



GEF/C.41/12/Rev.01
November 17, 2011

GEF Council Meeting
November 8–10, 2011
Washington, D.C.

Agenda Item 15

Criteria for the Establishment of Trust Funds within the GEF

This document is a revision of Council document GEF/C.41/12, *Criteria for the Establishment of Trust Funds within the GEF*, which was posted on the GEF's website on October 12, 2011 for the Council's consideration at its 41st Meeting. This revised document incorporates the changes to document GEF/C.41/12 which were presented to the Council in document GEF/C.41/CRP.01.

Council Decision

The Council, having reviewed documents GEF/C.41/12 and GEF/C.41/CRP.01, *Criteria for the Establishment of Trust Funds within the GEF*, took note of the documents and requested the Secretariat, bearing in mind the comments of the Council, to keep the documents under review and resubmit the proposal in the future at the Council's request.

EXECUTIVE SUMMARY

1. This document addresses the question how does the GEF respond when new priorities, including when new guidance is given by the conventions which the GEF serves and donors agree to fund it through the GEF. Noting that currently new resources cannot be added to the GEF Trust Fund without reopening the programming document, violating the practice of not earmarking contributions, and altering the burden share, this document explores practical options to allow the Facility to respond pragmatically in these circumstances as financial mechanism for the conventions, while protecting the integrity of the GEF and the replenishment process.

2. This document concludes by recommending the establishment of a standing trust fund under which multiple windows can be created within a given replenishment period, as well as criteria for identifying whether to open windows within that standing fund or to integrate new resources and programming guidance into the GEF Trust Fund mid-replenishment. The standing fund would be governed by the GEF Council and would operate under the following specific conditions:

- (a) any new trust fund window would be established in response to new priorities, including convention guidance for which there is not adequate provision in the current GEF programming;
- (b) any new window would be interim in nature, with a requirement that the Council would review each window for decision for mainstreaming into GEF programming prior to the end of the replenishment cycle; and
- (c) contributions to any window in the standing trust fund would be voluntary in nature.

3. Annexed to this document is a set of guiding principles and procedures developed by the GEF Trustee for establishing a standing trust fund to be governed by the GEF Council.

4. When the new resources proposed to be provided at mid-replenishment are expected to exceed a threshold amount of \$100 million, it is proposed that those resources be provided to the GEF Trust Fund and integrated into GEF programming guidance instead of employing a window of the standing trust fund. Similar criteria would govern any decision to take this step, including:

- (a) the GEF Trust Fund should be re-programmed only in response to convention guidance for which there is not adequate provision in the current GEF programming;
- (b) expected contributions would have to amount to a minimum of \$100 million;
- (c) donors would be required to contribute to the fund over and above their regular contributions to the GEF Trust Fund; and
- (d) the additional contributions should be voluntary in nature.

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BACKGROUND

1. At the 39th meeting of the GEF Council in November of 2010, the question of the desirability of and need for creating opportunities within the GEF to capture additional resources to respond to new priorities, including guidance from the conventions for which the GEF serves as a financial mechanism (the conventions), arose more than once. The issue first came up when the Council Member from Japan proposed for the Council's consideration that the GEF Council govern a new trust fund on access and benefit sharing, in response to guidance from the 10th Conference of the Parties (CoP) of the Convention on Biological Diversity (CBD) at the Nagoya meeting. Later, during a discussion on how to strengthen the relationships between the GEF and the different conventions, the issue again arose in the context of how to enable the GEF to respond robustly to new priorities, including convention guidance, that emerge between GEF replenishment cycles.

2. The GEF's inability to respond quickly to new priorities, including new guidance from the conventions, has been raised on many occasions over the years. Most recent discussions have highlighted the inability of the GEF to finance proposed additional reporting obligations under the UNFCCC.

