CLIMATE INVESTMENT FUNDS

FIP/SC.4/4/Rev.2~~1~~
June 24, 2010

Meeting of the FIP Sub-Committee
Washington, D.C.
June 24, 2010

FIP: INVESTMENT CRITERIA AND FINANCING MODALITIES

(REVISED with Track Changes)

Proposed Decision by FIP Sub-Committee

The FIP Sub-Committee reviewed document FIP/SC.4/4/Rev.2~~1~~, *FIP Investment Criteria and Financing Modalities*, and approves the procedures and modalities as a basis for FIP investments.

Note: This paper is a revised version of document FIP/SC.3/4*/Rev.1*, *FIP Investment Criteria and Financing Modalities*, which was circulated to the FIP Sub-Committee for approval ~~by a decision-by-mail~~on June 24, 2010. All changes made to the document subsequent to its previous circulation to the FIP Sub-Committee are ~~marked in tracked changes (red)~~highlighted for easier reading.

I. Purpose of Document

1. This document details the investment criteria to guide the programming of FIP investments in selected pilots based on priority assessments and the financing modalities for those investments. The basis for these guidelines is the FIP Design Document, specifically chapter VI. *Criteria for FIP Investment Strategies, Programs and Projects* and Annex II *Initial Guidance on How Transformational Change will be Defined and Assessed under the Forest Investment Program*. It should be considered alongside the *FIP Operational Guidelines* which detail the more operational aspects of FIP programming at the country level.

2. The document also defines the financing products that the multilateral development banks (MDBs) may deploy using FIP resources, the terms for such financing, including fees for MDB project development and supervision costs, and standard FIP co-financing conditions and review procedures.

3. The FIP will support innovative international financing for forests. This will include moving away from a traditional project-based aid approach to support national REDD+ strategies and programs (or equivalents) through a programmatic approach. In this context, the document identifies the role of the public and private sector in FIP investments. Forest and forest landscape management, including the interaction with other sectors, is capital intensive and requires long-term investments. It also involves a concerted effort by the various sources of finance – public and private, be it national or international. Both are not only a potential source of co-finance for leveraging FIP resources but also resources for transformational change in the way they approach the management of forest resources or of natural resources affecting forests.

4. The FIP may also support innovative international financing for forest climate. This ~~would~~ may include: a) moving away from traditional project-based aid approach to support national REDD+ strategies and programs (or equivalents) through a programmatic approach; b) providing results-based incentives~~, e.g. through performance-based payments based on multi-year contracts for reduced forest-based emissions~~; c) concessional financing ~~to the private sector~~ for forest rehabilitation and sustainable forest management; and d) grant financing to protect existing stocks of forest carbon. It is proposed that these financing modalities be reviewed by the FIP Sub-Committee on the basis of actual experience in their application. Furthermore, the MDBs will prepare a report for consideration by the Sub-Committee within 24 months of start-up to propose, if necessary, any changes that may serve to enhance the effectiveness of the FIP.

Formatted: Not Highlight

~~II. Role of Public and Private Sector in FIP Investments~~

~~5. The public sector plays an important role in the forest sector and those sectors affecting forests as it fulfils three main functions: (a) establishing a policy, regulatory and~~

~~institutional environment that can support private-sector and public investments; (b) stimulating private-sector investment in sustainable forest and forest landscape management (SFM), re-/afforestation and conservation through grants, tax-relief and subsidized loans; and (c) providing the main source of finance for forestry activities that produce social and environmental benefits.~~

~~6. Private sector investments in forest and natural resource operations as well as forest-based industries dwarf the combined flows from multilateral development banks, bilateral agencies, civil society organizations, and charities. Currently, it is estimated that the private sector accounts for about 80-90 percent of financing for forestry, with small and medium scale businesses forming the overwhelming majority of forest-related enterprises in developing countries.~~

~~7. The FIP's role in initiating transformational changes in the forest and other sectors affecting forest ecosystems is primarily catalytic in terms of shifting countries from the business-as-usual of how forests are managed to a sustainable low-carbon growth path with multiple co-benefits. It is crucial that FIP investments directly respond to country priorities identified in REDD+ strategies and action plans (or equivalents). Forest management is capital intensive and a long-term investment. Mechanisms channeling finance for forestry and related sectors have diversified considerably and become more innovative over the past few years by introducing concepts such as payment for environmental services, performance-based payments or carbon credits linked to the emerging carbon market.~~

~~8. Most barriers to sustainable forest management are linked to a non-conducive enabling environment manifested in inefficient and/or poorly enforced policy, legal and institutional arrangements. The short-term economic gains from unsustainable forest management practices and conversions of forest land to other land uses currently outweigh the investment returns from sustainable practices. Incentives supporting a long-term sustainable forest management regime need to be put in place. These enabling activities are in the domain of the public sector.~~

~~9. Support from the FIP can also help to reduce investment risks and market barriers for responsible private operators in regions or countries where national enforcement capacity is weak by addressing forest governance, transparency, land tenure and complex social and environmental challenges which are beyond the capacity or appropriate role of such private operators. There are also significant opportunities for the FIP to help leverage environmentally and socially sustainable private sector investment in climate relevant operations, such as afforestation, reforestation, and restoration of degraded landscapes, conservation and sustainable natural forest management. FIP funding can be instrumental in supporting sound agro-business and bio-energy investments which are climate friendly and socially acceptable by providing incentives for stabilizing forest margins, supporting best practice examples, and by supporting mutually beneficial company supplier partnerships with forest smallholders. In addition, FIP investment to the private sector can promote sustainable market chains for wood and non-wood products; support the country-wide establishment and implementation of a certification~~

~~scheme for wood and non-wood products; support country and region-specific environmental management and land use planning promote payment schemes for ecosystem services for create viable partnerships between the private sector and local communities such as eco-tourism in forest protected areas; and support forest-relevant processing industries with low-carbon technologies.~~

~~10.~~

~~III.~~II. FIP Investment Criteria

~~11.~~5. Financing from the FIP will be provided on the basis of an Investment Strategy, developed under the leadership of the recipient country in coordination with the MDBs, for the use of FIP resources in the country through a joint MDB program. The Investment Strategy should highlight how it is embedded in national development plans and REDD+ strategies and action plans or any equivalent framework that include low carbon objectives from natural resources management. The Investment Strategy will include a potential project pipeline and associated notional resources envelope.

~~12.~~6. Country requests for FIP investments will have to make the case for initiating transformational change by highlighting activities that are additional and provide an alternative to the business-as-usual scenario and result in sector- and cross-sector wide impact related to GHG savings. Investment Strategies[1] as well as projects and programs supported under it would need to describe what and how activities will result in significantly reduced GHG emissions or enhanced carbon sequestration that would not have occurred or are significantly enhanced had it not been for the FIP investment.

~~13.~~7. The following criteria are based on the initial guidance provided in the *FIP Design Document* as to what constitutes transformational change in the context of FIP and the need for proof of going beyond business-as-usual. The criteria are complemented by more detailed information on ways to review a proposed investment strategy, program or project. These criteria are consistent with the FIP Design Document (see annex A):

(a) Climate change mitigation potential.
(b) Demonstration potential at scale.
(c) Cost-effectiveness.
(d) Implementation potential.
(e) Integrating sustainable development (co-benefits).
(f) Safeguards.

~~14.~~8. The FIP will focus on high abatement opportunities at the country level and address the country-specific key barriers to address REDD+. It is understood that not all criteria will be applicable to each project and program. Nevertheless, all criteria need to be addressed in a program or project proposal and applicability should be discussed. A core set of indicators will be applied to FIP investments which are consistent with the FIP results framework[2].

[1] See: FIP/SC.3/3, *FIP Operational Guidelines*
[2] The proposed FIP logical model will be reviewed during the fourth FIP Sub-Committee meeting in June 2010. Based on the logical framework, the FIP results framework will be developed.

