Global Environment Facility

GEF/C.23/8/Rev.1
April 29, 2005

GEF Council
June 6-8, 2005

Agenda Item 14

PROPOSAL FOR REVISING THE FEE SYSTEM

Recommended Council Decision

The Council, having reviewed GEF/C.23/8/Rev.1, *Proposal for Revising the Fee System*, agrees with the proposal to implement a flat fee of 9 percent of the GEF grant.

The Council requests the Secretariat, in collaboration with the Implementing and Executing Agencies, to closely monitor the implementation of the new system to ensure that there is an appropriate portfolio balance.

Executive Summary

In fiscal year 2000, the GEF introduced a Fee-based System for the recovery of reasonable costs incurred by Implementing and Executing Agencies for provision of Project Cycle Management Services. Since the introduction of the system, it has been subject to a number of reviews, including a proposal for revising the system, which was discussed by the Council at the May 2003 meeting, where the Council requested the Secretariat to continue with the current system, and present a fee structure proposal for review at the May 2004 meeting. The Proposal was presented, but was postponed for consideration at the June 2005 Meeting.

This document presents a proposal for revising the fee system on all GEF projects approved by Council/CEO commencing July 1, 2005. The proposed fee structure was developed through consultations between the GEF Secretariat and the three Implementing Agencies (IBRD, UNDP, and UNEP). The consultations were based on the guidelines and comments given by the Council at the May 2003 Council Meeting, the GEF experience with the Fee-based System during the period FY00-FY05, as well as lessons drawn from previous proposals and analyses on the fee structure since FY00.

The proposed fee system applies the same flat percentage fee (9 percent of the GEF grant) to all project types. In addition, an adjustment to the present system is proposed to provide the Agencies with the option to request an advance on the fee upon approval of a Project Development Facility (PDF) B or C to cover the project cycle management costs related to development/preparation-cycle phases.

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I. INTRODUCTION

1. This document presents a proposal for revising the fee system on all GEF projects approved by Council/CEO commencing July 1, 2005, for the recovery of costs incurred by the Implementing and Executing Agencies for provision of Project Cycle Management Services (see Annex 1 for definitions of project cycle management services).

Background

2. In fiscal year 2000, the GEF introduced the Fee-based System for the cost recovery by the Implementing and Executing Agencies (acting under expanded opportunities)[1] for the reasonable cost of the provision of Project Cycle Management Services on GEF-funded projects. Since the inception of the system, several steps have been taken in order to develop a more efficient and sustainable fee structure:

(a) Benchmarking Review, April 2000. To reinforce the implementation of the proposed fee structure, GEF Secretariat carried out a Benchmarking Review[2] soon after the system began implementation.

(b) Consultants Report on an Independent Review, April 2002. During its third year of operation, in January - March 2002, the consulting firm of Deloitte & Touche carried out an independent review[3] of the Fee-Based System, which was discussed by the Council at its meeting in May 2002. Council requested GEF Secretariat, in consultation 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 is meeting in October 2002.

(c) Interim report on Revision of Fee Structure, October 2002 Council meeting. Reviewing this paper[4] at its October 2002 meeting, Council provided further guidance and asked that GEF Secretariat, in consultation with the Implementing and Executing Agencies, to present a proposal for review at its May 2003 meeting.

(d) Proposal for Revised Fee Structure, May 2003 Council meeting. After review and discussion of the proposed fee structure[5] at the May 2003 meeting, the Council agreed that the existing system should continue to be applied and requested that

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[1] *Expanded Opportunities for Executing Agencies* GEF/C.13/3 dated April 7, 1999 and *Joint Summary of the Chairs, GEF Council Meeting, May 5-7, 1999* dated May 10, 1999.
[2] *Report on a Benchmarking Review of Implementing Agency Fees* GEF/C.15/Inf.7 dated April 7, 2000.
[3] *Consultant's Report on an Independent Review of the Fee-Based System* GEF/C.19/12 dated April 19, 2002
[4] An Interim Report on the Revision of the Fee Structure, GEF/C.20/5, dated September 16, 2002.
[5] *A Proposal for a Revised Fee Structure,* GEF/C.21/10 dated April 11, 2003

the Secretariat, based on Council's guidelines and comments, present another fee structure proposal for Council review at its May 2004 meeting.

(e) A proposal to revise the fee system (GEF/C.23/8) was submitted to the Council for discussion at the May 2004 Council meeting, but could not be discussed due to the heavy agenda and was postponed to be discussed at the June 2005 meeting.