3. The Evaluation Office of the GEF addressed the issue squarely in the Fourth Overall Performance Study of the GEF (OPS4), which noted that when a CoP provides "guidance that would move the GEF in new directions" after a GEF replenishment has been concluded, "the GEF needs to wait until the next replenishment to take such guidance into consideration." OPS4 noted that this problem "is complicated by the fact that GEF does not allow donors to target contributions to special guidance in its main Trust Fund, although this is possible in the Special Climate Change Fund (SCCF)."¹

4. Discussions at the 39th GEF Council meeting acknowledged that this problem has been unresolved for a long time. In order to consider seriously the value of new trust funds as one possible means to respond to CoP decisions and other convention guidance that arise between replenishments, and to place the proposal of Japan in a broader context, the Council requested the GEF Secretariat to prepare a document that would outline general criteria for the establishment of new trust funds within the GEF for the spring 2011 GEF Council meeting. Document GEF/C.40/12, which proposed such criteria, was discussed, allowing Council Members to further articulate their views on this question. The Council requested the GEF Secretariat to revise the document in light of Council comments for the November 2011 meeting.

5. It should be emphasized that establishing a new trust fund governed by the GEF Council is not the only means for the GEF, as a convention's financial mechanism, to respond effectively to donors' desires to finance new priorities, including decisions of the convention. Consequently, this document also explores and compares additional options for accepting new resources into the GEF to respond to new priorities, including guidance from the conventions, that seek between replenishments to move the GEF in new directions.

¹ See OPS4, pp. 44-49.

PROVIDING THE GEF SUFFICIENT FLEXIBILITY TO RESPOND TO NEW PRIORITIES IN A TIMELY FASHION

6. The question to answer is: when new priorities are identified by the Council, including in response to guidance that is given to the GEF and donors agree to pay for it through the GEF, how does the GEF respond? Currently, new resources cannot be added to the GEF Trust Fund without reopening the programming document and altering the burden share. While the time and resources required to reopen the GEF Programming Document associated with the replenishment might be justified if the infusion of resources is going to be significant, it would be a disproportionate response to new priorities that carries with it smaller levels of new financing. Yet, if the GEF does not respond pragmatically in these circumstances, interested donors will naturally put the resources into another institution. The GEF must identify a practical option if it wants to remain as the flexible financial mechanism of the conventions.

7. Allowing donors to place resources under the governance of the GEF Council in response to new convention guidance would not only maintain the integrity of the GEF as an integrated financial mechanism for the major international environmental conventions, it would allow the GEF Council to continue to approve programming across the range of issues related to the conventions. The GEF Council would also be in a position to decide when and how the new area of programming should be folded into, or kept separate from, the GEF Trust Fund during subsequent replenishment discussions.

8. At the same time, some Council Members share an understandable concern not to overwhelm the GEF with multiple new funds, each of which take months of time and substantial financial resources to set up. What the GEF can do to respond to this concern is to minimize the implications of accepting funds between replenishment periods by applying the criteria set forth in this document and by designing a single fund to be governed by the GEF Council to manage donor contributions provided in response to new priorities.

GUIDING PRINCIPLES FOR CAPTURING NEW RESOURCES IN THE GEF BETWEEN REPLENISHMENT PERIODS IN RESPONSE TO CONVENTION GUIDANCE

9. The design of a system whereby the GEF can accept new resources between replenishment periods for specific purposes should be guided by the rationale motivating the policy, namely to respond in a timely manner, to new priorities, including inter alia convention guidance. At the same time, the design must address concerns of Council Members over the establishment of a process to accept new funds between replenishments, including the following:

- (a) Such a system could draw financial resources away from the GEF Trust Fund. Replenishment Participants may reduce their pledges to the GEF Trust Fund in anticipation of creating within the GEF a new means to finance activities in their priority issue areas.
- (b) A system allowing the GEF to accept additional resources for a specific purpose might lead towards an excessive proliferation of GEF trust funds, thereby making the GEF unwieldy, fragmented, and difficult to manage.

- (c) If and when the new programming priorities are to be absorbed into the programming of the GEF, commensurate new resources might not be forthcoming, thus diluting resources available for existing GEF focal area objectives.

ALTERNATIVE MODALITIES FOR CAPTURING NEW RESOURCES IN THE GEF BETWEEN REPLENISHMENT PERIODS IN RESPONSE TO CONVENTION GUIDANCE

10. There are three, progressively difficult, ways to provide new resources to the GEF between replenishment periods: (i) supplementary and targeted contributions to the GEF Trust Fund; (ii) establishing additional trust funds with single or multiple windows; and (iii) expanding the GEF Trust Fund.