***Climate change mitigation potential*.**

~~15.~~9. The FIP was established to "catalyze policies and measures … to facilitate the reduction of deforestation and of forest degradation ..., leading to emission reductions and the protection of forest carbon stocks" (paragraph 7, *FIP Design Document*). Each proposal for FIP funding will provide an assessment of the direct GHG savings over the lifetime of the proposed project/program. Emission reductions and avoidance will be calculated by subtracting projected lifetime emissions of the FIP-financed project from the projected lifetime emissions of the business-as-usual using a clearly-articulated reference level (baseline)[3].

~~16.~~10. As noted in the FIP Design Document, "[t]he FIP would not in itself provide the incentives presently necessary to significantly reduce forest related GHG emissions, but would enable pilot countries to leverage such incentives if established under a UNFCCC forest mechanism"[4]. This implies that certain activities financed by the FIP may not result in immediate emission reductions, but may rather serve to enable countries to leverage REDD+ incentives in the future. For this type of projects and programs, this criterion would have limited applicability.

Demonstration Potential at Scale

~~17.~~11. Investment Strategies, programs and projects should support replicable pilot programs in order to demonstrate how to scale up public, private and other resources and activities so as to achieve transformational change. Rather than favoring FIP investments that are themselves necessarily geographically large, FIP will support investments that, if scaled-up to target a particular activity, region, or forest type, have significant scope for climate change mitigation potential.

~~18.~~12. FIP investments should address REDD+ priorities as presented in national REDD+ strategies or action plans (or equivalents). This indicator will help ensure that FIP investments address the main drivers of deforestation and forest degradation.

~~19.~~13. The demonstration of scale of project and program proposals might be based on information on the area targeted by FIP investments. Each proposal will provide information on the direct or indirect contribution of the FIP investment to the forest and forest landscape area conserved, restored, sustainably managed, protected, or afforested/reforested.

~~20.~~14. In addition, in the geographic area of the proposed investment, information needs to be provided on what are the emissions that have been occurring historically (the reference level) or might occur (business-as-usual scenario), which could be mitigated immediately as part of the Investment Strategy. It needs to be discussed how the scale of

[3] See: *2006 IPCC Guidelines for National Greenhouse Gas Inventories* (http://www.ipcc-nggip.iges.or.jp/public/2006gl/index.html)
[4] Paragraph 7, *FIP Design Document*

emissions in the targeted area compare to other areas where deforestation or forest degradation is occurring, and how replicable lessons from this area would be for other parts of the country. The Investment Strategy should also explain how permanence and leakage risks have been addressed.

~~21.~~15. Each project and program should include information on relevant existing good practices which have potential to be scaled up through the FIP investment.

Cost-effectiveness

~~22.~~16. Each project and program, where appropriate, will include a calculation of the costs per ton of CO2eq reduced or avoided.

~~23.~~17. FIP investments should leverage additional financial resources, including from the private sector where feasible. It is expected that both public and private sector institutions (including civil society institutions) will be involved in the development and implementation of an Investment Strategy and related projects and programs. Projects and programs should provide information on the public and private sector institutions potentially involved in the implementation of the Investment Strategy, projects and programs, including the anticipated ratio of FIP co-financing to leveraged additional financial resources. The ratio of private to FIP funds actually invested should reflect substantial leverage (target at least 4:1), in circumstances where private sector investment is relevant[5].

~~24.~~18. FIP investment strategies, programs and projects should catalyze self-sustaining economically viable models for REDD+ at scale without the need for continuing subsidies. Each project and program should include information on how achieved results will be sustained after completion of the FIP investment, including measures that generate positive incentives and reverse problematic incentives across sectors and lead to lasting change.

~~25.~~19. FIP should promote ~~institutional~~ coordination among relevant institutions at the country-level with respect to implementing and financing proposed investments. Effective coordination should transparently monitor and record data about financing received, transferred and spent, with clear lines of accountability. Accountability can be promoted by linking this data to the specific objectives, geographic area, and expected emission reductions of proposed activities, and by making such data publicly available.

Implementation Potential

~~26.~~20. FIP investment proposals will be reviewed for dimensions closely related to successful implementation, consistent with MDB standards:

---

5 Annex II, *FIP Design Document*

~~27.~~21. Public policies and institutions should support REDD+ efforts, demonstrated through:

(a) *Country and sector strategies*: Key policy, institutional and other issues relevant to achievement of REDD+ objectives should be addressed. FIP investment strategies, programs and projects should capitalize on the lessons learned concerning inclusive and effective improvements in governance and enhancement of law enforcement in other environmental sectors. FIP investments should support such improvements as an integral part of necessary measures and policies to ensure forest related climate change outcomes. Forest governance criteria and indicators should be integrated into project and program design as well as into performance assessments to ensure measurable outcomes.

(b) *Institutional and implementation arrangements*: Institutions responsible for implementation should be identified, together with a description of their capacity to support REDD+ objectives. Required capacity building should be identified and funded.

(c) *Sustainability*: Evidence of commitment to, and ownership of, project and relevant policies, as well as arrangements for long term continuation of initiated activities, including conflict resolution measures.

(d) *Effective stakeholder participation and decision making*: FIP investment strategies should describe an inclusive process for stakeholder engagement in the design, implementation, monitoring and evaluation of FIP programs and projects. Such process may include the establishment of a conflict resolution mechanism where appropriate.

~~28.~~22. FIP co-financed investment proposals should confirm that the investment falls within the REDD+ national strategies or action plans (or equivalents), including, where appropriate, REDD+ readiness plans. In this context, an Investment Strategy should also provide information on the status of the enabling environment for REDD+ (public policy, regulatory framework and institutions), projects and programs should describe how they will address identified barriers and related needs, including the creation of a cross-sectoral coordination mechanisms to deliver on REDD+ and to integrate the role of forests into national sustainable development strategies.

~~29.~~23. A key objective of the FIP is to mobilize resources at scale for the implementation of REDD+ activities. Investment opportunities should be prioritized on the basis of the co-financing leveraged from domestic public and private sector sources, including carbon finance, as well as bilateral and multilateral development partners.

~~30.~~24. Consistent with MDB policies and procedures, projects and programs will present risks associated with the proposed FIP investment and proposed mitigation measures. In this context, each project and program should also include information on the process for developing and implementing activities in terms of participation, transparency, coordination, capacity and accountability.

Integrating sustainable development (co-benefits)

~~31.~~25. A key objective of the FIP is to contribute to the livelihoods and human development of forest dependent populations, including indigenous peoples and local communities, and to sustain biodiversity and ecosystem services and enhance the adaptive capacity of forest ecosystems and forest dependent communities to the impacts of climate change.

~~32.~~26. The potential development impacts of projects and programs will be assessed consistent with standard MDB appraisal criteria. To monitor and evaluate the contribution of projects and programs to sustainable development, a core set of indicators will be applied to FIP investments which are consistent with the FIP results framework.

~~33.~~27. Investment strategies, projects and programs will need to demonstrate economic, social and environmental impacts from FIP investments and demonstrate consistency with relevant national strategies and plans. Proposals should set out how FIP investment will catalyze, support and measure and monitor the delivery of, *inter alia*, the following (as appropriate):

a) Demonstrable improvement in social and economic well-being of forest dependent communities, including poverty reduction, job generation, wealth creation, equitable benefit sharing, and acknowledgement of the rights and role of indigenous peoples and local communities.
b) Protection of biodiversity.
c) Strengthened resilience of ecosystems, with associated ecosystem services.

~~34.~~28. The Investment Strategy should describe the status of planning and implementation for activities under the *Dedicated Grant Mechanism for Indigenous Peoples and Local Communities* and how coordination between the Mechanism and the Strategy, together with its associated projects and programs has been and will be ensured.