The Proposed Fee System

3. The proposed revision to the fee system was developed through consultations between the GEF Secretariat and the three Implementing Agencies (IBRD, UNDP, and UNEP).[6] The consultations were based on the guidelines and comments provided by the Council at the May 2003 Council Meeting,[7] the GEF experience with the Fee-based System during the period FY00-FY05 as well as lessons drawn from previous proposals and analyses on the fee structure since FY00. In proposing the new fee structure, the overriding objective of the GEF Secretariat and the Agencies is to establish a system that: (i) is easy to understand and operate; (ii) is more transparent than the present one; and (iii) responds to the Council's request to maintain Agency fee-to-grant ratios at reasonable levels.

4. The proposal for an improved fee system applies the same flat percentage fee to all project types for all Implementing and Executing Agencies. The flat fee is applied to all elements of the project grant, namely all PDFs (A,B,C) and the project allocation. In addition, an adjustment to the present system is proposed to provide Agencies with the option of requesting an advance on the fee upon approval of a PDF-B or PDF-C to cover the project cycle management costs related to development/preparation-cycle phases. The proposed system offers many improvements over the present one, and responds significantly to earlier guidance from the Council.

5. The fee-based system has been in operation at the GEF for nearly six years. The system has been subject to a number of reviews/evaluations and proposals for revisions. There is sufficient data, analysis and operational experience that support immediate transition to a fee system that is transparent, consistent, easy to operate, and does not burden the GEF with unnecessary transaction costs.

[6] A consultation with the Executing Agencies on operational issues was held in Washington in Nov 2004, where the Agencies raised some concerns regarding the proposed system.

[7] *Joint Summary of the Chairs*, GEF Council Meeting, May 14-16, 2003, dated May 20, 2003

II. DEVELOPING THE NEW FEE STRUCTURE

The Current Fee Structure

6. The current fee structure provides a flat fee for each project type, with possible premiums for full-sized Technical Assistance (TA) or Investment (INV) projects, that are multi-country, regional or global or complex single country projects. Table 1 shows the fees in the current system.

Table 1: Present GEF Fee Structure

	Enabling Activities	**Medium-Sized Projects**	**Full-sized Project - Technical Assistance**	**Full-sized project - Investment**
Fee	$54,000	$146,000	$382,000	$1,060,000*

*Typical fee for a seven year project. Fees for individual projects are adjusted according to the project's duration.

7. The current flat-fee system, while an improvement over the earlier mode of providing for recovery of project cycle services costs through the GEF corporate budget, has several weaknesses in implementation:

(a) For full-sized projects, the flat fee system does not fully accommodate the great variances in the characteristics of projects and changes in work program profiles. As a result, premiums had to be negotiated in a relatively high number of cases (86 out of 321 projects, or 27% of cases);

(b) The system is not fully transparent, since the basis for individual fee premiums for full-sized projects, vary from project to project and are not fully elaborated; and

(c) The system involves administrative costs since Agencies have to prepare fee proposals and the Secretariat must review, negotiate and approve them.

8. Deployment of Fees within the Agencies. It is important to note that, while the current system allocates fees on a project basis to the Implementing and Executing Agencies, the Agencies manage their fees at a portfolio level, since the project fees are based on average costs. Within the overall fee resources, the Agencies allocate project preparation and supervision budgets to departments and divisions following coefficients internal to the organizational structure and practices and procedures of the Agencies. These resources are, in turn, allocated to individual project teams in the Agencies, based on the specific needs of each operation. Therefore, project fees, as established by the GEF, have little direct influence in the selection of types and sizes of individual projects at the Agencies.

Council Guidance at its May 2003 Meeting

9. At its meeting in May 2003, the Council provided the following guidelines for the development of the new fee structure:

(a) A distinction in the fees depending on project type (for instance, full-size free standing projects, full-sized projects associated with a larger project of an agency, full-sized projects with co-financing, medium-sized projects and enabling activities);

(b) In reviewing fees for medium-sized projects and enabling activities, the comparative advantages of the agencies and mechanisms designed to address the expected growth in the number of medium-sized projects;

(c) Mechanisms that could lead to more administrative efficiency;

(d) Different incentives to reduce fees such as: competitive bidding; a set level of fees with the possibility of bonuses based on defined criteria; a floor for fees above which greater scrutiny would be given to the justification for higher fees; and use of corporate budget as an incentive to reduce fees.

Incorporation of Council Guidelines in the Fee Structure

10. After careful review of the Council’s guidance, most points were taken into account during consideration of various fee options. However, three of the points mentioned in point (d) above -- competitive bidding process, a set level of fees with possible bonuses, and use of corporate budget as an incentive to reduce fees -- are not compatible with the specific objectives of the fee structure or the structural operation of the GEF as explained below.

