will be applied to all GEF projects approved by Council and CEO during the three years from July 1, 2003 (March/April 2003).

38. Fees for projects approved by Council and CEO between July 1, 2002 and June 30, 2003 will be determined under the current fee structure; but will be subject to an overall ceiling as recommended by Council, at its meeting in the May 2002.
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 Work program 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
Annex 2

MANAGEMENT AND ALLOCATION OF FEES BY THE AGENCIES

IBRD-GEF

The World Bank implemented a cost-based budget system for its GEF program until FY99, which helped to establish a detailed historical record of costs and enabled the Bank to move to a fee-based budget system in FY00. The Bank adopted the fee-based budget system on the premise that it would recover its reasonable expenses, that the system would be transparent, and that it would incur low transaction costs.

The GEF project fee finances the Bank’s costs during GEF project preparation, supervision and evaluation on project completion. In order to promote genuine country ownership and to build country capacity for project design and implementation, all Bank/GEF projects are prepared by the client, with detailed Bank assistance and oversight. The Bank’s costs are distinct from the client’s costs, and reflect a long established due diligence practice with respect to processing investment operations that is responsive to the Bank’s operational policies and procedures, including environmental and social safeguards as well as technical and fiduciary aspects. Project preparation, appraisal, negotiations and supervision also address country and sector strategies and policy reforms.

The Bank’s fees for GEF projects are based on the actual average, fully loaded, cost of delivering single-country GEF investment projects, as captured by the Bank’s budget systems. They include the costs of regional operations staff as well as environmental specialists, legal department, disbursement, procurement, financial management, accounting, treasury, and evaluations.

The fee income is placed in a specific trust fund account and managed on a work program basis. This permits the Bank to re-allocate resources across regions to finance program development and to respond to changing demand. Within the Bank, utilization of the fee is governed by annual Work Program Agreements between the regional vice presidencies and the Vice President for Environmentally and Socially Sustainable Development, to whom Bank’s GEF Coordination Anchor reports. Each operating region’s GEF WPA establishes program delivery targets, based on discussions with country and sector units, with Bank-wide GEF budget coefficients allocated for different products and each milestone in the project cycle. These coefficients are based on the average Bank fee. It is at the regional operations level that project-specific allocations are made to task teams, reflecting the particular needs of each project from year to year, but remaining within the overall budget envelopes for the region.

The GEF Coordination Anchor regularly monitors each region’s work program delivery and budget utilization, facilitated by Bank institutional and GEF-specific information management and portfolio review systems, and provides management with mid-year and end-year reports.
The regional WPAs are also monitored to ensure that GEF projects are held to performance and cost standards comparable for IBRD and IDA operations.

This system has four main features: (a) it provides flexibility at the Bank-wide and project level to allocate resources as needed; (b) it keeps transaction costs low for budget transfers to a very large number of projects at various different stages of preparation and implementation; (c) it places accountability at the appropriate unit of management; and (d) it permits GEF programming and budgeting to be mainstreamed into Bank country operations.

UNDP-GEF

Fee amounts approved by the GEF Council are recorded in the UNDP/GEF ledger system for financial transactions and monitoring purpose. Fee allocations are categorized as (i) UNDP headquarters and central services; and (ii) UNDP country offices services. Within each category, annual amortization of individual fees pertaining to each project is determined based on the duration of the project and the four phases of the GEF project cycle, i.e. development, preparation, implementation, and evaluation phases.

UNDP headquarters’ allocation of fees is applied to project implementation services pertaining to project development, preparation and implementation costs. The fee pertaining to each approved project is disbursed to reimburse costs incurred in accordance with the incidence of the four project cycles phases. UNDP headquarters’ share also includes reimbursement of the parent organization’s costs incurred in rendering UNDP/GEF project-related infrastructure support with respect to administrative, finance, audit, and information technology activities. The categories of disbursement cover staff costs, consultants, travels, general operating expenses, and the share of institutional/fixed costs such as rent and utilities. All disbursements are recorded and monitored accordingly.

UNDP Country Offices’ fees allocation is used to reimburse country offices’ costs incurred in undertaking GEF project activities worldwide. Transfer of payment is done to the country offices concerned based on the calculated amortized amounts for each project. Again, the fee pertaining to each approved project is disbursed in accordance with the incidence of the four project cycles phases; and all transfers are recorded as UNDP/GEF administrative expenses.

UNEP-GEF

UNEP-GEF maintains a separate GEF Fee Based Trust Fund account for the specific purpose of managing and accounting for the GEF project implementation services fee. All implementing agency fees received from the GEF are credited and all fee related expenses for GEF projects are charged to this account. Separate records are maintained for management purposes, which allocate the fees received among the relevant approved projects and over the expected life of these project. This allocation of fees provides an annual basis against which UNEP-GEF monitors current and estimated future annual fee-related expenditures to ensure proper
management over fund availability for the delivery of its project portfolio. Currently, UNEP-GEF does not maintain records, which account for and monitor project implementation services expenditures against the fees received on a project-by-project basis. However, to provide a more substantive basis for managing and monitoring both the provision of project implementation services and the cost of doing so, definitive steps have already been taken to develop and implement a system which would account for the relevant staff resources and expenditures incurred, on a project-by-project basis.
Annex 3

ANALYSIS OF FEES BY PROJECT-TYPE/IMPLEMENTING AGENCY

1. Full Size Investment-Type Projects

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2. Full-Size Technical Assistance-Type Projects

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4. Enabling Activities

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