Safeguards

~~35.~~29. Consistent with its objectives, the FIP should safeguard natural forests and should not support the conversion, deforestation or degradation of such forests, *inter alia*, through industrial logging, conversion of natural forests to tree plantations or other large-scale agricultural conversion. In particular, the FIP should safeguard high conservation value forests (paragraph 16(g), *FIP Design Document*).

~~36.~~30. Agenda 21 adopted at the United Nations Conference on Environment and Development (UNCED) recognized the need to strengthen forest-related national institutions, to enhance the scope and effectiveness of activities of the management, conservation and sustainable development of forests, and to effectively ensure the sustainable utilization and production of forests' goods and services in both developed and developing countries. The Millennium Development Goals, the Johannesburg Declaration on Sustainable Development and the Plan of Implementation of the World Summit on Sustainable Development all recognized the critical role of the sustainable management of forests. It is also recognized that the United Nations General Assembly has adopted the United Nations Declaration on the Rights of Indigenous Peoples. A significant number of international and regional agreements, organizations and agencies are at the core of the forest financing architecture, with programs and projects implemented at the sub-national, national, regional and international levels. Many such programs and projects will contribute to the context and foundation for REDD initiatives by facilitating the readiness of countries to participate in REDD, including their ability to address the drivers of deforestation and forest degradation and to enhance the sustainable management of forests. Key organizations include Multilateral Development Banks (MDBs), UN, members of the Collaborative Partnership on Forests (CPF), bilateral aid programs, international NGOs, philanthropic organizations and the private sector (paragraph 6, *FIP Design Document*).

~~37.~~31. Consistent with relevant international instruments, obligations and domestic laws, FIP investment strategies, programs and projects should be designed and implemented under a process of public consultation, with full and effective participation of all relevant stakeholders on matters that affect their distinctive rights, including in particular groups that historically have tended to be marginalized such as indigenous peoples, local communities and women. FIP financed activities should, moreover, be consistent with, and/or complement, national sustainable development plans and be based upon broad community support and effective collaboration between indigenous peoples and local communities, government ministries, private sector and financial institutions in planning and implementing investment strategies. FIP should also seek to engage other major stakeholders such as major groups identified by Agenda 21 (paragraph 16(d), *FIP Design Document*).

~~38.~~32. The guidelines presented in Annex III to the *FIP Design Document* should be followed to facilitate the full and effective participation of indigenous peoples and local communities likely to be affected by a proposed strategy, program or project in a process of public consultation.

~~39.~~33. FIP financed activities should, moreover, be consistent with, and/or complement, national sustainable development plans and be based upon broad community support and effective participation of indigenous peoples and local communities, government ministries, private sector and financial institutions in planning and implementing investment strategies.

~~40.~~34. MDBs should provide detailed information on safeguards to be applied to each project and program~~-~~, and confirm application of the guidelines in Annex III of the *FIP Design Document* and consistency with relevant decisions for REDD+ under the UNFCCC once decided (see Annex B).

Additional Project-specific Criteria

~~41.~~35. In addition to the above criteria that are focused more on assessing proposed FIP investments against their potential for initiating transformational impact, additional criteria may clarify and help guide the design of FIP public and private sector programs and projects. Public and private sector projects may be assessed against how they will mitigate market distortions.

~~42.~~36. In addition, private sector projects may be assessed how effective the will utilize concessional finance.

~~43.~~37. Private sector program proposals will follow the template provided in Annex C~~B~~

IV. Financing Modalities

~~44.~~38. A number of financing products (grants, concessional finance, guarantees and equity) will be available under the FIP, all of which will include a grant element tailored to the additional cost of the investment, or the risk premium required, in order to make the investment viable. These products could include concessional finance in the form of grants, and concessional loans with a significant grant element, guarantees[6] as well as equity, or a combination of these. The grant element will be tailored to provide the appropriate incentive to facilitate the scaled up deployment of forestry investments or investments positively impacting forest ecosystems. To incentivize transformational change, grants and loans may be disbursed subject to achieved results as outlined in the Investment Strategy. All FIP financing will be denominated in US Dollars.

~~45.~~39. It will be important to ensure that concessional terms do not displace investments that might have taken place anyway using commercial or standard MDB borrowing or guarantees, or carbon finance. Concessional forms of finance need to be designed to minimize market distortions and potential disincentives to long-run private investment.

~~46.~~40. Under the FIP, resources may be blended with will be its ability to provide the MDBs with the instruments to blend FIP resources with other sources of financing. When FIP resources are blended, terms may be ~~to~~ tailored ~~terms~~ to a target level of concessionality, which will vary depending on project-specific factors. Concessional forms of finance could help unlock demand for the financing of such projects and programs. Blending FIP resources and multilateral development bank loans could augment the volume of financing available, and better tailor concessionality to needs, with the degree of concessionality calibrated to achieve transformative investments which would otherwise not proceed.

~~47.~~41. It is proposed that the FIP provide the multilateral development banks (MDBs) with a menu of ~~blending~~ financing options to accommodate different needs of client countries and program interventions. The FIP could co-finance MDB non-concessional loans or provide additional financing of new components within ongoing investment

Formatted: Font color: Black

[6] The actual term of the debt would be determined by the lenders who are expected to take into account the guarantee while determining the debt terms.

lending operations, on concessional terms. Resources from the FIP would thereby increase the concessionality of the overall financing for the project or program. The development of such co-financing arrangements can be done in a relatively low-cost manner when fully embedded in the project preparation and supervision process.

~~48.~~42. Co-financing from the FIP may be provided through a variety of financing instruments utilized by the MDBs for investment and development policy lending. For example, these would include instruments that:

- Support the creation, rehabilitation, and maintenance of economic, social and institutional infrastructure
- Provide phased support for long-term development programs through a series of loans that build on lessons learned from the previous loan(s) in the series
- Build institutional capacity
- Provide long-term resources to local financial institutions to finance real sector investment needs
- Provide fast-disbursing loans or grants to help a borrower/recipient address actual or anticipated development financing requirements through a program of policy and institutional actions

➢ **Financing Modalities for Public Sector Involvement**

~~49.~~43. FIP funds used for public sector initiatives will seek to avoid market distortion and crowding out of the private sector. FIP funds will not be priced or structured to displace commercial financing or set unsustainable expectations in a market. FIP funds will be used to "crowd in" the private sector by enabling projects and investments to happen that otherwise would not by catalyzing those investments with their concessionality.

Grants

~~50.~~44. Grants may be used for:

Preparation activities

(a) Preparation of FIP investment strategies, where needed.

(b) Preparation of FIP supported projects.

Implementation activities

(c) Capacity development activities and activities related to policy and regulatory frameworks in the context of mitigating risks for future investments (especially in IDA countries).

(d) Grants for FIP investment projects or programs.

(e) Grant mechanisms for indigenous peoples and local communities.

(f) Grants for knowledge management activities as component of investment projects and programs[7].

These are explained in more detail below.

~~51.~~45. Care should be taken not to overlap or duplicate support but rather complement what is available from related programs such as the Forest Carbon Partnership Facility or UN-REDD.

~~52.~~46. *Preparation of Investment Strategies*: Since investment strategies will build on existing country strategies and programs, including REDD+ strategies (where available), it is expected that such grants will be used primarily for project and program preparation and less for the preparation of the Investment Strategy . In countries lacking an adequate basis for preparing investment strategies, the FIP may provide financing for the preparation of such plans. Such grants can be used to finance:

(a) strengthening consensus among key national stakeholders;
(b) ensuring that FIP investments are based on sound analytical work linking forest sector investments to economic growth and poverty-alleviation strategies; and
(c) other readiness planning activities.