11. Competitive Bidding. The idea of establishing a competitive bidding process is based on an assumption that the three Implementing and the Executing Agencies have the same role, responsibilities and capacities. As specified in the GEF *Instrument*, the GEF has been established on the basis of partnership between three Implementing Agencies based on their different, but complementary, demonstrated comparative advantages; the seven Executing Agencies have been brought in to further develop the partnerships based on their respective comparative advantages. The establishment of a competitive bidding system would require structural changes in the GEF's operations as a whole, including the GEF project cycle and the role of the Secretariat. The GEF is not involved in the selection of the Agency for the implementation of a project. Under the current project cycle process, a country has the sole prerogative to choose the Agency(ies) with which it wishes to operate. Therefore, establishing a competitive bidding process involves issues which are beyond the scope of an improvement in the fee system. Finally, the Overall Performance Studies have noted the importance of collaboration and coordination among Agencies, and the damaging effects of competition among Agencies at the country level.

12. Bonuses. To have a set level of fees with the possibility of bonuses based on defined criteria would add complexity to the fee structure with the result that the cost of administration would increase, while transparency would diminish.[8] First, the Secretariat and the Agencies

[8] The current flat fee system includes a provision for premiums for complex full-sized projects such as those involving implementation in multiple countries. The experience is that this is a complex process involving negotiations between the Secretariat and the Agencies that hampers the project cycle.

would have to go through the difficult task of defining set criteria for the bonuses. Given that the Secretariat deals with ten different Agencies, with various cost drivers and project cycles, a common ground would be hard to establish. Second, this process would add an additional step in the GEF project cycle, therefore adding administrative burden and cost to the Secretariat and the Agencies. Third, the criteria will most likely be of a complex technical nature, making the fee structure less transparent to the Council and stakeholders. Furthermore, the fee should allow the agency to fully recover all reasonable costs of Project Cycle Management Services. A bonus system, may mean that the agency might not recover its reasonable costs or might be reimbursed more than its cost, i.e., make a profit. Either of these possible outcomes is not desirable in an effective fee system.

13. Use of Corporate Budget. The use of the corporate budget as an incentive to reduce fees would be counter to the objectives of the Fee-based System. Prior to the establishment of the fee system in FY00, agency fees were incorporated as part of their respective parts of the corporate budget. The fee system was specifically developed to clearly distinguish costs associated with the participation of Implementing Agencies in GEF Corporate activities such as Institutional Relations, Policy/Strategy and Programming, Finance and Management, Outreach and Communications, and Monitoring and Evaluation, from costs directly associated with provision of Project Cycle Management Services.

Options Considered for the Fee Structure

14. In considering options for the new fee structure, the Secretariat and the Implementing Agencies took into account the guidelines provided by the Council at its May 2003 meeting, the GEF experience with the Fee-based System during the period FY00-FY05 as well as lessons drawn from previous proposals and analyses made on the fee structure since FY00.

15. Given the shortcomings of the present fee structure (para 7), a more transparent and flexible alternative that is used in many other development organizations, is a percentage-based fee system.[9] Under this structure, a project's fee is calculated as a percentage of the project grant. With appropriate percentages, this structure responds to the needs of the desired fee structure through its simplicity, transparency and cost-effectiveness. Consequently, three options, which are variations of a percentage fee structure, were considered (Refer to Annex 2 for a detailed assessment of the options):

(a) Option 1. A flat percentage fee to be applied to both Enabling Activities (EA) and Medium-Sized Projects (MSP) and a lower percentage fee applied to Full-Sized Projects (FSP).

(b) Option 2. A flat percentage fee to be applied to both Enabling Activities (EA) and Medium-Sized Projects (MSP) as per option 1 and a scaled percentage applied to FSPs. The scaled percentage would be:

[9] As reported in the *Report on a Benchmarking Review of Implementing Agency Fees*, footnote 2.

(i) for the first $1 million of the grant, the same flat percentage fee as for EAs and MSPs; and

(ii) for the remainder of the grant, a lower flat percentage fee.

(c) Option 3. A single flat percentage fee applied to all project types.

III. PROPOSED FEE STRUCTURE

16. Based on the evaluation of the three fee structure options, a flat percentage fee is proposed (Option 3) in light of its net advantages over the first two options. The flat percentage that is proposed to be applied to all project types of all Agencies is 9.00 percent, which is broadly in line with the historical overall fee ratio of 9.59 percent over the six year period, and much below the average for the past four years (see Table 2). The low ratio allocated to EAs and MSPs is offset on a portfolio level by relatively higher fees paid to the FSPs.