Option # 1: Supplementary and Targeted Contributions to the GEF Trust Fund

11. This is by far the simplest and straightforward approach. Council could agree to the GEF Trust Fund receiving supplementary contributions from donors between replenishments, and targeting it to an area within the replenishment package or a new area that is identified for GEF support by the Council, including as a result of new guidance from a convention. Such targeted contributions could be accommodated within the GEF Trust without reopening the entire replenishment package. To ensure that donors do not undermine the integrity of the GEF Trust Fund, the Council could agree that such targeted supplementary contributions from any single donor cannot exceed \$[10] million per year.

Option # 2: Creating One or More New Trust Funds between Replenishment Periods under Specific, Established Conditions

12. There are instances where donors seek to finance activities in response to emerging priorities, including new convention guidance, that involve significantly more sums (at least \$[10] million) and several donors (at least 3, with a minimum contribution of \$[1-3] million from each donor). Concerns regarding earmarking within the GEF Trust Fund may be magnified if we follow option #1. Such circumstances would warrant an alternative option for integrating the resources and programming objectives into the GEF's work.

13. Another option for providing the GEF with adequate flexibility to respond to emerging priorities, including convention guidance between replenishments would be to create one or more new trust funds governed by the GEF Council for specific purposes in response to convention guidance.

14. The GEF has in the past taken decisions to manage new trust funds in response to convention guidance, including the Least Developed Country Fund (LDCF), SCCF, Adaptation and Nagoya Protocol Implementation Fund (NPIF). These funds were created in response to specific new programming priorities of the conventions. However, they were created in the absence of set policies or articulated criteria to guide the GEF Council through its decision to associate these funds to the GEF.

15. Moving forward, the GEF Council could decide to allow for the creation of new trust funds within the rubric of a policy outlining specific criteria for their establishment.

16. Alternatively the GEF could opt to establish a standing trust fund with multiple windows that could be opened and closed as needed to direct financing toward new programming priorities, including new convention guidance, based on a Council decision.

17. This fund would function a bit like the GEF's SCCF or the Strategic Climate Fund (SCF) of the Climate Investment Funds (CIFs) in that it would have the ability to accept contributions targeted for a specific purpose and in that it would have multiple windows. It would differ from these funds in that the programming objectives of the windows could change over time in response to the decisions of the convention parties, the GEF Council, and donors and the windows would all be established with clear sunset provisions and rules for reallocating any money left over when the window closed.

18. The GEF Council would manage and govern either the multiple new funds or the standing trust fund, and the fund objectives would remain in line with the GEF Instrument. However, even if contributions to this fund were to end up rolling over into the GEF Trust Fund upon closure of the fund or of a window in the fund, the contributions would not confer additional voting rights to the donor.

19. Moreover, either of these approaches offers greater flexibility to test out new policies and governance models. For example, there may be a desire to test out in the context of the Nagoya Protocol Implementation Fund (NPIF) options for accepting resources from the private sector and more fully integrating them into programming decisions. While it is possible, in theory, to do this in the GEF Trust Fund, the GEF Trust Fund was not set up with this scenario in mind, and any serious effort to integrate private sector resources would have perverse impacts on voting rights.² It would be easier and carry less risk to undertake a novel policy move in a small, interim trust fund whose programming objectives may or may not be integrated later on into the GEF Trust Fund than it is to modify the provisions of the GEF Trust Fund to accommodate new priorities.

20. The standing trust fund option compares more favorably than does the option of creating multiple new funds. Perhaps the greatest benefit from establishing a standing trust fund over and above creating new trust funds lies in the *significantly* reduced cost and greater efficiency of establishing the standing trust fund. The administrative effort and associated costs required to establish a trust fund are considerable. These would be substantially reduced if the effort were directed to establishing new windows within an existing fund.

21. In addition, the standing fund will establish within the design of the fund itself the criteria articulated above to limit the uses of this financing vehicle to emerging priorities within a limited time frame. These criteria could be built into the design of the standing fund and reflected in its foundational documents.

