

PROPOSAL FOR REVIEW

PROJECT TITLE: BELIZE, COSTA RICA, EL SALVADOR, GUATEMALA, HONDURAS, NICARAGUA, PANAMA: CENTRAL AMERICAN FUND FOR ENVIRONMENT AND DEVELOPMENT: ACCOUNT FOR THE GLOBAL ENVIRONMENT

GEF FOCAL AREA: Biodiversity, Climate Change, International Waters

GEF ELIGIBILITY: All countries in the region have signed and ratified the Convention on Biological Diversity and the Framework Convention on Climate Change

TOTAL PROJECT COSTS: US\$ 28 million

GEF FINANCING: US\$ 15 million

GOVERNMENT COUNTERPART FINANCING OF GEF COMPONENT: Central American Governments: US\$ 2 million

CO-FINANCING: Other donors: US\$ 11 million (expected)

PARALLEL FINANCING: Multilateral Investment Fund, Inter-American Development Bank: US\$ 25 million (amount under discussion)

ASSOCIATED PROJECT: None

GEF OPERATIONAL FOCAL POINT: Mr. Jorge Cabrera - Executive Secretary- Central American Commission for Environment and Development (Comisión Centroamericana de Ambiente y Desarrollo - CCAD)

GEF IMPLEMENTING AGENCY: United Nations Development Program (UNDP)

EXECUTING AGENCY: Central American Fund for Environment and Development (Fondo Centroamericano de Ambiente y Desarrollo - FOCADES)

LOCAL COUNTERPART AGENCY: Not applicable

ESTIMATED APPROVAL DATE: October 1996

PROJECT DURATION: 10 years

GEF PREPARATION COSTS: None

OTHER PREPARATION COSTS: US\$ 107,000 from the Center for Sustainable Development in the Americas (CSDA) for the design and establishment of FOCADES

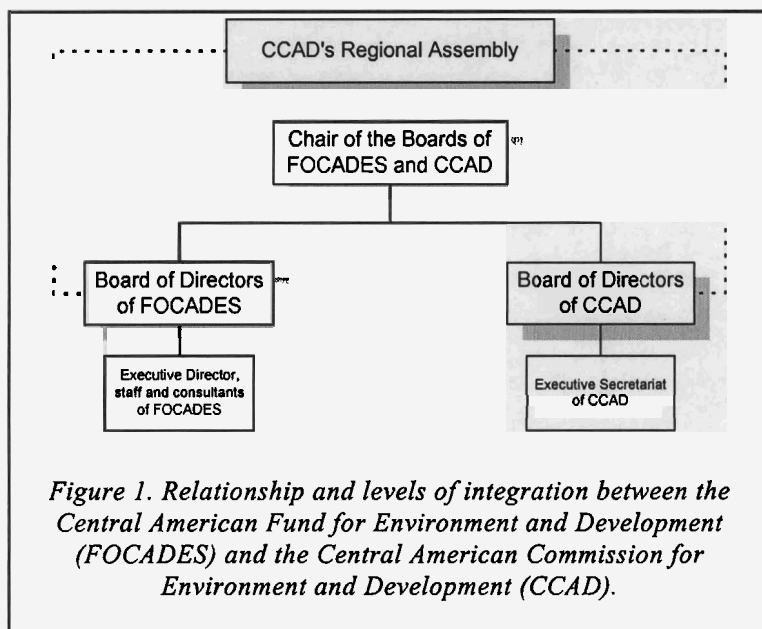
BACKGROUND

1. Central America holds vast natural resource riches because of a combination of biological, geological and historical factors. Central America's location, at the meeting point between the North and South American continental masses, its contact with the Pacific and Atlantic Oceans, its wide-ranging topographic formations, and its geological history, account for the staggering diversity of life and natural resources that can be found there. Unfortunately, these vast resources are under intense pressure and continuous threat. Unchecked population growth, over-exploitation of natural resources and its collateral damage, pollution from unregulated industrial and urban growth, economic and social inequities, and political instability have all contributed to the consolidation of development practices that have chipped away at the foundations that support the well-being of the peoples of the region. For the last 500 years, Central America has been in a permanent state of natural asset liquidation. This has not rid the region of all its natural wealth, only because of the vast quantities it once possessed. Things are much different now, however. More and more, the countries of the region are beginning to experience the limitations imposed on them by centuries of misguided development and resource use practices.

2. Very aware of the critical state of the region's affairs, the threat to the long-term welfare of their nations, and the urgent need to incorporate the environmental sustainability dimension into their development policies, the Heads of all the Central American States met in Managua in October 1994 to sign the Central American Alliance for Sustainable Development (the *Alianza*). In this document, the Presidents of Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua and Panama, and the representative of the Prime Minister of Belize, formalized their commitment to sustainable development. They viewed this undertaking as reaching every aspect of the lives and governance in their respective countries. The *Alianza* proposes to deal with political, economic, social, and environmental inequities in order to ensure the viability of the nations, and the region as a whole. One of the elements of the *Alianza* was the call for the establishment of a financial instrument that could develop a coherent and cohesive investment strategy and could provide stable financing for the sustainable development agenda being proposed. From this mandate the Central American Commission for Environment and Development (Comisión Centroamericana de Ambiente y Desarrollo - CCAD), with the support from the Center for Sustainable Development in the Americas (CSDA), embarked upon the design of the Central American Fund for Environment and Development (Fondo Centroamericano de Ambiente y Desarrollo - FOCADES). Detailed information on FOCADES and CCAD is included in Annex B.