Table 2: Project Allocation and Fee Trends for All Project Types, FY00-FY05*

Fiscal Year	Project Count	Total GEF Allocation ($m)	Total Agency Fees ($m)	Average GEF Allocation ($m)	Average Agency Fees ($m)	Fee Ratio
2000	124	474.63	39.14	3.83	0.343	8.25%
2001	166	494.53	41.03	2.98	0.265	8.30%
2002	197	400.43	45.71	2.03	0.233	11.42%
2003	228	537.16	53.83	2.36	0.237	10.02%
2004	189	645.03	67.35	3.41	0.360	10.44%
2005*	98	282.92	24.80	2.89	0.258	8.76%
Total	**1002**	**2,834.70**	**271.86**	**2.83**	**0.279**	**9.59%**

* Not including June 2005 Work Program

17. This proposal goes a long way in addressing the needed changes in the GEF fee structure, and in fact reduces the overall fees by 0.59 percent, or approximately $16.7m (0.59% x $2834.70 million) over a period of less than six years, or savings of about $2.78 million per year.

18. Furthermore, a benchmarking review reveals that the proposed flat percentage fee of 9.00 percent for the GEF is much lower than most fee percentages allocated in other organizations. Table 3 shows the comparison in fee percentages between the proposed GEF system and other existing systems in various institutions. For some organizations, the numbers shown are the percentage of fundraising and administrative costs as a percentage of total revenue. These are not exactly the same as, but broadly analogous to Agency fees.

TABLE 3: COMPARISON OF FEE PERCENTAGES AMONG MAJOR INSTITUTIONS

Institution	Fee Percentage
GEF (Proposed)	9.00%
National Audoban society	11.60%
United Nations	13.00%
Conservation International	13.20%
National Wildlife Federation	15.30%
Environment Defense Fund	17.20%
World Wildlife Fund	17.30%
Friends of the Earth	18.40%

Source: United Nations and Combined Federal Campaign 2003[10]

Project Development Facility – PDF-As, PDF-Bs and PDF-Cs

19. Presently, fees are paid to the agencies only after Council/CEO approval of projects, which is often a few years after a project enters the GEF pipeline. This means that the Agencies have to bear the preparation/development costs related to the Project Cycle Management Services for the first few years of the project.

20. A new provision is therefore proposed as an option for all Agencies, to request an advance on the project fee at the time of approval of a PDF-B or PDF-C. The suggested fee is 9.00 percent of the value of the PDF-B or PDF-C. At Council approval of the project, the remaining fee that would be paid is: 9.00% x (Total GEF amount (including PDF-A) – amount of PDF-B or C) to avoid double payments. Table 4 summarizes the proposed fee system.

Table 4: Summary of Proposed Fee Structure

Agency	PDF-B or C	EA	MSP	FSP	Premiums
Implementing Agencies: UNDP, UNEP, IBRD Executing Agencies: ADB, AfDB, EBRD, IFAD, IADB, FAO, UNIDO,	Optional 9 % advance on PDF B & C	9%	9%	9%	None

IV. ISSUES PERTAINING TO THE PROPOSED FEE STRUCTURE

Applicability of the Fee Structure

21. Project fees are allocated to Agencies to allow them to recover their Project Cycle Management Services costs so far as they apply to the incremental costs of the projects that are financed by the GEF grant. These include the project Preparation/Development, Supervision and Evaluation phases, details of which are set out in Annex 1.

[10] www.opm.gov/cfc

Dropped or Canceled PDFs/Projects

22. In the case where projects are dropped or cancelled before completion, the unutilized fees will be returned to the GEF Trust Fund as follows:

(a) For any Council or CEO-approved project that is dropped before approval by the Implementing/Executing Agency, 60 percent of the fee would be returned.

(b) For any project cancelled after approval by the Implementing/Executing Agency, fee returns would be prorated based on project duration as stated in the project document approved or endorsed by the CEO.[11]

23. The above arrangement will be applicable only to projects approved by the Council/CEO after July 1, 2005. Definitions of dropped and cancelled are set out in Annex 3.

Steps Towards Reducing Fees

24. In order for the Agencies to be able to reduce their costs related to Project Cycle Management Services, it is strongly recommended that the GEF project cycle be simplified. Since FY00, the transaction costs of GEF business have increased due to new steps in the project cycle, additional GEF project documentation requirements, mobilizing co-financing and coordination with multiple Agencies.

25. A simplified project cycle that would create faster and more efficient project processing, would help reduce the Agencies' preparation/development costs. The Agencies' acceptance of the reduced fees proposed in this paper is in fact linked to a clear expectation on their part that such simplifications will take place.