~~53.~~47. A FIP preparation grant for an Investment Strategy should not exceed US$250,000. The request for a preparation grant for the Investment Strategy, if necessary, will be submitted together with the terms of reference for the Joint Missions. The MDB Committee will review and approve the terms of reference and request for the preparation grant[8]. This preparation grant should be recipient country-executed if feasible and appropriate.

~~54.~~48. *Project preparation grants*: The purpose of FIP project preparation grants to a country is to develop quality investment projects or programs by financing feasibility studies and associated analytical and design tasks. These grants could also support project or program preparation-related consultations, workshops and training.

~~55.~~49. No cap will be set for a FIP preparation grant for projects and programs. Funds for project preparation grants would be included within the envelope requested for the Investment Strategy. Proposals for project preparation grants should be included in the Investment Strategy, and the FIP Sub-Committee would be requested to approve the requested funding when it endorses the Investment Strategy.

[7] See document CTF-SCF/TFC.4/4, *CIF Knowledge Management – Creating the Capacity to Act*
[8] If the FIP Sub-Committee approves the delegation of authority for reviewing and approving the preparation grant for an Investment Strategy to the MDB Committee, a proposal will be submitted to the SCF Trust Fund Committee at its next meeting to increase the Country Programming Budget which is managed as part of the Administrative Budget of the CIF Administrative Unit to cover these costs.

~~56.~~50. Annex C provides guidelines for the approval and management of FIP preparation grants for Investment Strategies and Public Sector Projects.

~~57.~~51. *Capacity building:* Grants can also be used to support capacity development and policy analysis/formulation for forest and climate issues, especially where national public sector financing would not normally be available. The need for capacity building is likely to be the greatest in low income countries.

~~58.~~52. *Grants for ~~blending~~ FIP investment projects or programs*: Grant financing could also be considered for project components with very high additional costs that constitute a substantial portion of the total costs or with significant risks, and innovative financing instruments to soften commercial and/or MDB lending terms for forestry projects or programs. This would be on a case-by-case basis and considered by the FIP Sub-Committee on the basis of an assessment of the justification for grant financing (including the amount requested) and the availability of grant funding from other sources, such as the GEF.

~~59.~~53. *Dedicated Grant Mechanism for Indigenous People and Local Communities*: Grants will also be provided through the Dedicated Grant Mechanism for Indigenous People and Local Communities that is described in the FIP Design Document and will be detailed in upcoming guidelines.

Blending for Concessional Loans

~~60.~~54. The FIP financing is to fill the investment gap in projects and programs that address the underlying causes of deforestation and forest degradation, with concessionality related to the additional costs and risks of such investment. Concessional lending from the FIP could be used, possibly in combination with revenues from emissions reductions, to make forestry investments financially attractive by improving the internal rates of return on such investments. It is important to note that lending on concessional terms will contain a grant element, which is defined as the difference between the loan's face value and the sum of the present value of debt service to be made by the borrower, expressed as a percentage of the face value of the loan. Care should be taken not to overlap or duplicate concessional financing that is available from other sources such as bilateral donors, other development partners or GEF grants in sustainable forest management.

~~61.~~55. MDBs may provide FIP financing support through: (a) lending to national governments; (b) lending to national governments for on-lending to sub-national entities; or, (c) lending to sub-national entities[9]. The FIP grant or loan will have the same legal

[9] Sub-national entities would be eligible for support under either the public or the private sector window depending upon the source of complementary multilateral support. FIP financing could also be provided to special purpose vehicles owned either by the private sector or owned in part by the private sector and the government to carry out a project on a limited recourse basis where the resources for the project are derived from government entities. Such entities would be eligible for support under either the public or private sector windows depending upon the source of complementary multilateral support.

ranking as the MDB loan for the project (i.e., if the MDB loan is unsecured, the FIP grant or loan will be unsecured and if the MDB loan is collateralized, the FIP grant or loan would also be collateralized). MDBs' standard appraisal criteria will address credit risk through their assessments of borrower creditworthiness, financial viability, corporate governance, and safeguards against irresponsible borrowing.

~~62.~~56. Consistent with MDBs' standard lending practice, they will not seek any guarantee or security for FIP grants or loans to sovereign governments. If a FIP grant or loan is made to a sub-national entity, the member country, where appropriate, will be required to guarantee the grant or loan, where MDB sub-sovereign lending requires such guarantees. Annex D provides further information on measures the MDBs will take to administer loans, particularly with respect to guarantee or security of loans, as well as default provisions.

~~63.~~57. Given the objectives of the FIP to address the costs and risks of scaled-up forestry and forest-relevant investments by pilot countries, it is proposed that the FIP adopt lending terms similar to "IDA-only" or Regional Bank's equivalent for its loan operations. Furthermore, given the potential development impacts and environmental co-benefits of the FIP's investments, IDA-like terms should offer the appropriate balance in the concessionality of funding.

~~64.~~58. Therefore, it is proposed that the FIP offers two products for blending with MDB loans on the basis of an analysis in each project of its financial internal rate of return without FIP co-financing:

(a) Grants, for projects with:
  i. Negative rates of return.
  ii. Rates of return below normal market threshold.

(b) Concessional loans, for projects:
  i. with rates of return near or above normal market threshold, but below risk premium for project type, technology or country; or
  ii. with rates of return near or above normal market threshold, but where intensified forestry investment will have higher opportunity costs.

(Note: this might include investments in protected area systems to conserve existing reservoirs of forest carbon and biodiversity)

~~65.~~59. The following concessional loan terms for public sector projects are proposed. It is proposed that the FIP Sub-Committee reviews these terms after experience is gained in developing FIP programs and projects.

Box 1: Proposed Public Sector FIP Loan Terms[10]

---

a) The service charge is charged on the disbursed and outstanding loan balance. Principal and service charge payments accrue semi-annually to the FIP trust fund.
b) Grant element is calculated using the IDA methodology (assumptions: 6.33% discount rate for harder loans, semi-annual repayments; 8-year disbursement period)

	Maturity	Grace Period	Principal Repayments Year 11-20	Principal Repayments Years 20-40	FY10-11 Service Charge a/	Grant Element b/
FIP Loan	40	10	2%	4%	0.25%	~75%

~~66.~~60. Consistent with the objective of simplified loan administration procedures and streamlined project processing, it is proposed that the FIP will have uniform financing terms, rather than terms varying by country and/or projects, or each MDB applying different terms.

Guarantees

~~67.~~61. Guarantee instruments are used to improve conditions for investment in, or lending to, projects by mitigating risks that lenders and investors would not be willing or able to accept. FIP resources may be deployed as guarantees to promote forestry projects and programs which would otherwise fail to attract adequate capital. Proceeds from the FIP may be used to issue such guarantees by the MDBs, in accordance with their policies for determining eligible beneficiaries, eligible forms of investment, maximum tenor and maximum amounts. While guarantee support can be structured flexibly and may take various forms, these guidelines are intended to set generic parameters to guide MDBs in designing proposals which include the use of guarantees and similar risk mitigation mechanisms.

~~68.~~62. For each FIP operation, MDBs will appraise whether risk mitigation instruments could be an efficient and effective means to facilitate the mobilization of debt capital to finance the project, instead of, or in combination with, loan support from the FIP. Risk mitigation instruments should also be considered if the government or sub-national entity is not able to borrow debt on terms required for financial viability or attract financing without support, or if there is a perceived technology risk.

~~69.~~63. For purposes of FIP support, a distinction is required between conventional risks for which adequate mitigation measures are already available and "incremental" risks that are not assumed by sponsors and lenders, despite the appearance of financial viability of the investment. The additional risks of forestry projects can be quantified as the relative variance of a project's returns, as perceived by the main investors, for a given level of expected return.