3. FOCADES is conceived as a multiple fund with the ability to establish individual accounts pursuing specific objectives consistent with the regional agenda. Although an independent organization, FOCADES will have strong ties with CCAD (see Figure 1). They will share the same regional assembly, which currently exists in the context of CCAD. This assembly brings together representatives of the principal stakeholders in the region to provide guidance and advice to CCAD. This role will be extended to FOCADES once it begins to operate. Another important link in the integration between CCAD and FOCADES will take place at the level of the board of directors. The boards of directors of CCAD and FOCADES will be chaired by the same person in representation of the regional governments. He/she will be the only government representative on FOCADES's board. This level of integration will ensure that the environmental agenda developed by CCAD will drive the environmental investment priorities of FOCADES, and not the other way around. The other members of the board of FOCADES will include

representatives of regional community based organizations, nongovernment organizations, private sector associations and academic institutions. Donors will also have the opportunity to participate in board deliberations.



4. Operationally, FOCADES will adopt a modular structure based on various types of accounts according to agreements reached between the donors and FOCADES management. The Account for the Global Environment (the Global Account) will be the first account of FOCADES, providing the GEF with a unique opportunity to incorporate global environmental concerns into one of the most important instruments for sustainable development in the region. This modular structure will enable FOCADES to control operational expenditures by

adjusting the numbers and qualifications of its staff and consultants as needed by the different accounts. Programmatically, FOCADES will support regional initiatives¹ through grants, loans and technical assistance. It will rely on the national and regional installed capacity for project identification, screening, and implementation. This approach will permit FOCADES to be streamlined with regard to staffing, without compromising its effectiveness. By virtue of its structure FOCADES will be especially well placed to marry the goals of its accounts. By co-financing project components from its various accounts, it will seek to achieve not only inter-regional, but also programmatic synergy towards the sustainable development of the region.

PROJECT OBJECTIVES

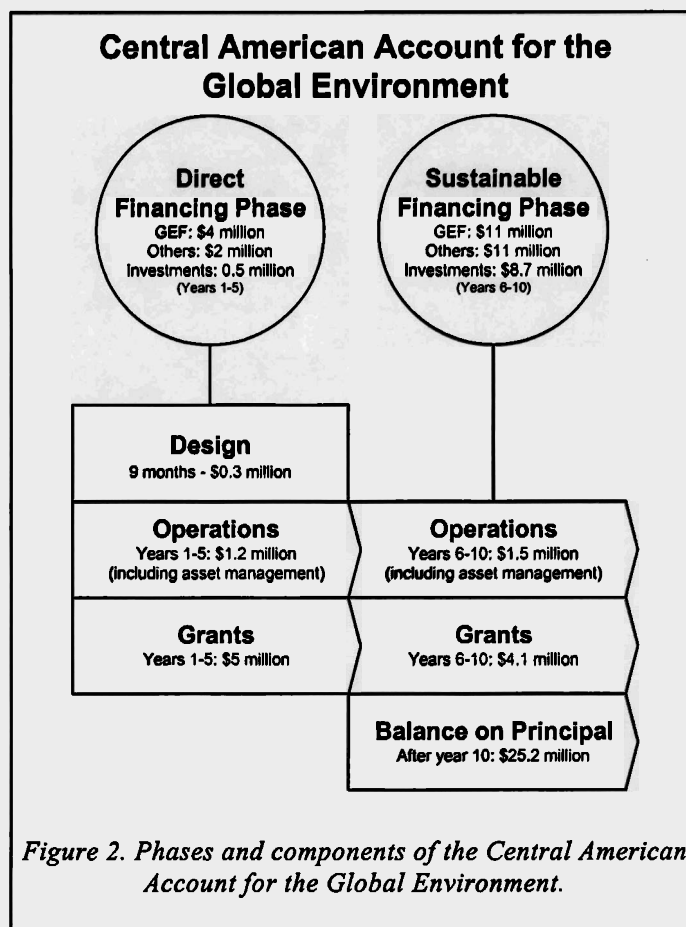
5. The main objective of the Global Account is to ensure the long-term financing of critical regional environmental activities of global relevance. This will be accomplished by: (a) establishing an account to provide funding, in perpetuity, for projects in the three relevant focal areas of the GEF (biodiversity, climate change, and international waters); (b) contributing to the establishment and operations of FOCADES, as the framework under which global and regional environmental and sustainable development initiatives will be supported; (c) actively promoting the participation of national and regional level organizations – from the public and private sectors – in the design and implementation of regional projects, or national projects of regional

¹ By regional initiatives are understood all those projects that involve more than one country, national components of regional projects, or other regionally relevant activities. The formal definition of what could be considered a regional initiative in the context of this project will be developed during the design of the Regional Account, as described in Annex A. .

relevance; and (d) establishing transparent administrative and operational procedures in order to ensure the long-term support of donors, governments and civil society in general.

6. The Global Account is intended to finance the incremental costs of activities associated with regional initiatives and/or national activities of regional relevance coordinated by the CCAD and consistent with GEF priorities. However, the limited amount of resources available for disbursement (less than US\$ 1 million per year among seven countries and three focal areas) will not preclude other GEF programming in the region. Instead, it is being designed to provide small-scale, targeted and strategic funding for incremental activities likely to have strong leveraging, catalyzing, and streamlining effects at the regional level. For example, the Global Account could finance the incremental costs of activities aimed at sustaining and replicating successful pilot experiences in sustainable use of biodiversity as demonstrated or promoted by other programs financed by the GEF and/or other bilateral or multilateral sources, e.g., Mesoamerican

Biological Corridor². The CCAD is coordinating the establishment of the Mesoamerican Biological Corridor, an initiative encompassing a number of both short and long-term programs that will require more funding than the GEF is likely to be able to provide on a sustained basis. National and regional activities within the framework of the Corridor – beyond the initial investment to be made by the GEF, GTZ and other donors to establish the foundation of the Corridor itself - would conceivably be eligible for funding under the Global Account. The Global Account is expected to focus not solely on the Mesoamerican Biological Corridor initiative, but on a growing variety of regional, binational or trinational initiatives. This example serves to illustrate the role that the Global Account can play to ensure the long-term viability of similar regional initiatives.