Maintaining Portfolio Balance & Review of Fee System

26. The proposed portfolio-based fee system will apply to all projects approved by the Council/CEO commencing July 1, 2005. In implementing the fee system, the GEF Secretariat and the Implementing and Executing Agencies will closely monitor any influences on portfolio balance, and will take efforts to maintain the appropriate balance among EAs, MSPs, and FSPs so far as this complies with Council directives.

[11] For example, if a project with a five-year implementation period is cancelled in year two, the Agency would return 36 percent of the fee (retain 40 percent for the period up to Agency-approval plus 12 percent per year for the two years of implementation).

ANNEX 1: PROJECT CYCLE MANAGEMENT SERVICES

1. The GEF project cycle consists of five phases: (i) project concept development; (ii) project preparation; (iii) project appraisal; and (iv) project approval and implementation supervision; (v) project completion and evaluation. These four phases are marked by four decision points: (i) Secretariat review for Concept Agreement; (ii) Secretariat Review for PDF B/C if requested, (iii)Work Program Inclusion; and (iv) CEO Endorsement.

2. To manage a project through the various phases of the project cycle, the Implementing Agencies and Executing Agencies (under the Expanded Opportunity Initiative) have to provide a core set of services for each project. Identified in the following tables are minimum sets of such services for the different types of GEF projects.

3. These services are carried out in accordance with each agency's operational policies and procedures as they may be applicable to the different project types. In particular, the Instrument mandates the agencies to apply to GEF projects their standard due diligence requirements related to financial, economic, legal, environmental, social, and technical aspects, which vary for project types.

Project Cycle Management Services
Full-size projects

Phase of Project Cycle	**Minimum Role of Implementing Agency/Executing Agency**	**Output**
Concept Development		
Identification	• Consult with appropriate stakeholders in-country, including the GEF operational focal point, identify opportunities for GEF financing, using country dialogue and other country planning/sector strategy documents as a basis. • Review options for co-financing and partnerships. • Incorporate GEF opportunity in appropriate planning/country assistance strategy documents of the IA/EA.	Project ideas
Concept Preparation	• Discuss GEF eligibility criteria with operational focal point and other stakeholders. • Undertake brief in-country consultation mission using a PDF-A if necessary. • Consult within IA/EA. • Assist project proponent prepare Concept /PDF-B document in consultation with appropriate stakeholders, including the GEF operational focal point • Assist with preparation of brief (particularly, where preparation of a brief is not handled under PDF-A or B) • Obtain endorsement letter from operational focal point. • Discuss with GEFSEC on pipeline entry	Project Concept Document
Preparation		
Detailed Project Preparation	• Prepare and execute legal agreements for PDF-B. Keep operational focal point informed. • Help project proponent write Terms of Reference for consultant, if required, to undertake PDF-B activities. • Assist project proponent to identify and recruit consultants to assist with project preparation, if necessary. • Supervise project preparation, in consultation with all appropriate stakeholders, including missions to the field, with particular focus on risk assessment, governance issues, execution arrangements, co-financing, capacity development, partnership building and outreach. • Help identify and recruit STAP reviewer; remunerate reviewer. • Negotiate and reach agreement on incremental cost with government and other relevant stakeholders. • Submit Project Document (with Project Executive	Project Document

Phase of Project Cycle	Minimum Role of Implementing Agency/Executing Agency	Output
	Summary) for Council Approval	
Project Appraisal		
	• Appraise project and finalize project implementation arrangements, including mission travel. • Submit Final Project Document for CEO endorsement	Final Project Document
Approval and Implementation Supervision		
Project Approval and Start-up	• Prepare legal and other documentation for approval by IA approval authority • Assist project proponent establish project management structure in country. • Assist project management agency draft TORs and select experts for implementation. • Facilitate project management agency with project start-up workshop.	• Project Document for Signature by Country. • Project Initiation Report
Implementation Supervision	• Mount at least one supervision mission per year, including briefing operational focal points on project progress. • Provide technical guidance, as necessary, for project implementation. • Pay advances to the Executing Agency and review financial reports. • Prepare annual project implementation reports for submission to GEFME • Prepare and participate in PIRs. • Monitor and record project expenditure reports • Prepare periodic revisions to reflect changes in annual expense category budgets	Annual Project Implementation Reports
Mid-term Review	• Undertake mid-term review, including possible project restructuring. Send copy to GEFME	Mid-term Review Report
Completion/ Evaluation		
	• Prepare Project Completion Report/Terminal Evaluation, and submit the report to GEFME. • Prepare project closing documents • Prepare financial closure of the project	Project Completion/ Terminal Evaluation Report

