

*Options for the operationalization of a loan scheme to facilitate CDM project development in countries with fewer than 10 registered CDM projects*

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# Background

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The 2/CMP5 decision: Para 49-51

- a) Executive Board requested to recommend modalities and procedures of a loan scheme to CMP 6
- b) Use interest accrued on resources of the Trust Fund for the CDM
- c) To extend Loans in countries with fewer than 10 registered CDM activities
- d) Loan to cover defined CDM development transaction costs: PDD, Validation, 1<sup>st</sup> Verification
- e) Repayment starting from first issuance of CERs



# Introduction

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- **EB 54 in May 2010** *“requested the secretariat to work further on developing modalities and procedures for operationalization of such a loan scheme based on a management model that has more outsourced functions and with minimum involvement of the secretariat for consideration by the Board at its next meeting”*
  - **Purpose of this presentation:**
    - a) present new options involving a much higher degree of outsourcing for loan scheme administration
    - b) further elaborate on the proposed eligibility criteria and loan terms and conditions
    - c) summarize the feed-back received from DNAs
    - d) highlight outcome of legal and administrative consultations
    - e) request EB to make decision on which variant of loan management model (see Conclusion)
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# Reminder: Loan scheme 4 key functions

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**Available resources: Start-up: ca U\$3mln** – expected U\$1-1.5 ml subsequent years

- **4 key functions need** to be performed in a loan scheme:

**a) F1: Project origination**

- Sourcing and screening

**b) F2: Project appraisal**

- Is the project feasible and financially viable?
- Does it meet CDM eligibility criteria?

**c) F3: Flows of funds**

- Sign the loan agreement
- Disburse and collect repayments

**d) F4: Loan administration**

- Manage portfolio
- Troubleshooting



# New proposal: three variants

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	Hybrid model (EB 54)	Variant 1	Variant 2	Variant 3
Origination F1	PI	PI	PI	PI
Appraisal F2	PI and Sec.	PI	PI but Sec. participates in Eval. Com	PI
Disbursing F3	Sec.	Sec	PI	PI
Loan administration F4	PI and Sec.	PI	PI	PI

**Key:** PI: Partner Institution – Sec.: Secretariat

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# Oversight by the secretariat (I)

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Contract between the secretariat and Partner Institution will cover **5 main areas** to ensure oversight role of secretariat:

To be tailored to the variant (v1, v2, v3) selected.

- 1. Transfer of funds to the Partner Institution (only v2 & v3)**
- 2. Business Plan, Reporting, Budget and Financial Account.**

The Partner Institution would prepare and submit for review by the secretariat:

- a) An annual Business Plan
- b) An annual Budget
- c) Quarterly reports
- d) An annual Financial Statement



# Oversight by the secretariat (II)

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- 3. Procedures for loan application submission and processing, including templates** will be defined by the Partner Institution in line with the principles set out in modalities and procedures developed, and subject to approval by the secretariat.
- 4. Interim performance evaluation of the loan scheme, by an independent expert.** Could take place at the end of the first year, so that adjustments can be made to the scheme as necessary.
- 5. Right for the secretariat to terminate the contract** in case of under-performance (e.g. fewer than x loans signed in a given period), or breach of contract (e.g. in case of misconduct).



# Oversight by the secretariat (III)

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## Steering Committee

- Proposed that performance of loan scheme be reviewed by a **Steering Committee** – to convene at least once a year, or more frequently, if at least two members of the Steering Committee so request.
- **Steering Committee** to have the right to summon the Partner Institution, if there are concerns about the performance or issues that require such meeting.
- **Membership of the steering committee** to be determined once it is clear which variant of the outsourced management model will be in place.