(a) Technical and economic performance risks generally constitute conventional risks because they can be mitigated by the quality of project design and the structure of mutually reinforcing contracts. However, technical and economic performance can also represent risk barriers insofar as they are attributable to the application of commercially viable technologies in new markets. Lack of experience with forestry management and/or conservation options may create risk to project operations that may be reflected in higher rates of return required by sponsors and lenders. Risk mitigation instrument could address increases in operations and maintenance costs above estimates and where the operator has refused to guarantee additional cost coverage because of a new management or conservation technique.

(b) Commercial and financial risks such as high transaction costs, small project scale, weaknesses in domestic capital markets, and perceived credit risks are often primary risk barriers at the project level in the specific context of developing countries, contributing to the increased required rates of return or otherwise general unavailability of financing. Such risks are relevant to the application of risk mitigation instruments with FIP resources.

(c) While country or political risks are more easily differentiated from commercial risks in private sector projects, differentiation of these risks is more difficult for public sector projects and programs, where the project or program will be implemented by the government and its agencies. The FIP would not, therefore, provide "political risk guarantees" in public sector projects to protect lenders against specific political risks. Regulatory and institutional barriers are generally more effectively addressed through support for policy reform, capacity building and technical assistance, or other risk mitigation instruments available in the market as well as from bilateral and multilateral institutions.

~~70.~~64. It is proposed that FIP resources may be deployed for two categories of guarantee products:

(a) Loan guarantees covering the loss on account of debt service default for lenders up to an agreed portion of the actual loss[11], with a view to extending maturities of commercial loans for forestry projects so that they are competitive with alternative land uses, or to address specific incremental operating or management risks that could cause default.

(b) Contingent finance disbursed to the project upon underperformance of a forestry technology and where such risk is not commercially insurable at reasonable costs or has occurred beyond the period for which commercial insurance is available.

~~71.~~65. In both types of guarantees, the borrower may be a sovereign government, sub-national government, state-owned utility, or any other public sector entity which implements the proposed forestry project or program. Guarantees from FIP resources offered to public sector projects will have the following general terms:

[11] Depending upon the project and market needs, the amount guaranteed could be up to 100%. Some sharing could be useful for providing the right incentives to guarantee holders.

Box 2: Proposed Public Sector FIP Guarantee Terms

	Loan Guarantees	**Contingent Finance**
Guarantor	MDB will issue the guarantee acting as the Implementing Entity for the FIP (i.e. the guarantee beneficiary's recourse is solely to funds in the FIP).	MDB will be the provider of contingent finance acting as the Implementing Entity for the FIP (i.e. the Contingent Finance provider will provide funding solely from funds in the FIP).
Guarantee Beneficiary	Commercially-run institutions providing debt	Project entity
Guaranteed Debt	Any form of debt instrument (e.g. loans, bonds)	Not applicable
MDB Fee[12]	0.1% per annum on the undisbursed balance of the guaranteed financing, or 0.25% front-end fee on the guaranteed amount, to cover the MDB's appraisal, negotiation, supervision, disbursement, and reporting costs and any costs associated with restructuring and dispute resolution.	One-time charge of $200,000, to cover the MDB's appraisal, negotiation, supervision, disbursement, and reporting costs.
Guarantee Charge	0.1 % per annum on the disbursed and outstanding amounts of the guaranteed financing (accrues to the FIP trust fund).	0.1% per annum of the committed and undisbursed balance of the contingent finance (accrues to the FIP trust fund).

~~72.~~66. The following general terms are applicable for both types of guarantees:

Fund management: In order to maintain the creditworthiness of the guarantor in the eyes of commercial financiers, the MDB will retain FIP funds in an amount to match guarantees committed on a one-to-one basis.

Currency of

[12] See Annex B for explanation of the MDBs' project development and supervision costs.

Denomination:	US Dollars.[13]
Maximum Maturity:	Loan Guarantee term will be consistent with the maturity of the guaranteed debt. The term of the contingent finance will be decided on a case by case basis but not exceeding 20 years.
Minimum Maturity:	No restriction. MDB will ensure that the proposed tenor for either Loan Guarantee or Contingent Finance will make the proposed project or program financially viable and affordable in the given regulatory environment of the country.
Counter-Guarantee:	No requirement for sovereign government indemnity for any Loan Guarantee or Contingent Finance. Credit risk exposure under the FIP financing will be borne by the SCF trust fund.
Cross Default Clause:	There will be an optional cross default clause with MDB loans for the project/program.
Conditions:	Application of standard MDB policies and procedures. This should also ensure that the borrower has in place acceptable warranties and insurance consistent with industry practice.

Guidance on Choice of Financing Modality

67. The country financial and macro-economic circumstances differ in the selected pilots. While two FIP pilot countries are currently eligible to borrow on standard MDB loan terms, others may access only subsidized credit through a variety of windows. Some are eligible for a mix of credit and grant financing and some only for grant financing. In this context, the **countries' risk of debt distress should be assessed**. It is proposed that the risk ratings follow the same practice as in IDA and the relevant Regional Development Banks, that is from country-specific forward-looking debt sustainability analyses. For IDA, this is based on the joint IMF-World Bank debt sustainability framework (DSF) for low-income countries. The IDA grant framework then translate these debt distress risk ratings into "traffic lights", which in turn determine the share of IDA grants and highly concessional IDA credits for each country: high risk or in debt distress ("red" light) is associated with 100 percent grants, medium risk ("yellow" light) with 50 percent grants and 50 percent credits, while low risk ("green" light) is associated with 100 percent credits and zero grants.

MDB Fee

~~73.~~68. The MDB fees are to reimburse the MDB for its incremental staff, consultants, travel and related costs of project development, appraisal, implementation support, supervision and reporting (Annex E~~D~~).

[13] In the event that an MDB issues a guarantee in another currency, it bears the foreign exchange risk.

~~74.~~69. It is proposed that a simplified system be used to determine the MDB fee on each public sector project and program, and that such fees be approved at the time that an investment plan is endorsed by the Sub-Committee.

~~75.~~70. It is proposed that the same system for determining fees be used for all SCF targeted programs. A proposal, based on the MDB experience in preparing and supervising projects through their normal lending activities is under discussion by the MDBs. Once this proposal is agreed by the MDBs, it will be submitted to the Sub-Committee for approval.

- **Financing Modalities for Private Sector Involvement**

~~76.~~71. Because each country, sector and project faces a unique set of barriers, FIP financing will not be uniformly offered to all private sector companies, but will be tailored to address the specific barriers identified in each project and intervention.

~~77.~~72. MDBs will seek to use FIP funds in private sector markets where the risk/reward profile of initial project entrants are not balanced (ie. when the investment return on the initial projects do not compensate sponsors for the risks they experience) but where the risk/reward profile for future projects are eventually expected to be sufficient to encourage private investment without future subsidies (ie. where risks come down because of the track record established from the early projects and where costs go down – and returns go up - because precedents are set which facilitate project implementation). Given the probability that some FIP interventions will start at an earlier stage of development, the time lag from initial interventions to achieving long term sustainability will likely take longer in the FIP.

Principles for using FIP funds in private sector investments

~~78.~~73. FIP funds used in private sector investments will adhere to the principles outlined below.

~~79.~~74. *Minimum concessionality*: MDBs will seek to provide the minimum concessionality needed to catalyze projects and programs within a sector. In order to honor this principle, FIP funds will be structured on a case-by-case basis to address the specific barriers identified in each project/program. The amount and terms of FIP funding offered to an individual client will be determined between the MDB and the client on the basis of efficient and effective use of FIP and MDB resources. While an attempt will be made to quantify the additional costs faced by early entrants and compare that with the subsidy element implicit in the financing terms being offered, country, industry and individual company dynamics will impact the amount of concessionality a company will accept in order to undertake a project. Finding the right amount of concessionality[14] is

[14] Concessionality (or the subsidy element) of a FIP investment is calculated as the difference between the hypothetical market interest payments and the actual FIP interest payments over the life of the loan and

largely a matter of client needs, market conditions and negotiation, and is dependent on information not flowing between the companies or being available in the market. MDB's will always seek the minimum concessionality necessary to enable projects to happen and will justify the amount of concessionality requested in each FIP proposal.