² This initiative identifies the principal strategic interventions required to establish and sustain a multi-national land management commitment that will link regionally significant ecosystems and habitats into a globally significant biological corridor network, through the consolidation of a continuous system of protected areas, buffer zones and land corridors across Central America.

PROJECT DESCRIPTION

7. The project will be implemented in two phases: (1) in the direct financing (sinking fund) phase the Global Account will be designed and established, and funding of regional projects will begin based on the first phase of disbursements from the GEF; and (2) in the sustainable financing (endowment) phase the Global Account will be capitalized so that it can provide grants, loans, and technical assistance for regional initiatives with income generated from the investment of the principal. Each of these project implementation phases will consist of at least two principal components: (a) operations and management of FOCADES and the Global Account, and (b) the grants program, *per se*. The design of the Global Account will be a separate initial component, under which all the operational and legal instruments will be developed; the design component will be executed first as part of the direct financing phase of the project (Figure 2).

PROJECT IMPLEMENTATION PHASES

Direct Financing Phase

8. This phase will have a duration of five years and an estimated cost of US\$ 6.0 million (US\$ 4 million GEF and US\$ 2 million in matching funds) to be disbursed in equal annual amounts as a sinking fund. An additional US\$ 0.5 million will be obtained from the investment of these contributions. This phase will be organized in three components: design, operations and the grants program. These components are described in detail in the following section. With the exception of the first year, when the design activities will be taking place at an estimated total cost of US\$ 0.3 million, over 80% of the funds received from the GEF and other donors will be used to support eligible projects through the grants program. The operations and management costs of the Global Account are not expected to exceed US\$ 0.24 million annually. These costs include the fees of an asset manager, who will be hired to invest the contributions from GEF and other sources. Although revenues from these funds are not expected to be high, they will provide an opportunity for FOCADES to develop experience in commissioning and supervising the management of financial investments required for the implementation of the sustainable financing (endowment) phase of the project.

9. At the end of the direct financing phase, an evaluation of the Global Account will be performed by the GEF. The following phase – sustainable financing phase – is only expected to be approved if the evaluation shows that (1) FOCADES has managed the grants program effectively and efficiently; and (2) sufficient matching funds have been raised to bring the principal amount to at least US\$ 22 million.

Sustainable Financing Phase

10. On the sixth year of the project and contingent on the outcome of the evaluation of the direct investment phase, the GEF will disburse the balance of the grant (US\$ 11 million) which will be matched, one-to-one, by an additional US\$ 11 million from other sources. These funds will be transferred to the Global Account where they will be used to generate revenues (estimated at US\$ 8.7 million in years 6-10), in perpetuity, to support regional initiatives consistent with the objectives of the GEF and the *Alianza*. Given that the nature of the grant would make it difficult to establish a closing date, for the purposes of the GEF, the sustainable financing phase will last 5 years, bringing the total life of the project to 10 years. In this period

UNDP, as the GEF implementing agency, will supervise the project and conduct periodic evaluations as described below.

11. This phase will consist of two components: (a) the operation and management of FOCADES and the Global Account; and (b) the grants program funded with the revenue from the investment of the Global Account's principal.

PROJECT COMPONENTS

Design of the Account for the Global Environment

12. All the operational, administrative and legal instruments of the Global Account will be prepared under the design component of the direct financing phase of the project. Additionally, four pilot projects will be developed for funding as soon as funds for grants become available. The goals of these pilot projects are first, to launch the Global Account as soon as it becomes operational; and second, to test and review all the operational and administrative procedures for the processing and management of the grants program.

13. The design component will produce the final project document which will include the following supporting documentation: (a) guidelines for the processing of projects, including selection and eligibility criteria, and technical review process; (b) guidelines for the selection of the endowment account manager and for the management of the investments; (c) administrative and operational manuals; (d) legal instrument and internal regulations; (e) a supervision, monitoring and evaluation plan; and (f) an implementation plan. Additionally, there will be a series of sectoral and regional workshops aimed at involving a broad range of institutions in the design of the Global Account and the preparation of the pilot projects. *A detailed description of the design component can be found in Annex A. .*

14. In a parallel and concurrent process, CSDA and CCAD are designing FOCADES in close coordination with the UNDP/GEF, MIF and other potential donors. These activities are aimed at establishing the umbrella in which the Global Account will be anchored. The formal establishment of FOCADES is expected to take place by mid November. The estimated cost of the design of FOCADES is US\$ 107,000, which is being covered by CSDA with grants from the Rockefeller, Ford and MacArthur foundations. The Global Account will be the first account of FOCADES, giving the GEF the opportunity to contribute significantly to the definition of FOCADES's operational and administrative procedures, and to set the tone for the management of future funding. For these reasons, the opportunity to start the FOCADES with a GEF-funded account should be taken as an important challenge in the development of regional, multi-country, environmental initiatives of global relevance. *A full description of FOCADES can be found in Annex A. .*

Operations and Management

15. This component includes support for the operations of FOCADES and the management of the Global Account. Funding will be provided for staff and consultants, equipment, travel, general expenditures, and the costs of the asset manager. During the direct financing phase these expenditures will not exceed 20% of the grant amounts. In the sustainable financing phase the GEF financed operational and management costs of FOCADES and the Global Account will not

exceed 1.3% of the principal. Detailed cost estimates for operations and management will be made as part of the design activities.