# Partner Institution

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- **Profile – requirements**

- a) Expertise in performing three (v1) or all (v2, v3) four functions.
- b) Track record in managing similar loan schemes in developing countries.
- c) Charging a reasonable cost for its services.
- d) Single firm or consortium, from public and/or private sector
- e) Ideally one Partner Institution recommended

- **Remuneration**

- a) 20% is a rough estimated cap on the overall administrative cost
- b) Equivalent to \$320,000 pa on average, for an hypothetical volume of resources of \$8mln in the next five years (\$3mln+5x1mln)

- **Selection process**

- a) Competitive bidding advisable and potential UN agencies as per existing rules and procedures



# Project eligibility criteria (I)

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- **Countries**

- a) Only those that have a DNA
- b) Proposed not to set country-related criteria other than UN security phases

- **Projects and project proponents**

- a) Integrity. Only information in public domain will be utilized.
- b) Capacity of project owner to implement and operate the project
- c) Commercially viable and available technology
- d) Financial viability
- e) Potential of securing investment finance
- f) Potential of project being completed and commissioned
- g) Minimum CDM track record of project owner or its CDM advisor, and willingness (of the latter) to share in development risk (payment tied to milestones.)



# Project eligibility criteria (II)

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- **Minimum emission reduction potential over crediting period**  
[100ktCO<sub>2</sub>]
- **CDM process**
- Potential of meeting CDM eligibility criteria (EB is the ultimate judge...)
- **Eligible CDM transactions**
- PoAs included
- **Eligible costs**
- PDD, validation, first verification
- Consider inclusion of methodology development and other, non-CDM but essential development costs in light of interim evaluation



# Loan terms and conditions (I)

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- **Borrower:** the project owner
- **Duration:** linked to 1<sup>st</sup> issuance of CERs.
- **Interest rate:** zero.
- **Fees:** zero. Alternatively lender could charge a **one-time fee of 1% (with min. of \$1,000)** to discourage non-serious applications
- **Disbursement** upon milestones (e.g. validation) and directly to CDM advisor/DOE as the case may be.
- **Repayment**
  - a) Normally one instalment, in first issuance year, to accelerate reflows
  - b) Option given to project owners to repay in cash or through monetization of CERs
  - c) Consider in the latter case whether loan scheme could take CDM market risk



## Loan terms and conditions (II)

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- **Security/collateral:** none other than issued CERs – (pending account and distribution of issued CERs when fees are paid).
- For projects that are not registered but are built and operated, the loan would remain due.
- **Loan amount:** Maximum would be lesser of **[\$150,000]** or **[90]% of eligible costs**. Exceptions possible if new methodology development costs eligible - **[\$50,000]**
- Require some degree of **competition** between service providers (CDM advisor, DOE)
- **Reporting** on a six-monthly basis to lender



# Feedback from consultation with DNAs (I)

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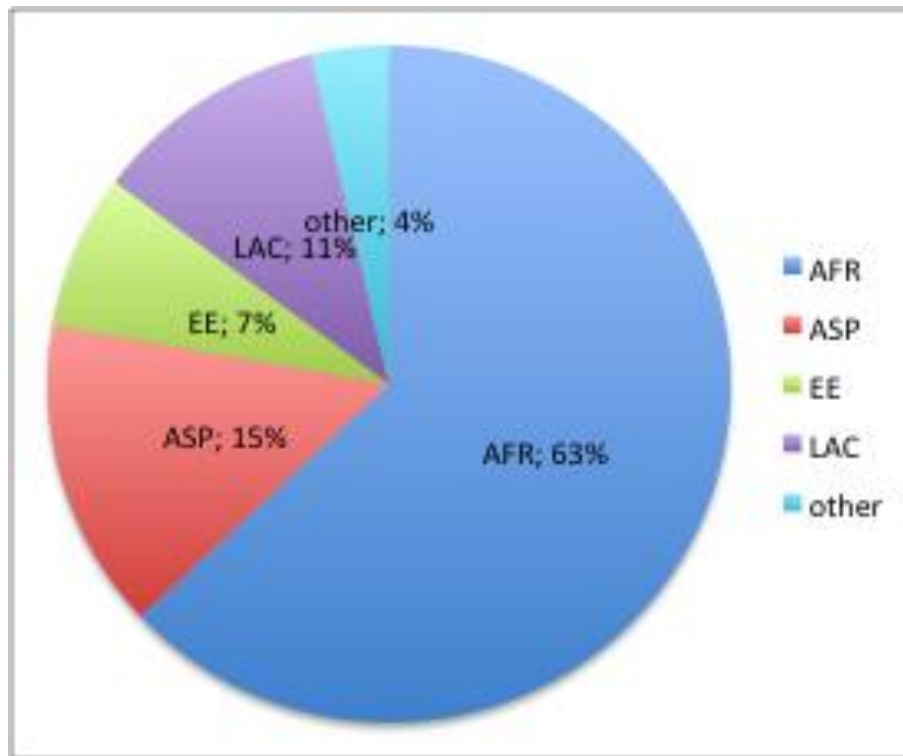
- Questionnaire was sent to 129 DNAs
  - 6 questions:
    1. Would a loan scheme facilitate the development of CDM projects in your country?
    2. Should loan eligibility be restricted to certain types of projects, methodologies?
    3. Do you think DNAs should play a role in the loan scheme?
    4. Do you agree with the proposed loan terms ?
    5. Which institution would be best qualified and positioned to perform the functions of project selection and appraisal?
    6. Which recommendations would you make to ensure success of loan scheme?
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## Feedback from consultation with DNAs (II)