~~80.~~75. *Avoiding distortion and crowding out:* FIP funds will not be priced or structured to displace commercial financing or set unsustainable expectations in a market. FIP funds will be used to "crowd in" the private sector by enabling projects and investments to happen that otherwise would not by catalyzing those investments with their concessionality.

~~81.~~76. *Leverage*: FIP funds will seek to catalyze and maximize the amount of MDB and other bilateral financing as well as commercial financing available for its projects and programs. A key feature of the FIP will be its ability to unlock both MDB and other private sector financing for REDD+ investments and catalyze ongoing sustainable investments in these sectors beyond the initial FIP investments.

~~82.~~77. *Financial Sustainability*: FIP programs will be developed to maximize the probability of long-term financial sustainability once the FIP funds are no longer available/have been used. Projects and programs should not be approved if they are likely to be dependent on a continuous flow of FIP funds. The project or program should at a minimum have the potential to achieve a substantial reduction in the need for subsidies in similar future projects beyond the initial few projects supported by FIP.

Private Sector FIP Instruments

~~83.~~78. Private sector engagement will generate both private and public benefits. For example, grants for the private sector may be justified when the intervention has clear demonstration effects that provide benefits beyond the company itself. Such public benefits could accrue to communities or advance market development. FIP funding to the private sector will encompass both grant and concessional finance.

~~84.~~79. Below is a description of the types of FIP instruments that may be structured to address the barriers identified in each case and justify the use of FIP funds in private sector investments.

Grants

~~85.~~80. Grants may be used for:

discounted using the relevant zero-coupon swap curve in the relevant currency; divided by the amount of FIP financing. For non debt products the interest payments in this calculation would be substituted by the relevant investment payments (eg. guarantee fees).

a. Market development activities, including but not limited to developing technical expertise, knowledge dissemination and capacity building of project sponsors and strategic market players (e.g. certifiers).
b. Capital cost buy-downs or performance grants for projects with a strategic / catalytic nature which cannot be better addressed through concessional financing or guarantees (capital cost buy downs would need to demonstrate how the use of FIP funds in this structure could lead to future projects of a similar nature without the need for subsidies.)
c. Community outreach and development that supports private sector participation.

~~86.~~81. Care would be given not to overlap or duplicate but instead complement activities undertaken in related programs such as public sector FIP activities or activities supported by UN-REDD or the Forest Carbon Partnership Facility.

Concessional Loans and Equity

~~87.~~82. FIP will offer concessional finance and equity products to support private sector projects and programs that have the potential of being replicated in the future without further subsidies. The terms and structures of each financial investment would be determined on a case by case basis to address the specific barriers identified in each case. These barriers may include:

a) Perceived risk, either by a project sponsor, a financier or both.
b) High costs of early entrants (the additional costs associated with being the first player to implement new regulations or work through unprecedented systems; they could also include higher input costs because economies of scale have not been achieved in the market.
c) Combined risk and cost barriers

~~88.~~83. Examples of projects that could be financed with FIP resources include (not comprehensive):

a) Lending for new non-traditional practices adoption which may reduce incentives pressures which lead to deforestation - concessionality may be needed to offset the costs of adopting such practices until a track record of costs and benefits can be achieved.
b) Lending to alternative livelihood projects which can be replicated in scale to reduce deforestation - such projects are likely to be perceived as too high risk for commercial banks to finance; FIP funding could help to develop a track record for such projects until commercial banks enter the market.
c) "Seed" equity could be provided to catalyze senior investments into a fund which makes FIP eligible investments (e.g. in reforestation or new sustainable harvesting practices) – once the projects have established a performance track record investors should be willing to continue investing without the need for additional seed capital.

Guarantees

~~89.~~84. Guarantees are typically used for the same reasons in the private sector as they are in the public sector, e.g. to address risks and improve the investment conditions for project sponsors. FIP would seek to use guarantees to mitigate risks in the project cycle with the objective of establishing a project performance track record which would then entice future private investment without the need for future subsidies/risk mitigants. For example, guarantees could be used to mitigate the risk and encourage external financiers to provide new financial products for FIP eligible projects (e.g. loans with extended grace periods to support harvesting cycles or first loss investments in a sustainable forestry bond structure; the benefit of guaranteeing commercial financiers is that their positive experiences would have the fastest replication impact, both in terms of scaling up their own financing programs and in eliciting competition among other financiers). The need for guarantees would be established on a case by case basis based on the project fundamentals.

MDB Fees

~~90.~~85. *Project specific budget allocation for implementation and supervision costs*: Private sector projects will vary in tenor and complexity resulting in the need for different supervision budgets for each project (e.g. a five year investment will typically require less supervision budget than a 10 year investment). As a result, private sector projects will not receive a standard percentage fee allocation per project, but will submit a customized budget request to cover supervision costs over the life of the project along with each project/program submission for Sub- Committee approval. Extraordinary costs associated with complex restructurings or exists would require the submission of a request for additional budget to the FIP Sub-Committee.

~~91.~~86. *Project and sub-project Implementation includes*: sub-project due diligence; structuring, approval preparation and review; preparation and negotiation of legal agreements; and, board approvals; project and sub-project loan/grant disbursement management; oversight of, or management costs related to, sponsor capacity building or completing knowledge management products; and procurement and management of consultants;

~~92.~~87. *Project and sub-project Supervision includes*: monitoring and completion of reports, site visits, negotiation and implementation of waivers and restructurings; monitoring and evaluation of individual projects including independent evaluation of completion/performance reports.

V. Financing Procedures and Conditions

~~93.~~88. Individual operations under each country’s FIP Investment Strategy will be processed through the MDBs selected by the country. Each operation will follow the investment lending policies and procedures of the MDB, including its fiduciary standards and environmental and social safeguards. Each MDB will apply its own appropriate procedures in appraising, approving, supervising, monitoring and evaluating operations to be financed from the FIP.

~~94.~~89. The following requirements will apply to all financing products financed by the FIP:

(a) Each operation will be approved and administered in accordance with the applicable guidelines of the concerned MDB, which will discharge its responsibilities with the same degree of care as it exercises with respect to its own resources;

(b) Allocations by the FIP Sub-Committee will be denominated in United States Dollars. However, MDBs may denominate individual financing provided by them to the beneficiaries according to their own policies and procedures, subject to the MDB assuming any exchange rate risk;

(c) The MDB will, for purposes of each financing, conclude an agreement with the beneficiary, indicating in particular that the resources have been provided from the FIP;

(d) Eligible expenditures under individual financing will be determined in accordance with the policies and procedures of the respective MDBs and with FIP investment criteria;

(e) The design and implementation of activities financed with FIP resources will ensure that appropriate environmental and social safeguards arrangements are carried out in accordance with MDB's policies and procedures;

(f) In each eligible country, the principle of sovereign programmatic prior no-objection will be a foundation of the Investment Strategy. The MDB will agree with the government on the overall program framework and will consult with the central government and request its endorsement on the engagement in each country. The MDBs will not seek their Boards' approval for any financial transaction which is not acceptable to the national government. The MDBs will follow their own operational procedures regarding notification of the national government of a proposed financing before Board consideration.