Grants Program

16. The funds allocated for the grants program will be used to support regional projects in the three relevant GEF focal areas: (a) biodiversity; (b) climate change; and (c) international waters; this will include projects in the area of land degradation and desertification as it relates to the three areas. As part of the design activities, detailed project eligibility criteria will be developed in consultation with GEF, other donors and regional stakeholders to ensure ownership, promote leverage and maximize impact. Additionally, project size estimates will be made to assess more accurately the funding requirements and the relative level of support that the Global Account will provide.

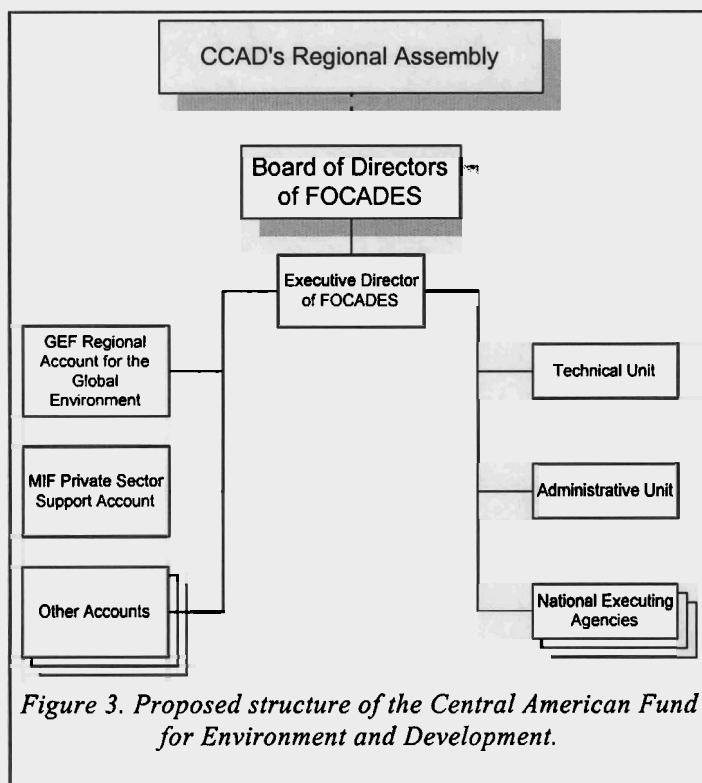
INSTITUTIONAL FRAMEWORK FOR PROJECT IMPLEMENTATION

Institutional Framework

17. The Global Account will operate within the framework of FOCADES. The design characteristics of both FOCADES and the Global Account emerge from the extensive consultations conducted at the regional and national levels and on the recommendations of the UNDP/GEF mission report of June 1995. The design effort of FOCADES is proceeding at an accelerated pace under the coordination of CSDA and CCAD. The target date for its official establishment is mid November 1996 when the Central American Heads of State are expected to meet in a regional summit. *A detailed description of FOCADES can be found in Annex A.*

18. FOCADES is being designed to be an umbrella fund (Figure 3) with the following characteristics: (a) a board composed of representatives of the governments of the region, indigenous groups, academic institutions, non-government organizations, and the private sector; (b) the flexibility to manage funding from different sources and with different emphasis without compromising the conceptual integrity and mandate of the *Alianza*; (c) the administrative and operational transparency and flexibility to ensure broad support from the public and private sectors and civil society as a credible instrument to organize, increase and manage investment flows for regionally relevant environmental and sustainable development initiatives; (d) the implementation of regional projects or national components of regional programs through national executing agencies based on a competitive process; and (e) a close integration with CCAD, to ensure coherence and consistency between policy and investments (Figure 1). Although these two organizations will be autonomous and independent, the integration of FOCADES and the CCAD will be accomplished on two levels: (1) the Chair of the Board of Directors of CCAD will also chair the Board of Directors of FOCADES; and (2) FOCADES will operate in the context of a regional environmental plan or agenda produced, monitored and updated by CCAD.

19. Funds raised by FOCADES will be managed as separate accounts if program needs and donor requirements prevent them from being managed in a consolidated account (Figure 3). Each separate account could have its own coordinating body, if so required, for the successful implementation of its specific program, and if sufficient funds are allocated for this purpose. Although not every account will have a coordinator and coordinating body, this option will increase FOCADES's transparency and ability to meet the needs of the users.



20. FOCADES will develop the project pipeline and will manage the grants awarded through national executing agencies. The FOCADES Board will select these agencies on a competitive basis to solicit and pre-screen proposals. National environmental funds, NGOs, private sector organizations and financial institutions are among the organizations eligible to play the role of national executing agencies.

21. The Global Account will be managed by a financial institution (the asset manager), with demonstrated relevant experience, to be selected through an international competitive bid. The asset manager will be responsible for the assets of the account and for ensuring a positive real rate of return on the investments. The projects funded with the proceeds

of the account investments will be selected from projects submitted by organizations in the region that meet the GEF criteria (i.e., global impact, incremental costs).

RATIONALE FOR GEF FINANCING

22. GEF support for the Global Account is justified because, consistent with the GEF Operational Strategy (February 1996), it will contribute to the sustainability of global environmental benefits by, *inter alia*, (a) promoting national policies that will contribute to the implementation of country- and regionally-driven initiatives that are within the scope of the GEF mandate; (b) strengthening institutions that are supportive of global environmental protection; (c) engaging civil society at all levels by providing the opportunities for participation in environmental management activities; (d) supporting projects that promote innovation, experimentation, demonstration and replicability; and (e) effectively complementing and enhancing traditional development funding from national, regional, and international sources for globally important environmental initiatives.