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- 27 respondents; ca 20% of the targeted group
- Geographical distribution shows Africa over- and Asia and Pacific below-represented



# Feedback from consultation with DNAs (III)

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- **Unanimous support** for loan scheme -**100%**
- Split opinions (50/50) on whether to restrict access loan scheme to certain types of projects/methodologies
- **No clear consensus on which projects to support**, although small-scale, EE and RE got large backing
- **Majority support for DNA involvement - 96%**: provide information, project selection and assessment, majority indicating DNAs to have key role in project selection
- **Majority endorsement of key proposed terms and conditions - 96%** e.g. concessional, size, repayment tied to issuance of CERs
- **No clear consensus on who should manage the scheme**: significant proportion indicating - to DNAs (10) with at least part of that role or to EB (4)
- **Strong demand for simple procedures**



# Legal considerations (I)

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- **Can the interest earned by CDM Trust Fund be used for the loan-scheme?**
  - a) Paragraph 8 of Article 12 of the Kyoto Protocol (KP), the CMP “indicates: ensure *that a share of proceeds from certified project activities is used to cover administrative expenses as well as to assist developing country Parties ....to meet the costs of adaptation.*” - not clear whether the proceeds could be legally used for loan scheme. Parties may need to clarify their understanding of this provision of KP – require CMP decision
  - b) With respect to whether interest income can be considered distinct from the share of proceeds, the answer appears to be no. [Legal to expand if required]
- **Does the secretariat have the mandate to oversee management of such a loan scheme?**
  - a) Article 8.2 (f) of the Convention clearly specifies that the secretariat functions shall be (inter alia)... “*to enter...into such administrative and contractual arrangements as may be required for the effective discharge of its functions*”.
  - b) In addition, 8.2(g) states “*...and such other functions as may be determined by the COP*”.  
Secretariat would require a clear mandate from the CMP to oversee management of such a loan



# Legal considerations (II)

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**How would the secretariat address potential risks associated with overseeing management of such loan scheme (e.g. misappropriation or misuse of funds, recovering the funds if no project is ever submitted, etc?)**

- a) Secretariat would address potential risks associated with overseeing the management of such a loan scheme through adequate contractual arrangements with the entity outsourced to manage loan scheme
  
- b) Selection of the outsourced entity to manage the fund will go through procurement process, unless it is a UN agency – MOU will apply



# Conclusion

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## The Board is requested to:

- Indicate which **variant** of the outsourced management model it endorses;
- Indicate whether it agrees with the **proposed eligibility criteria and loan terms and conditions**;
- Indicate whether it agrees to charging an **upfront fee** to borrowers, and the maximum amount of this fee;
- Provide any **other guidance** to the secretariat as may be necessary to further develop the modalities and procedures of loan scheme