Annex A: Criteria to be considered in reviewing FIP Investment Strategies, Projects and Programs

Consolidated Criteria for FIP Investments		**Guidance from FIP Design Document on achieving FIP Objectives**	**What proposals need to present**[15]
Climate Change Mitigation Potential	GHG emission reduction or avoidance potential	Climate change mitigation potential	*An assessment of the direct GHG savings over the lifetime of the proposed project/program*: Emission reductions and avoidance will be calculated by subtracting projected lifetime emissions of the FIP-financed project from the projected lifetime emissions of the business-as-usual using a clearly-articulated reference level (baseline)
Demonstration Potential at scale	FIP investment addresses REDD+ priorities Area targeted by FIP investment compared to total area affected by forest degradation and deforestation. Information on historic emissions (reference level) or emission that might occur (business-as-usual	Addressing drivers of deforestation and degradation Demonstration, learning and impact capacity Measurable outcomes and results-based approach	*FIP investments address REDD+ priorities as presented in national REDD+ strategies or action plans (or equivalents):* This indicator will help ensure that FIP investments address the main drivers of deforestation and forest degradation. *Demonstration of scale of project*

[15] If a criteria or category is not applicable to the proposal, it should be so stated and a brief justification provided for the limited or non-applicability.

	scenario), which could be mitigated immediately as part of the Investment Strategy. Comparison between scale of emissions in the targeted area and other areas where deforestation or forest degradation is occurring, Permanence and leakage risks and current mitigation measures. Core set of indicators for application in FIP investments (consistent with FIP results framework) Description of good practices with potential for scaling up through FIP investment Description of good practices with potential for scaling up		*and program proposals*: This will be based on information on the area targeted by FIP investments compared to the total area affected by forest degradation and deforestation. Each proposal will provide information on the direct or indirect contribution of the FIP investment to the forest and forest landscape area conserved, restored, sustainably managed, protected, or afforested/reforested. *Use of good practices:* Each project and program will include information on relevant existing good practices which have potential to be scaled up through the FIP investment. *Results measurement:* A core set of indicators will be applied to FIP investments which are consistent with the FIP results framework
Cost-effectiveness	Economic and financial viability (catalyze self-sustaining financially profitable models) (paragraph	Leveraging additional financial resources, including from private sector Coordinating with other REDD efforts	Information on how achieved results will be sustained after completion of the FIP investment, including measures that generate positive

	16 (i) FIP investment per ton of CO2eq reduced or avoided Co-financing ratio FIP investment confirms REDD+ activities in national strategies or action plan, including where appropriate REDD+ readiness plans	(and cooperation with other actors and processes)	incentives and reverse problematic incentives across sectors and lead to lasting change. Where appropriate, a calculation of the costs per ton of CO2eq reduced or avoided. Information on the public and private sector institutions potentially involved in the implementation of the Investment Strategy, projects and programs, including the anticipated ratio of FIP co-financing to leveraged additional financial resources. Confirmation that the investment falls within the REDD+ national strategies or action plans (or equivalents), including, where appropriate, REDD+ readiness plans. (can be captured under criteria *Demonstration potential at Scale*).
Implementation Potential	Status of enabling environment for REDD+ (public policy, regulatory framework and institutions)	Forest-related governance provisions Country's ownership, preparedness and ability to undertake REDD+ initiatives (including strengthening cross-sectoral	Description how identified barriers and related needs will be addressed, including the creation of a cross-sectoral coordination mechanism to deliver on REDD+ and to integrate

	Institutional framework and cross-sectoral coordination mechanism to deliver REDD+ Identification of capacity building needs Public and private national and international contribution to FIP investment Risk assessment	ownership to scale up implementation) Capacity building measures for local and national institutions identified, including indigenous peoples and local communities	the role of forests into national sustainable development strategies. Expected co-financing leveraged from domestic public and private sector sources, including carbon finance, as well as bilateral and multilateral development partners. Presentation of risks associated with the proposed FIP investment and proposed mitigation measures.
Integrating sustainable development (co-benefits)	Identification of co-benefits from FIP-Investments (livelihoods, including gender dimension; biodiversity, ecosystems, climate resilience) Core set of indicators for application in FIP investments (consistent with FIP results framework)	Integrating sustainable development (livelihoods, biodiversity, ecosystems, economic viability)	A core set of indicators capturing co-benefits which are consistent with the FIP results framework. Demonstration of economic, social and environmental impacts from FIP investments and of consistency with relevant national strategies and plans. Information on how FIP investment will catalyze, support and measure and monitor the delivery of, *inter alia*, the following (as appropriate): a) Demonstrable improvement in social and economic well-being

			of forest dependent communities, including poverty reduction, job generation, wealth creation, equitable benefit sharing, and acknowledgement of the rights and role of indigenous peoples and local communities. b) Protection and enhancement of biodiversity. c) Strengthened resilience of ecosystems, with associated ecosystem services. Details on the inclusion of activities to be financed through the *Dedicated Grant Mechanism for Indigenous Peoples and Local Communities* and on coordination between projects and programs and the Mechanism.
Safeguards	Stakeholder involvement and consultation plan (including indigenous peoples and local communities; and gender considerations) Application of MDB safeguards and consistency with the decisions for REDD+ under the UNFCCC safeguards and consistency	Inclusiveness of processes and participation of all important stakeholders, including indigenous peoples and local communities Safeguarding the integrity of natural forests	Confirmation that FIP investment will not support the conversion, deforestation or degradation of such forests, *inter alia*, through industrial logging, conversion of natural forests to tree plantations or other large-scale agricultural conversion. Information on stakeholder consultation and participation plan.

	with the decisions for REDD+ under the UNFCCC		Applied MDB-specific safeguards. Consistency with decisions for REDD+ under the UNFCCC.

Annex B: MDB Safeguards
(to be checked by MDBs)

African Development Bank (AfDB)

http://www.afdb.org/fileadmin/uploads/afdb/Documents/Project-related-Procurement/ESAP%20for%20Public%20Sector%20Operations.pdf

Asian Development Bank (AsDB)

http://www.adb.org/safeguards/default.asp

European Bank for Reconstruction and Development (EBRD)

http://www.ebrd.com/pages/research/publications/policies/environmental.shtml

Inter-American Development Bank (IADB)

http://www.iadb.org/topics/sustainability/policies.cfm?lang=en

Bank for Reconstruction and Development (IBRD)

http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/EXTPOLICIES/EXTSAFEPOL/0,,menuPK:584441~pagePK:64168427~piPK:64168435~theSitePK:584435,00.html

International Finance Corporation (IFC)

http://www.ifc.org/policyreview

UNFCCC Ad Hoc Working Group on Long-Term Cooperative Action under the Convention

Draft decision -/CP.15 "Policy approaches and positive incentives on issues relating to reducing emissions from deforestation and forest degradation in developing countries; and the role of conservation, sustainable management of forests and enhancement of forest carbon stocks in developing countries":

http://maindb.unfccc.int/library/view_pdf.pl?url=http://unfccc.int/resource/docs/2009/awglca8/eng/l07a06.pdf

Annex C~~B~~: FIP Private Sector Proposal Template

Name of Program	
FIP amount requested / Total Program Cost (US$):	
Country targeted	
DETAILED DESCRIPTION OF PROGRAM	
Description of the Program including: ➢ Fit with the FIP Investment Plan ➢ Country and sector context ➢ Barriers that exist for market transformation ➢ Program in generic terms including: a) **a profile of the sub-projects** expected to be financed under the Program (sector, average size, geography, **ranges of expected results**, etc - for purposes of confidentiality, company names and details that would make the program identifiable by third parties are not to be included in the description.); the number of investments expected in portfolio; the **financial instruments** expected to be used including how the grant/concessional finance portion will be applied (which components of the program, percent of overall financing, etc); and the **financing parameters for CTF investments** (floor pricing, expected tenors, subordination, security, etc) b) a description of the **advisory services and knowledge management** initiatives and instruments. ➢ note the expected life of the Program from date of approval (investment & supervision period)	
Describe the Proposal's strategy for achieving market transformation including: ➢ Explain how the Program addresses the objective of market transformation at a country and/or sector level. ➢ Describe how the Proposal fits i) the identified role of the private sector as described in the Investment Plan; and ii) within a country's existing regulatory environment and government policies; where it doesn't, explain how this will be addressed/ mitigated ➢ Explain how the MDB will leverage its ongoing activities and existing strengths	
FIT WITH INVESTMENT CRITERIA ***Note:* Not all investment criteria will be applicable to all programs. Provide comments only on those relevant to the program being proposed.**	
i)Climate change mitigation potential: ➢ Calculate the amount of CO_2-eq~~uivalent~~ emissions savings expected to result during the life of the proposed Program	