Project Cycle Management Services
Medium-sized Projects

Phase of Project Cycle	Minimum Role of Implementing Agency/Executing Agency	Output
Concept Development		
Identification	• Consult with the GEF Operational Focal point and other appropriate stakeholders in-country, identify opportunities for GEF financing, using country dialogue and other country planning/sector strategy documents as a basis. • Review options for co-financing and partnerships. • Incorporate GEF opportunity in appropriate planning/country assistance strategy documents of the IA/EA.	Project ideas
Concept Preparation	• Discuss GEF eligibility criteria with operational focal point and other stakeholders. • Consultation within IA/EA. • Assist project proponent prepare concept /PDF-A document in consultation with operational focal points and other appropriate stakeholders. • Obtain endorsement letter from operational focal point for PDF-A.	MSP Concept
Preparation		
Detailed Project Preparation	• Prepare and execute legal agreements for PDF-A. Keep operational focal point informed. • Help project proponent write Terms of Reference for consultant, if required, to undertake PDF-A activities. • Assist to identify and recruit consultants to assist project proponent with project preparation. • Supervise project preparation, in consultation with all appropriate stakeholders, including missions to the field. • Negotiate and reach agreement on incremental cost with operational focal point and other relevant stakeholders. • Submit project brief, with operational focal point endorsement, for CEO approval.	MSP Brief
Approval and Implementation		
Project Approval and Start-up	• Prepare legal and other documentation for appraisal and approval by IA approval authority, with special attention to management arrangements, risk assessment, capacity development, partnership building and outreach.	• Project Document for signature by Country • Project

Phase of Project Cycle	Minimum Role of Implementing Agency/Executing Agency	Output
	• Assist project proponent establish project management structure in country. • Assist project management agency draft TORs and help select experts for implementation. • Facilitate project management agency with project start-up workshop.	Initiation Report
Implementation Supervision	• Mount at least one supervision mission per year, including briefing operational focal points on project progress. • Provide technical guidance, as necessary, for project implementation. • Prepare and pay advances to the Executing Agency and review financial reports. • Prepare annual project implementation reports for submission to GEFME. • Participate in PIR. • Monitor and record project expenditure reports • Prepare periodic revisions to reflect changes in annual expense category budgets	Annual Project Implementation Reports
Mid-term Review	• Undertake mid-term review, including possible project restructuring, with the involvement of the operational focal point. • Send copy to GEFME	Mid-term Review Report
Completion/Evaluation		
	• Prepare Project Completion Report/Terminal Evaluation, with the involvement of the operational focal point. Submit a copy to GEFME • Prepare project closing documents • Prepare financial closure of the project	Project Completion/ Terminal Evaluation Report.

Project Cycle Management Services
Enabling Activities under expedited procedures

Phase of Project Cycle	Minimum Role of Implementing Agency/Executing Agency	Output
Proposal Development & Approval		
Proposal Preparation	• Discuss GEF eligibility criteria with the GEF Operational Focal point and other relevant stakeholders. • Help project proponent prepare proposal following the GEF criteria for the appropriate enabling activity. • Review co-financing opportunities and assist with negotiations. • Obtain endorsement letter from operational focal point • Submit proposal for CEO approval	Enabling Activity Project Proposal
Approval and Implementation		
Project Approval and Start-up	• Prepare legal and other documentation for appraisal and approval by IA approval authority, with particular attention to policy issues and capacity development. • Assist project proponent establish project management structure in country. • Help project management agency draft TORs to select experts for implementation. • Facilitate project management agency with project start-up workshop.	• Project Document for signature by Country • Project Initiation Report.
Implementation Supervision	• Mount at least one supervision mission per year, including briefing operational focal points on project progress. • Provide technical guidance, as necessary, for project implementation. • Prepare and pay advances to the Executing Agency and review financial reports. • Prepare annual progress reports. • Participate in annual GEFME stocktaking of EAs. • Monitor and record project expenditure reports • Prepare periodic revisions to reflect changes in annual expense category budgets	Annual Reports to IA to be included in GEFSEC's annual EA stocktaking.
Completion/Evaluation		
	• Prepare Project Completion Report/Terminal Evaluation, with the involvement of the operational focal point. Submit copy to GEFME • Prepare project closing documents	Project Completion/ Terminal Evaluation

Phase of Project Cycle	Minimum Role of Implementing Agency/Executing Agency	Output
	• Prepare financial closure of the project	Report.

ANNEX 2: OPTIONS CONSIDERED FOR THE FEE STRUCTURE

1. Three options were considered for the fee structure:

   (a) Option 1. A flat percentage fee to be applied to both Enabling Activities (EA) and Medium-Sized Projects (MSP) and a lower percentage fee applied to Full-Sized Projects (FSP).