23. As a region, Central America has shown its commitment to sustainable development and sound environmental management. All the countries in the region have signed and ratified the Convention on Biological Diversity and the Framework Convention on Climate Change. Additionally, they have signed regional agreements and established the necessary institutional mechanisms for the implementation of regional initiatives for the conservation of biodiversity, the protection of forest and the application of climate change measures. The *Alianza* is but the latest of several regional initiatives seeking to address in a more comprehensive manner the sustainable development needs of Central America.

24. The true nature and depth of this commitment was clearly seen by a UNDP-supported exploratory mission to Central America, in June 1995. In their report, the mission leader concluded that “[after] the difficult decade of the eighties, environment is widely seen as an area on which the political will exists to make the needed regional approach toward the challenge of sustainable development.” The report went on to state that “[building] on [the] elements of a regional consensus perceived by the mission, the team outlined design features of a possible regional sustainable development fund for Central America.” Many of the recommendations made by the mission members, have been incorporated into the design of FOCADES and the proposed structure and functioning of the Global Account.

25. The leverage of the Global Account will be realized in three ways,

- (a) First, a stable source of funding encourages additional contributions from the governments in the region and other donors. Often these opportunities have not been fully developed in existing environmental endowments and trust funds, because fundraising success after the initial grant has been limited. By making matching funds a condition for the disbursement of funds for the sustainable financing phase, adequate encouragement is provided to FOCADES management to develop and implement an aggressive fundraising campaign. Furthermore, the fact that the sustainable financing phase follows a five-year direct financing phase, allows FOCADES management enough time to realize tangible results which are essential for any fundraising effort.
- (b) Second, a stable long-term source of funding is essential to promote the changes that the *Alianza* calls for. Although, in financial terms it may appear that allocating important sums of money for the establishment of endowments is an inefficient use of funds, experience has shown repeatedly that short term injections of funds have not had an effect proportional with the investments. The benefits of sustained funding are realized in the changes in attitude of people and institutions when they are liberated from the burden of relatively short project cycles.
- (c) Third, other GEF-supported initiatives, such as the Mesoamerican Biological Corridor would be well positioned to take advantage of the funds of the Global Account, as well as other sources and types of funding that the FOCADES would seek. The Corridor initiative will launch a number of programs that would require more funding than the GEF could or would be prepared to provide, but that would conceivably be eligible for funding under the Global Account. Although the Global Account will not focus solely on the Corridor initiative, this serves to illustrate the role that it can play ensuring the long-term viability of similar programs.

FINANCIAL SUSTAINABILITY

Recurrent Funding

26. The recurrent funding requirements of the Global Account will be met first by direct contributions from the GEF and other co-financing agencies during the direct financing phase of the project, and then from a fraction of the revenues generated by the investment of the Global Account’s principal during the sustainable financing phase. FOCADES, as the umbrella

organization, would require additional funds from other donors or from the governments in the region. Both of these options are being aggressively pursued by CCAD and CSDA. Negotiations with the Multilateral Investment Fund (MIF) have been realized and discussions are presently under way regarding the design of a MIF-supported account. Regular and timely contributions from the governments in the region are likely because of their stated commitment to sustainable development, and the fact that only those countries that are current with their contributions to CCAD and FOCADES would be eligible for funding under any of the FOCADES accounts.

OTHER DONORS: MULTILATERAL INVESTMENT FUND'S PRIVATE SECTOR SUPPORT ACCOUNT

27. Discussions have been held with the MIF of the Inter-American Development Bank to establish an account in FOCADES to support environmental initiatives by the private sector. The targeted amount of the MIF contribution is US\$ 25 million. The activities that will be funded under this account would complement those of the Global Account. The MIF account would support the efforts of small and medium sized enterprises (SME) to adopt environmentally friendly technologies and practices in their production processes. These enterprises require technical assistance and financing, and the MIF account would provide both. The technical assistance component would avail SMEs of information and consultant services at subsidized rates or at cost. This component is expected to be terminated once the funds allocated for this purpose are fully utilized. The credit component would provide SMEs with access to financing for the implementation of environmental solutions. This line of credit would be managed on market terms and is expected to generate enough revenues to be self-sustaining.

28. The approach to be used, the management arrangements, and the regional linkages are still under discussion and will not be defined until well into the design process. Likewise, the criteria of eligibility for both the projects and the enterprises will be clearly defined as the design process gets under way.

PARTICIPATION

29. With the signing of the *Alianza*, the Central American Heads of State have formalized their commitment to sustainable development and sound environmental management. The *Alianza* clearly calls for the establishment of a financing instrument to make this possible. The CCAD, with its broad regional representation has been the designated lead agency for the establishment of this financing instrument and is the principal promoter on behalf of the participating governments of the initiative to establish the Global Account. CCAD has received strong support from organizations like CSDA – which has solid ties to the region – to accomplish the creation of FOCADES and the establishment of the Global Account, the MIF's Private Sector Support Account, and others.

30. Civil society has also endorsed the concept of FOCADES and the establishment of the Global Account. This conclusion is a result of extensive consultations that have taken place at the regional and national level by CCAD and CSDA with the support from the Rockefeller Foundation, and more recently the Ford and MacArthur foundations. The consultation process started in December 1994 when representatives of Central American NGOs met in Costa Rica to sketch out the concept of what was to become FOCADES. In January 1995, NGO and government representatives met in Panama and decided on the methodology for the national level consultations. The following February and March a total of 178 interviews with government

agencies, NGOs, businesses, academic institutions and international development agencies (see Table 1) were conducted in all seven Central American countries.