Specific Criteria for Creating One or More New Trust Funds between Replenishment Periods

22. An articulated set of criteria must guide the decision of the GEF Council to reopen the GEF Trust Fund or to create or open a new fund or a window of a standing fund between GEF

² Contributions to the GEF Trust Fund from non-Participants would impact the voting rights of Participants, because the second leg of the double majority rule for GEF Council decisions requires a 60% majority of total contributions. Private sector contributions would count as part of total contributions and would "dilute" the voting power of Participants.

replenishment periods. The criteria would be carefully constructed to address the legitimate concerns of Council Members not to overwhelm the GEF with multiple new funds and not to undermine the GEF Trust Fund. They would include:

- (a) **CRITERION 1:** (to avoid a proliferation of trust funds at the GEF and to avoid earmarking in the GEF Trust Fund): An initial criterion could be that any establishment of a window under the standing trust fund would occur only in response to new priorities, including convention guidance, for which there are inadequate provisions, on recommendations by the CEO and decided by the Council, in the current GEF programming. A minimum number of donors (3), each with a minimum contribution of \$[1-3] million, would be required. Each window must be funded at a minimum of \$[10] million. These conditions would inhibit an uncontrolled proliferation of funds.

In addition, this condition would not allow the establishment of new windows associated to the GEF at the whim of any individual donor or small group of donors with a purpose of earmarking for specific activities. Individual replenishment Participants would not be able to earmark contributions narrowly to their own priority issues as part of a replenishment, since new priorities, including guidance from the conventions, as decided by the Council would be a condition for establishing any window under the standing trust fund.

- (b) **CRITERION 2:** (to avoid a proliferation of trust funds at the GEF): To further address concerns over the proliferation of funds associated with the GEF, the Council could agree that new windows under the standing trust fund would be interim in nature, with a requirement that the Council review each new window prior to the end of the replenishment cycle. With this review, the replenishment Participants could reconsider the rationale for the creation of the trust fund/fund window in question to determine whether to integrate its programming objectives into the programming framework of the next GEF Trust Fund replenishment cycle. A decision to do so would obviate the need for the new trust fund/window, allowing the Council to terminate it.

Of course, the Council might terminate the window without integrating its objectives into the GEF Trust Fund programming. Alternatively, the Council might decide that the programming priority, while important, is not one that fits well within the GEF Trust Fund, yet wish to keep the new window open for an additional period. To address the concerns over the proliferation of funds within the GEF, it would be important, however, that these new windows be decisively time limited; therefore, an exceptional extension of the life of a window should not be allowed to extend more than beyond one additional replenishment cycle. Moreover, any decision to extend the life of a window would have to be accompanied by pledges of additional contributions adequate to warrant the continuation of the window. The administrative agreements establishing the standing fund and windows would have to clearly spell out the interim nature of the windows, as well as rules for allocating any left-over resources.

Option 3: Expanding the Existing GEF Trust Fund

23. A third option for responding to new priorities would be to accept additional funds in the GEF Trust Fund between replenishment negotiations and integrate the new guidance into GEF programming. Council could undertake this approach, if it is concerned about the perversities of earmarking that may emerge with the approach noted in option 1.

24. Introducing additional resources and new GEF programming mid-replenishment would require the Council to re-open discussions on programming during the replenishment period to establish new programming priorities. This would entail reopening the entire replenishment package, unless explicitly agreed otherwise by every Council Member. A second programming negotiation could be costly and extend some months. Replenishment programming negotiations typically run their course over a period of close to two years. Integrating the new guidance into GEF programming could also mean renegotiating the relevant GEF Focal Area Strategy to account for the intended outcomes and objectives and indicators for the new programming area.

25. While this is potentially a good option in circumstances where donors seek to bring significant sums of additional resources to the GEF, it could prove to be a cumbersome solution for smaller amounts (i.e., less than \$100 million). Consequently, this option should be considered only where substantial additional contribution would justify such additional effort.