   (b) Option 2. A flat percentage fee to be applied to both Enabling Activities (EA) and Medium-Sized Projects (MSP) as per option 1 and a scaled percentage applied to FSPs. The scaled percentage would be:

      (i) for the first $1 million of the grant, the same flat percentage fee as for EAs and MSPs; and

      (ii) for the remainder of the grant, a lower flat percentage fee.

   Under options 1 and 2, consideration was given to applying floors and caps on fees and to provision for premiums for multi-country, global, innovative and complex projects. The options were simulated with and without floors, caps and premiums and the evaluation of these options is discussed in the next section.

   (c) Option 3. A single flat percentage fee applied to all project types. This option recognizes that implementation costs of different types of projects vary on a project by project basis according to, for example, project type, location, and complexity. However, rather than seeking to provide or mimic cost recovery on a project by project basis, the system seeks to establish cost recovery on the portfolio as a whole. Provision for floors, caps and premiums would not be applicable to such a portfolio-based system.

2. In all three options, the fee percentage is applied to PDFs (A, B, and C) as well as the project allocation.

3. The rationale for a portfolio approach was raised after analyzing GEF's experience with the present fee structure. It was observed that even when fees are allocated by project type, given the large portfolio of the Agencies, and over an extended period of time, the fee ratios for the entire portfolio tend to be similar across the years. This option is discussed in more detail in the following section.

Evaluation of Fee Structure Options

4. The underlying data for the analysis and simulations of the fee structure are the Implementing and Executing Agencies' projects from FY00 up to, and including, the February 2005 Inter-sessional Work Program.

Options 1 and 2

5. During the evaluation process, options 1 and 2 (project type specific fee ratios) showed the potential for many complications:

(a) Challenge of determining appropriate floors and caps. Given the various cost structures of the Agencies, particularly with regards to full-sized projects, the determination of common floors and caps were very difficult. The approach would have to be Agency specific, which complicates the system. Furthermore, even with an Agency approach, given the variety of FSPs that each organization deals with, the evaluation of floors and caps would result in a lengthy and costly exercise.

(b) Cost of negotiating premiums. When both options were simulated with and without floors and caps based on historical percentages, the results showed a high number of projects necessitating premium negotiations, which again increases the administrative cost of the system.

Option 3

6. The portfolio approach presents many advantages over the present system and avoids the complications faced by the other two options. Table A. 1 illustrates allocation and fee trends for the period of the current Fee-based System, FY00-Feb05.

Table A.1 : Project Allocation and Fee Trends for All Project Types, FY00-FY05*

Fiscal Year	Project Count	Total GEF Allocation ($m)	Total Agency Fees ($m)	Average GEF Allocation ($m)	Average Agency Fees ($m)	Fee Ratio
2000	124	474.63	39.14	3.83	0.343	8.25%
2001	166	494.53	41.03	2.98	0.265	8.30%
2002	197	400.43	45.71	2.03	0.233	11.42%
2003	228	537.16	53.83	2.36	0.237	10.02%
2004	189	645.03	67.35	3.41	0.360	10.44%
2005*	98	282.92	24.80	2.89	0.258	8.76%
Total	**1002**	**2,834.70**	**271.86**	**2.83**	**0.279**	**9.59%**

* Not including June 2005 Work Program

7. As can be observed, half of the time, fee ratios are below 10 percent for the entire portfolio for the six year period since the introduction of the system and on average 9.59 percent. In a more detailed analysis, Table A.2 provides the breakdown of historical fees of the Implementing and Executing Agencies by project type.

8. We can draw two important observations from Table A.2. First, even when allocating fees on a project type basis, in the long term, agency fee ratios converge to about 9 percent on a

portfolio basis. Second, individual Agency overall fee ratios are very similar to the overall fee ratio of the portfolio.