31. Finally, in March 1996 the Central American national environmental funds, in their meeting in Guatemala stated their firm support for FOCADES and their willingness to participate in its design and implementation. In addition to the CSDA and CCAD-led consultations, during the UNDP/GEF mission of 20-29 June 1995, the mission members held meetings with many representatives of the public and private sectors, non-government organizations and regional and international development agencies (a complete list can be found in Annex B.), confirming the conclusions of the consultation process.

Table 1. Number and types of organizations that participated in the national consultations for the establishment of FOCADES.

	Belize	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Panama	Total
NGO	6	13	15	18	21	18	7	98
Government Agencies	2	2	1	11	3	5	2	26
Private Sector	3	5	1	1	5	5	0	20
Academic Institutions	0	4	2	10	0	2	0	18
Development Agencies	4	4	0	0	0	0	0	8
Financial Institutions	0	2	1	3	1	0	1	8
Total	15	30	20	43	30	30	10	178

32. The emphasis on broad consultation and participation is being institutionalized in FOCADES through the CCAD Regional Assembly. The Regional Assembly is composed of a wide range of institutions that meets annually to review CCAD's accomplishments and to advise on future initiatives. FOCADES, and through it the Global Account, will use this established and recognized forum to keep the designated representatives of civil society informed and to receive guidance and feedback on all aspects of its programs and operations. The fact that the Regional Assembly already exists and is being supported by CCAD, means that FOCADES can benefit from its input without increasing its administrative load.

LESSONS LEARNED

33. Trust funds and endowments to support environmental initiatives are not new. Many have been established using GEF grants. GEF has supported the following national or local level trust funds: Bhutan's Trust Fund for Environmental Conservation (1992); Uganda's Trust Fund for the Bwindi Impenetrable National Park & Mgahinga Gorilla National Park (1995); Peru's National Trust Fund for Protected Areas (1995); Brazil's Biodiversity Fund (1996). The GEF has also supported a regional trust fund (Foundation for Eastern Carpathian Biodiversity Conservation - 1994) and a private sector investment fund (Biodiversity Enterprise Fund for Latin America - 1996). Another private sector fund (Renewable Energy and Energy Efficiency Fund) was brought to the GEF Council for consideration in early 1996.

34. A thorough review of these experiences can be found in the World Bank's Environment Department Paper No. 011 (*Issues and Options in the Design and GEF Supported Trust Funds for Biodiversity Conservation*) published in April 1995, and a survey of National Environment Funds is presented in the report of the First Global Forum on Environmental Funds held in Bolivia in May 1994. The general assessment is that endowments have a role to play in environmental management. However, some cautionary notes are sounded, principally, that

endowments are not a solution to all financing problems. They should be used to finance activities that cannot readily generate revenues. Because most of the revenue-generating activities are nationally or locally based, regional initiatives are particularly well suited for funding by endowment-generated income. Additionally, a regional approach could be instrumental in overcoming barriers to otherwise cost-effective projects.

PROJECT FINANCING AND BUDGET

35. The design of the Global Account will have an estimated cost of US\$ 0.3 million (Table 2) and a duration of approximately 9 months. Annex A. contains a detailed work breakdown structure, timetable and budget by activities. The expenditure categories for this component include consultants (53%), support services (3%), travel and per diem (21%) and workshops (23%).

Table 2. Estimated cost of the design component of the direct financing phase

	Total
Design team	\$163,700
Project Coordinator	\$65,000
Natural Resource Specialist	\$23,700
Financial Analyst	\$25,600
Legal Advisor	\$12,900
Local Consultants	\$26,500
STAP reviewers	\$10,000
Support services	\$10,225
Administrative support	\$5,025
Translation services	\$5,200
Travel	\$63,400
International airfare	\$20,700
International per diem	\$31,520
NYC airfare	\$2,450
NYC per diem	\$2,730
Regional airfare	\$6,000
Workshops	\$70,000
Sectoral workshops	\$40,000
Regional workshops	\$30,000
Total Design Phase	\$307,325

36. The initial estimates are that FOCADES, with only the Global Account, will require annually US\$ 0.46 million to operate (Table 3). Approximately US\$ 0.23 million will be contributed annually by the GEF grant. This amount does not include fees and other costs associated with the management of assets, which will vary depending on the amount of the principal invested and the terms of the contract with the asset manager. A detailed operations and management budget for the first five years – the direct financing phase – will be prepared during the design of the Global Account.

Table 3. Indicative amounts and financing plan for the operations and management expenditures.

	Total a/	GEF	Other
Salaries	\$ 187,200	\$ 66,300	\$ 120,900
Executive Director	\$ 48,000	\$ -	\$ 48,000
Chief Technical Unit	\$ 36,000	\$ 36,000	\$ -
Chief Administrative Unit	\$ 36,000	\$ -	\$ 36,000
Secretary	\$ 18,000	\$ 9,000	\$ 9,000
Office Assistant	\$ 6,000	\$ 6,000	\$ -
Benefits	\$ 43,200	\$ 15,300	\$ 27,900
Office Expenses	\$ 87,000	\$ 49,000	\$ 38,000
Office Furniture	\$ 20,000	\$ 10,000	\$ 10,000
Office Equipment	\$ 25,000	\$ 12,000	\$ 13,000
Office Rent	\$ 36,000	\$ 24,000	\$ 12,000
Supplies	\$ 6,000	\$ 3,000	\$ 3,000
Travel and Per Diem	\$ 24,000	\$ 12,000	\$ 12,000
Asset Manager b/	\$ -	\$ -	\$ -
Other Expenditures	\$ 116,000	\$ 86,000	\$ 30,000
Printing and Publications	\$ 12,000	\$ 9,000	\$ 3,000
Consultants	\$ 40,000	\$ 40,000	\$ -
Phone and Postage	\$ 24,000	\$ 12,000	\$ 12,000
Audits	\$ 10,000	\$ 10,000	\$ -
Meetings and workshops	\$ 30,000	\$ 15,000	\$ 15,000
Contingencies	\$ 41,420	\$ 21,330	\$ 20,090
Total Operations Costs	\$ 455,620	\$ 234,630	\$ 220,990

a/ Totals may not add up due to rounding.

b/ Costs of asset management will be based on amount of principal.