26. Moreover, any decision to accept additional funds in the GEF Trust Fund and integrate new guidance into GEF programming should ensure that the new contributions and programming do not, in the future, dilute resources available for existing GEF focal area objectives and also not constitute earmarking at the GEF. Consequently, such an approach should be followed only where specific criteria have been met:

- (a) **Criterion 1:** (to avoid earmarking in the GEF Trust Fund): An initial criterion could be that any expansion of the GEF Trust Fund would occur only with Council decision based on emerging priorities, including in response to new convention guidance for which there are inadequate provisions in the current GEF programming. This condition would prevent the expansion of the existing GEF Trust Fund at the whim of any individual donor or small group of donors with a purpose of earmarking for specific activities. Individual replenishment Participants would not be able to earmark contributions narrowly to their own priority issues as part of such contributions to the GEF Trust Fund, since the entire Council will have to decide on the new priorities for which resources need to be provided.
- (b) **Criterion 2:** (to ensure that donors do not dilute the GEF Trust Fund by expanding the programming objectives of the Fund without commensurate increases in pledges): To address concerns over a potential proliferation of programming priorities within the GEF Trust Fund, the Council could agree that the Trust Fund would not be expanded unless new donor contributions were anticipated to amount at least \$100 million.
- (c) **Criterion 3:** (to avoid drawing money away from the GEF Trust Fund). Another rule or practice could serve as a safeguard against the concern that the reopening the GEF Trust Fund programming could divert resources from the existing GEF focal area objectives. Donors will have to provide the additional contribution in addition

to honoring their pledges under the GEF replenishment. Only amounts provided over and above the original pledged amounts could be directed toward programming activities under the new programming objectives.

27. The option of accepting additional funds in the GEF Trust Fund could be way of integrating the new priorities into GEF programming where the additional funds are significant enough to warrant entering into new programming discussions, but without the concerns of earmarking associated with the first option. It must be acknowledged, however, that GEF programming documents are usually presented to the GEF Assembly after they have been completed. Presenting a renegotiated programming document to an Assembly, in between replenishment periods would be impractical.

CONCLUSION

28. It is important that the GEF develop rules and mechanisms to allow the Facility to respond readily to important new priorities, including guidance from the conventions that the GEF serves as the financial mechanism. Where donors are prepared to provide new resources in excess of \$100 million to finance activities in response to new priorities, it makes sense to reopen the entire programming package of the GEF Trust Fund to allow the GEF, to program for the new priorities. Reprogramming should take place, however, only where there are inadequate provisions in the current GEF programming to respond to the new priorities and if the further contributions are in addition to donors' pledge commitments under the current GEF replenishment.

29. The option of employing a standing fund with multiple windows offers an attractive means to respond in a timely fashion to innovations and fresh priorities, including those of the conventions throughout the entire replenishment cycle, without the concerns of earmarking within the GEF Trust Fund. The conditions imposed by the suggested criteria protect the integrity of the GEF Trust Fund and maintain the practical efficiency of GEF operations while allowing the GEF to serve as a more responsive financial mechanism to its conventions and to emerging environmental priorities.

30. Where the additional resources in response to new guidance are expected to be less than \$100 million, however, the establishment of a standing trust fund in which multiple windows can be created is recommended under the following specific conditions:

- (a) any new trust fund windows should be established only in response to new priorities, including convention guidance, as decided by the Council on the CEO's recommendation for which there is not adequate provision in the current GEF programming;
- (b) new windows must be interim in nature, with a requirement that the Council would review each window prior to the end of the replenishment cycle and the administrative arrangements for the standing fund and/or windows must reflect this fact;
- (c) contributions to any window in the standing fund should be voluntary in nature.

31. The alternative scenario, where the GEF is not sufficiently flexible to respond to new priorities, could have a negative impact on the GEF and on the general perception of its usefulness as a financial mechanism of the conventions. It would also likely lead to further fragmentation of international assistance for global environmental issues, as donors wishing to be responsive to the conventions would establish alternative financial mechanisms to host required new funds. This would lead to a proliferation of funds; albeit, not a proliferation of funds *at the GEF*, but a proliferation of funds, nevertheless, with all the attendant inefficiencies. This outcome would undermine the fundamental premise of the GEF, to have a single, integrated financial mechanism for the major international environmental conventions.