TABLE A.2: HISTORICAL AGENCIES' FEES BY PROJECT TYPE, FY00-FY05*

Type	Agency	Project Count	Average Project Size ($m)	GEF Amount ($m)	IA Fees Actual ($m)	% over GEF Amount	% over Complete Portfolio	% over Agencies portfolio
Enabling Activities								
	UNIDO	37	0.468	17.305	1.998	11.55%	0.61%	81.01%
	UNDP	281	0.193	54.283	7.885	14.53%	1.91%	5.37%
	UNEP	109	0.281	30.661	4.284	13.97%	1.08%	9.52%
	World Bank	18	0.284	5.121	0.811	15.83%	0.18%	0.36%
	TOTAL	**445**	**0.241**	**107.370**	**14.978**	**13.95%**	**3.79%**	
Full-sized Projects								
	ADB	4	8.811	35.242	3.083	8.75%	1.24%	93.94%
	IADB	2	3.650	7.300	0.719	9.85%	0.26%	100.00%
	IFAD	1	5.943	5.943	0.565	9.51%	0.21%	100.00%
	UNIDO	1	4.057	4.057	0.382	9.42%	0.14%	18.99%
	UNDP	131	6.656	871.918	73.141	8.39%	30.76%	86.32%
	UNEP	40	6.193	247.730	16.424	6.63%	8.74%	76.90%
	World Bank	142	9.655	1,361.408	128.609	9.45%	48.03%	95.18%
	TOTAL	**321**	**7.893**	**2,533.597**	**222.922**	**8.80%**	**89.38%**	
Medium Sized Projects								
	ADB	3	0.758	2.275	0.438	19.25%	0.08%	6.06%
	UNDP	98	0.856	83.886	14.063	16.76%	2.96%	8.30%
	UNEP	57	0.767	43.746	8.070	18.45%	1.54%	13.58%
	World Bank	78	0.818	63.822	11.386	17.84%	2.25%	4.46%
	TOTAL	**236**	**0.821**	**193.729**	**33.957**	**17.53%**	**6.83%**	
Overall								
	ADB	7	5.360	37.517	3.521	9.38%	1.32%	
	IADB	2	3.650	7.300	0.719	9.85%	0.26%	
	IFAD	1	5.943	5.943	0.565	9.51%	0.21%	
	UNIDO	38	0.562	21.362	2.380	11.14%	0.75%	
	UNDP	510	1.981	1,010.087	95.089	9.41%	35.63%	
	UNEP	206	1.564	322.137	28.778	8.93%	11.36%	
	World Bank	238	6.010	1,430.351	140.806	9.84%	50.46%	
	TOTAL	**1,002**	**2.829**	**2,834.695**	**271.857**	**9.59%**	**100.00%**	

* Not including June 2005 Work Program

9. Based on these observations, the use of a single averaged fee percentage applied to all project types is a credible and sustainable option. Listed below are the main advantages of this option compared to options 1 and 2, and the current system:

(a) Advantages

(i) Simplicity. The fee can be easily computed and does not require specific rules or guidelines.

(ii) Transparency. The Council and other stakeholders would have a clear view on how Agency fees are allocated. In the current system, and under the other two options, premium negotiations take place on some projects, on the basis of project-specific conditions, rather than quantified criteria.

(iii) Credibility. The system is widely used by many other large organizations such as, the United Nations and prominent NGOs (Table 3). For example, the Multilateral Fund of the Montreal Protocol has successfully implemented a percentage-based fee system for a number of years.

(iv) Lower administrative costs. Fee premium negotiations are eliminated therefore saving time at the Secretariat and at the Agencies.

(v) Stability. One of the main concerns of the Council at the outset of the Fee-based System was to prevent fee-to-grant ratios from increasing to unreasonable levels. By using a single percentage, fee-to-grant ratios will be held constant and at reasonable levels.

(vi) Predictability. The Secretariat would have a better idea at the beginning of the fiscal year about the amount of resources that will be allocated to fees for the upcoming Work Programs, allowing better management of future resource commitments. The Agencies on their part, would benefit by being able to plan their cost recovery allocations.

(b) Concerns

(i) The main concern that was raised during consultations is that the portfolio flat percentage fee might provide an incentive to increase average grant size, thus shifting the overall portfolio mix towards more and larger Full-sized Projects at the expense of Enabling Activities and Medium-Sized Projects.

(ii) However, portfolio development and project design are a function of several factors: delivery of global environmental benefits, incremental cost calculations, GEF strategic priorities and funding targets, Agencies' country dialogue, country capacity and priorities, and Agency operational policies and sector strategies, in addition to budget considerations. Moreover, budget allocations at the project level are substantially removed from the fee allocations at the portfolio level. Therefore, the fee of a project is not a significant part of considerations during project choice and design. Project size is more needs-driven than fee-driven. Therefore, it is reasonable to conclude that this fee system will not impact portfolio composition significantly.

ANNEX 3: PROJECTS ENDED BEFORE COMPLETION

1. The following definitions apply to projects that are ended prior to their completion depending on various stages of the project cycle.

(a) Dropped before CEO/Council approval: A project that is ended anytime between pipeline entry/concept and CEO/Council approval.

(b) Dropped after CEO/Council approval: A project is ended anytime between CEO/Council approval and IA approval.

(c) Cancellation without disbursement: A project is ended anytime between IA approval and the completion of the project, but no disbursements have occurred.

(d) Cancellation with disbursement: A project that is ended anytime between IA approval and the completion of the project, where disbursements have taken place.