37. The preliminary financial analysis suggests that approximately US\$ 0.5 million could be generated from the investment of the annual disbursements from the GEF during the direct financing phase (Table 4). Although this amount is not significant, it would provide a valuable opportunity for FOCADES to become familiar with the management of financial investments. The US\$ 4 million from the GEF, the US\$ 2 million match from other donors and/or from the governments in the region, and the income from the investments bring the total amount available for the direct financing phase to approximately US\$ 6.5 million. Keeping a cap on the operations and management expenditures of about US\$ 0.24 million annually (approximately US\$ 0.23 million for operation of the Global Account, as indicated in Table 3, and the balance for the asset manager) and taking into account the design costs of approximately US\$ 0.3 million, the amount available for the grants program will be close to US\$ 5 million (77% of the funding available) during the first five years of the project.

Table 4. Disbursement Schedule and Expenditure Plan for the Direct Financing Phase.

	Year 1	Year 2	Year 3	Year 4	Year 5	Total a/
GEF Contributions	\$ 800,000	\$ 800,000	\$ 800,000	\$ 800,000	\$ 800,000	\$ 4,000,000
<u>Other Contributions</u>	<u>\$ 400,000</u>	<u>\$ 400,000</u>	<u>\$ 400,000</u>	<u>\$ 400,000</u>	<u>\$ 400,000</u>	<u>\$ 2,000,000</u>
Total Contributions	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	\$ 6,000,000
Nominal Principal b/	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	\$ 1,200,000	
Projected Investment Income c/	\$ 90,000	\$ 90,000	\$ 90,000	\$ 90,000	\$ 90,000	\$ 450,000
Design of Regional Account	\$ 307,325					\$ 307,325
Operations and Management d/	\$ 240,000	\$ 240,000	\$ 240,000	\$ 240,000	\$ 240,000	\$ 1,200,000
<u>Grants Program e/</u>	<u>\$ 742,675</u>	<u>\$ 1,050,000</u>	<u>\$ 1,050,000</u>	<u>\$ 1,050,000</u>	<u>\$ 1,050,000</u>	<u>\$ 4,942,675</u>
Projected Expenditures	\$ 1,290,000	\$ 1,290,000	\$ 1,290,000	\$ 1,290,000	\$ 1,290,000	\$ 6,450,000
Balance on Principal e/	\$ -	\$ -	\$ -	\$ -	\$ -	
Rate of Principal Increase/Decrease	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

a/ Totals may not add up due to rounding

b/ Nominal principal at the beginning of year.

c/ Nominal income at the end of year. Assumes a rate of return of 7.5%.

d/ Projected operations and asset management expenses (including fees and other transactions costs) does not exceed 20% of the annual contributions.

e/ Balance on principal at the end of year.

Table 5. Preliminary Investment Analysis and Expenditure Plan for the Sustainable Financing Phase.

	Year 6	Year 7	Year 8	Year 9	Year 10	Total a/
GEF Contributions	\$ 11,000,000	\$ -	\$ -	\$ -	\$ -	\$ 11,000,000
<u>Other Contributions</u>	<u>\$ 11,000,000</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 11,000,000</u>
Total Contributions	\$ 22,000,000	\$ -	\$ -	\$ -	\$ -	\$ 22,000,000
Nominal Principal b/	\$ 22,000,000	\$ 22,600,000	\$ 23,221,500	\$ 23,860,091	\$ 24,516,244	
Projected Investment Income c/	\$ 1,650,000	\$ 1,695,000	\$ 1,741,613	\$ 1,789,507	\$ 1,838,718	\$ 8,714,838
Operations and Management d/	\$ 280,000	\$ 282,500	\$ 290,269	\$ 298,251	\$ 306,453	\$ 1,457,473
<u>Grants Program e/</u>	<u>\$ 770,000</u>	<u>\$ 791,000</u>	<u>\$ 812,753</u>	<u>\$ 835,103</u>	<u>\$ 858,069</u>	<u>\$ 4,066,924</u>
Projected Expenditures	\$ 1,050,000	\$ 1,073,500	\$ 1,103,021	\$ 1,133,354	\$ 1,164,522	\$ 5,524,397
Balance on Principal f/	\$ 22,600,000	\$ 23,221,500	\$ 23,860,091	\$ 24,516,244	\$ 25,190,440	
Rate of Principal Increase/Decrease	2.7%	2.8%	2.8%	2.7%	2.8%	

a/ Totals may not add up due to rounding

b/ Nominal principal at the beginning of year.

c/ Nominal income at the end of year. Assumes a rate of return of 7.5%.

d/ Projected operations and asset management expenses (including fees and other transactions costs) does not exceed 1.3% of principal.

e/ Grant fund expenditures estimated at 3.5% of principal.

f/ Balance on principal at the end of year.