32. On the other hand, if the GEF were to operate interim funds to respond to new priorities, including guidance of the conventions, the GEF Council would retain oversight over the future of these funds—their programming priorities could be folded into or kept separate from the GEF Trust Fund at the discretion of the GEF Council. In this way the fundamental premise of the GEF: to have a single, integrated financial mechanism for the major international environmental conventions would be maintained and even strengthened. And the number of trust funds dealing with global environmental issues related to the conventions could more readily be rationalized. The GEF Council would continue to exercise significant influence over the coherence of multilateral environmental financing.

33. Finally, the GEF has demonstrated efficiencies, both financial and programmatic, that are generated currently by its secretariat's managing other funds, including the SCCF, the LDCF and the Adaptation Fund. Fostering synergies across themes for higher impact and reducing the costs of providing the necessary technical screening of projects and programs proposed for funding are significant comparative advantages of the GEF.

ANNEX 1: PRINCIPLES FOR ESTABLISHING A STANDING GEF TRUST FUND WITH MULTIPLE WINDOWS

The following summarizes guiding principles and procedures developed by the GEF Trustee for establishing a Standing Trust Fund to be managed by the GEF:

Guiding Principles:

- The objectives of the Standing Trust Fund should be aligned with the priorities of the GEF and its mandate;
- The Standing Trust Fund may have multiple Windows, each dedicated to a GEF focal area/convention/priority;
- The Windows should fund only those activities that cannot be funded through any existing trust fund managed by the GEF;
- Windows should be established only in response to new CoP guidance for which there is not adequate provision in the current GEF programming.
- The establishment of Windows must be approved by the GEF Council after a review and assessment of risks (financial, reputational, operational);
- The World Bank, as Trustee, reserves the right to decline the establishment of any new Window.

Governance and Organizational Structure:

- The GEF Council will have the overall authority and responsibility for governance of the Standing Trust Fund including Windows;
- The rules and procedures and governance structure of the GEF will apply to the Standing Trust Fund including its Windows, unless modified by the GEF Council in agreement with the Trustee;
- Roles and responsibilities of the GEF Trustee and Secretariat, under the GEF Instrument will apply to the Standing Trust Fund;
- Eligible Implementing Agencies and Executing Agencies (including any new agencies through an approved accreditation process) will have the same eligibility to access funds as for the GEF, and their roles and responsibilities as defined under the GEF Instrument or its policies taken by the GEF Council will apply;
- The duties and responsibilities of the CEO/Chairperson of the GEF as defined under the GEF Instrument will apply to the Trust Fund.

Operating Procedures:

- The Standing Trust Fund will follow all policies and procedures applicable to the GEF Trust Fund under the GEF Instrument (as amended from time to time);
- The rules and procedures of each of the eligible Agencies apply to the use of funds;
- Allocation of resources will be proposed by the Secretariat and approved by the GEF Council;
- The Memorandums of Understanding entered into between the GEF Secretariat and the Agencies for the purposes of allocation of GEF resources shall apply to this Standing Trust Fund;
- The duties and responsibilities of the Trustee and the Agencies under the Financial Procedures Agreements between the Trustee and the Agencies will be effective for the Standing Trust Fund;

Standing Trust Fund Structure:

- Donors can designate their contributions to one or more Windows;
- Windows can co-exist concurrently but the activities to be funded should not overlap across Windows;
- Investment income will accrue to each respective active Window;
- Windows will have a finite life term and shall close at the end of the replenishment period in which they were established, unless otherwise agreed by the GEF Council, and the unallocated balances be moved to the GEF Trust Fund;
- Transfer of resources between Windows will not be allowed;
- Records and transactions for contributions to each Window and transfer of funds to recipients will be maintained;
- The Trustee will report to the Council on an annual basis the financial situation of the Standing Trust Fund;
- The Standing Trust Fund is expected to follow the single audit procedure of the World Bank.

Internal Approval in the Bank:

- Once the GEF Council approves the establishment of the Standing Trust Fund, the proposal will be sent for Senior Management Review and the World Bank Executive Directors for approval;
- The Standing Trust Fund will be established in accordance with the policies and procedures applicable for establishment of Trust Funds in the Bank.