Formatted: Subscript

ii) Demonstration Potential at Scale: ➢ Provide information on the direct or indirect contribution of the FIP investment to the forest and forest landscape area conserved, restored, sustainably managed, protected, or afforested/reforested.	
iii) Cost-Effectiveness: ➢ The expected GHG reduction during the life of the program per FIP donor dollar invested and per total program cost dollar invested.	
iv) Implementation Potential: ➢ Describe how the program supports REDD+ efforts demonstrated through country and sector strategies; institutional and implementation arrangements; sustainability and effective stakeholder participation and decision making ➢ Note the extent to which the current regulatory environment supports, or does not impede, the development of the private sector; where barriers exist, explain how these will be addressed. Outline the range of resources mobilized by non-FIP funds, including the MDBs and the private sector – both domestic and international, including carbon finance if appropriate.	
v) Integrating Sustainable Development (co-benefits): ➢ Describe how programs will demonstrate economic, social and environmental impacts from FIP investments	
vi) Safeguards ➢ Provide information on how environmental and social safeguards and criteria, including those defined in the *FIP Design Document* are to be applied to the program	
vii) Financial Sustainability ➢ Describe how sustainability will be achieved (i.e. why similar future programs would need significantly less or no grants/concessional finance). Programs should not be approved if they are dependent on a continuous flow of FIP funds. The Program should at a minimum have the potential to achieve a substantial reduction in the need for subsidies in future projects. ➢ Identify specific institutional factors that will be necessary to enhance the commercial viability of the project, if any.	
viii) Level of Concessionality ➢ Quantify the level of concessionality	
ix) Mitigation of Market Distortions ➢ Discuss how the Program will seek to minimize or avoid distorting markets, displacing private sector investment, including carbon finance where it is supporting similar investments within a country and/or sector, or reducing competitiveness.	
x) Risks ➢ Discuss the risks inherent in the Program or Proposal and how these are being mitigated/addressed.	
xi) Performance Indicators ➢ List relevant "Performance Indicators" for the program.	

Annex D~~C~~

Guidelines for the approval and management of FIP preparation grants for Investment strategies and Public Sector Projects

1. Objectives. The purpose of Forest Investment Program (FIP) preparation grants is to develop a quality investment portfolio by: (i) strengthening consensus among key national stakeholders and development partners; (ii) enhancing capacity of national institutions for robust policy reform and priority setting; (iii) ensuring that FIP investments are based on sound analytical work linking forest sector investments to economic growth and poverty-alleviation strategies; and, (iv) assessing the poverty and social impacts of programs and projects.

2. Grant Execution Arrangements. Preparation grants will be generally Recipient-executed if feasible and appropriate. All preparation grants will be supervised by the MDB in order to ensure compliance with its operational policies and procedures, including procurement and financial management guidelines. The closing date of FIP grants should not exceed 2 years from the date of signature of the grant agreement by the MDB.

3. Eligible Grant Activities. FIP preparation grants may be used for developing FIP investment strategies and preparing FIP co-financed projects by recipient countries. The following activities will be eligible:

(a) Analytic work to inform a country's policies and programs.
(b) Design of policy reforms and preparation of legislation and regulations.
(c) Consultation workshops.
(d) Training.
(e) Institutional development.
(f) Feasibility Studies.
(g) Environmental and social impact assessments.
(h) Technical[16], managerial, and financial project design.

4. Maximum total FIP preparation grant allocation for an investment strategy will be US$250,000.

5. Eligible Expenditures. There will be no maximum allocation for a project preparation grant. The grant amount will be included in the FIP funding available for the Investment Strategy endorsed by the FIP Sub-Committee but will be made available prior to approval of FIP funding for the project to finance country-driven preparation activities. The preparation grant will finance expenditures for: (i) consultants' services, local training, workshops and seminars and, (ii) operating costs and office equipment for the implementation management of grant activities not to exceed 10% of the grant amount.

[16] Including environmental and social consultants.

6. Ineligible Expenditures. The following expenditures will be ineligible: (i) salaries for civil servants in recipient countries hired as consultants or otherwise; (ii) purchase of vehicles; (iii) foreign training and study tours; and (iv) salaries and travel of MDB staff and consultants.

7. Reallocation of Grant Activities and Funds. If the reallocation requires a formal amendment to the grant agreement according to the MDB's policies, then the MDB will seek approval from the FIP Sub-Committee prior to amendment. If no amendment is required according to the MDB's policies, the MDB may reallocate according to its procedures and will inform the FIP Sub-Committee upon such revision.

8. Grant Cancellation Policy. In addition to the requirement of each of the relevant MDB's policy on cancellation, the balance of preparation grants may be subject to cancellation under the following circumstances: (i) the grant agreement has not been signed six months after approval of the grant; or (ii) there has been no implementation progress, including zero disbursements for 12 months after signature of the grant agreement. The MDB may approve exceptions on the basis of a satisfactory explanation, which will be reported to the FIP Sub-Committee.

9. Schedule. Requests for project preparation grants should be submitted as part of the Investment Strategy when it is submitted to the FIP Sub-Committee for endorsement. Upon approval by the FIP Sub-Committee, the appropriate authority in the MDB will be authorized to sign a grant agreement.

Annex E~~D~~
MDB Public Sector Project Development and Supervision Costs

1. Cost recovery for the MDBs' expenditures related to managing the project cycle will be based on MDB fees approved by the FIP Sub-Committee and paid by FIP recipients in the case of loans and guarantees, and by the SCF trust fund in the case of grants. The MDB fee will reimburse the MDB for its incremental staff, consultants, travel and related costs of project development, appraisal, implementation support, supervision and reporting. In particular, the MDBs will carry out the following tasks:

Project Preparation

(a) Project concept review.
(b) Quality enhancement and assurance to meet quality at entry standards;
(c) Risk management.
(d) Financial management and procurement assessments of project implementing entities.
(e) Country dialogue on and appraisal of the sector policy, technical, economic, financial, institutional, fiduciary, environmental and social aspects of projects.
(f) Preparation and negotiation of legal agreements.
(g) Board approvals.

Project Supervision

(a) Implementation status reporting.
(b) Adaptive management of project strategy and design.
(c) Loan/grant disbursement management.
(d) Implementing project at-risk systems.
(e) Supervision of project monitoring, evaluation, environmental and social safeguard measures, procurement and financial management by borrower/recipient.
(f) Implementation completion reporting.
(g) Independent evaluation of completion reports.

2. FIP financing will generally be seamlessly blended with MDB financing, resulting in significant transaction cost savings. However, there will be some incremental costs to the MDBs for mobilizing FIP co-financing for clients, due diligence, and reporting, which will be recovered through the MDB fee. Such costs include:

(a) Analysis of consistency with FIP investment criteria.
(b) Additional financial analysis to justify FIP concessional financing.
(c) Calculation of GHG emissions reductions benefits.
(d) Inclusion of forestry specialists in operations teams.
(e) Monitoring and evaluation for FIP results measurements system.
(f) Additional cost of legal, loan and accounting departments to administer FIP trust fund resources.

3. The MDBs will provide an annual report to the FIP Sub-Committee on their project processing and supervision costs, which may provide the basis for any adjustments to the MDB fee by the FIP Sub-Committee.