38. It is expected that US\$ 11 million will be available from the GEF at the beginning of the sustainable financing phase. This amount will be matched with an additional US\$ 11 million from other donors and/or the governments in the region (Table 5). Using a conservative annual rate of return of 7.5%, the expected income from the investment of the principal during this phase (years 6-10 of the project) is approximately US\$ 8.7 million. Of this amount, 47% (US\$ 4.1 million) will be used for the grants program, 37% (US\$ 3.2 million) will be plowed back into the Global Account principal, and 16% (US\$ 1.5 million) will be used for operating the Global Account (approximately US\$ 1.2 million, based on the estimates in Table 3) and for the management of the assets (US\$ 0.3 million). The amount available for projects on an annual basis, if a ceiling of 3.5% of principal is imposed, will be between US\$ 0.8 and US\$ 0.9 million, about the same as during the direct financing phase. The same is expected for the Global

Account operations expenditures. The asset management costs, however, are expected to be higher because of the increased amount of the principal to be managed. The combined costs of operations and management is not likely to exceed 1.3% of the principal. From the investment revenues, the plowback to the corpus of the Global Account will be between 2.7% and 2.8%, sufficient to maintain its value in real terms.

PROJECT IMPLEMENTATION

39. *Criteria for Grant Awards.* The projects selected for funding under the Global Account will meet all the GEF criteria and in addition will be regional in scope or must be considered to be of regional relevance. National projects that could serve as demonstration for similar projects elsewhere will be eligible, provided that they establish partnerships with other national organizations or companies in other countries in the region interested in developing similar activities. Detailed grant award criteria will be developed at the time of the design of the Global Account.

40. *Selection of Asset Manager.* The asset manager of the Global Account will be selected through an international competitive bid. The terms of reference and selection procedures for the asset manager, as well as the investment objectives, guidelines and criteria to be used by the asset manager selected, will be prepared during the design of the project and will be approved by FOCADES's Board of Directors in consultation with the GEF Implementing Agency. Any changes in these investment objectives, guidelines and criteria within the five years of the project will require the no-objection of the GEF Implementing Agency.

41. *Procurement.* FOCADES will use public and competitive selection practices to recruit and hire its staff and consultants. The purchase of office and other equipment will be done using local or international bidding. During the five years of the project, annual procurement plans will be submitted to the GEF implementing agency as part of the annual operating plans. Grantees will be expected to use standard commercial procurement practices in the execution of the grants awarded.

42. *Audits.* Independent auditors will be selected in consultation with the GEF Implementing Agency to conduct annual audits of the Global Account, and if necessary of FOCADES in general. These audits will be conducted according to generally accepted accounting principles and will focus on overall financial management, control and effectiveness in the management of the Global Account funds.

43. *Annual Operating Plans.* Annual operating plans will be submitted by FOCADES to the GEF Implementing Agency. These plans will include the specific objectives, activities, expected outputs, monitorable performance indicators, detailed budgets and procurement plans. The content and format for these plans will be developed during the design of the Global Account.

44. *Supervision, Monitoring and Evaluation.* The Implementing Agency will supervise this project semi-annually during the five years of the direct financing phase. A mid-term evaluation will be conducted during the direct financing phase. At that time any major adjustments to the management of the account, including the investment criteria, the grant selection process, the project eligibility criteria, the operational procedures, the disbursement schedules, the impact and performance indicators, and other project implementation parameters will be reviewed and if necessary revised. At the conclusion of the direct financing phase, an in-depth evaluation of the performance of the grants program and the efficiency of the operations and management of

FOCADES and the Global Account will be done. This evaluation, along with evidence that matching funds have been obtained, will be used to determine whether the project is to proceed to the sustainable financing phase, or is to be terminated. During the five years of the sustainable financing phase, the project will be supervised semiannually, and in-depth evaluations conducted mid way through the implementation of this phase and at the conclusion of the project period.

INCREMENTAL COSTS

45. The Global Account will only finance the incremental costs of activities designed to generate global benefits in the GEF operational focal areas. Baseline funding will be available through the sustainable development initiatives to be financed by FOCADES and/or other sources. During project design guidelines for the calculation of incremental and baseline costs will be provided to facilitate their future estimation on a project by project basis. These guidelines will be consistent with GEF established criteria and will be tested during the preparation of the pilot projects.

ISSUES, ACTIONS AND RISKS

46. The formal establishment of FOCADES is the most critical issue for this project. For this reason, no funding will be available for projects until FOCADES has been properly staffed and is operational. The risk that FOCADES's final design characteristics are not suitable to support the Global Account and/or that there are questions about the qualifications of the staff being hired is being reduced by the close working relationship between UNDP, CCAD, and CSDA in the final design and establishment of FOCADES. Close collaboration is also expected in the recruitment of FOCADES staff.

47. **The selection of the asset manager** is another critical issue that will be addressed during the design of the Global Account. The terms of reference and selection procedures will be discussed thoroughly with regional representatives, UNDP, CCAD, and CSDA. Consensus on this aspect of the project is fundamental.

48. Although the consultation process has been extensive and exhaustive, close attention will be paid to the selection of national implementing agencies. This issue will be addressed during the design of the Global Account. The design process includes workshops aimed at dealing with more technical aspects of project selection and management, which include the role of national level organizations, and issues of costs in project administration and management.

49. There is the risk that matching funds will not be obtained at the times or in the amounts required. In this regard, the most critical time will be the direct financing phase because FOCADES would not have had the opportunity to develop a project pipeline or a track record of successful project selection and implementation. This is the reason for the rather modest funding requirement for the first five years of the project. The major funding commitment will be for the sustainable financing phase, however, the five years of experience gained during the previous phase would allow FOCADES the time and the credibility to raise the needed funds. If FOCADES fails to perform to agreed standards or is unable to raise matching funds, the GEF would have the option of canceling the project with minimal exposure after the conclusion of the direct financing phase.

TECHNICAL REVIEW

(see Attachment)

ANNEXES AVAILABLE UPON REQUEST

- A. Design of the Account for the Global Environment
- B. Description of FOCADES
- C. Persons and Institutions Contacted by the UNDP/ GEF Mission to Central America
(20-29 June 1995)