



# Global Environment Facility

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GEF Council  
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Agenda Item 8

## REPORT ON INCREMENTAL COSTS

***Recommended Council Decision***

The Council, having reviewed the *Report on Incremental Costs* (document GEF/C.14/5), takes note of the progress that has been made in addressing the recommendations that emerged from the earlier consultative process and requests the Secretariat and the Implementing Agencies to continue their efforts to make the process of determining incremental cost more transparent and its application more pragmatic.

## INTRODUCTION

1. At its last meeting in May 1999, the Council had before it the *Note on Incremental Cost* (GEF/C.13/7) which outlined steps proposed to be undertaken to make the process of determining incremental cost more transparent and its application more pragmatic. The Council approved these steps and also requested the Secretariat to keep it informed of progress made in completing the proposed activities and to identify specific actions to be implemented for real, measurable progress in this area.

2. Three principles have guided the Secretariat and the Implementing Agencies in their work to achieve concrete progress. First, to address the specific recommendations that emerged from the earlier consultative work. Second, to mainstream the outputs from these specific actions into existing GEF processes and procedures, since the estimation and agreement of incremental costs should be a very coherent part of project design, rather than a separate or additional issue which is handled along a parallel pathway. Third, to continue to be proactive in seeking opportunities to further increase the transparency and pragmatic application of incremental costs.

3. This *Report on Incremental Costs* to Council provides a summary of the progress made, and in particular highlights a programmatic focus to the determination of incremental costs.

### *Project Cycle and Project Review Criteria*

4. In accordance with the agreement of the Council, the GEF project cycle is being updated to incorporate Council approved procedures. As part of that work, the incremental cost requirements will be incorporated into the project cycle.

5. *Agreement process for incremental cost:* Strengthening country involvement in estimating and reaching agreement on the incremental costs is a priority. The incremental cost working group, comprised of representatives from the Implementing Agencies, the Convention Secretariats, and the GEF Secretariat, elaborated “Principles for the Agreement Process for Incremental Costs” to clearly articulate and underline the agreement process. These principles provide for country involvement in incremental costs estimation and negotiation at discrete points in the project cycle (i.e. pipeline entry, approval and endorsement phases) (Annex A).

6. *Streamlined Procedures for Incremental Cost Assessment:* Earlier recommendations supported the broader application of streamlined procedures through different stages of the project cycle. These procedures are being incorporated in the updated project cycle and the project review criteria relating to each phase of the cycle. Most valuable, in this context, is the formalization of the pipeline entry phase which allows for upstream consultation to be conducted in an open and transparent manner, and for the incremental reasoning to be clearly articulated at an early stage. Throughout the project cycle, incremental costs remain a key review criteria, with

increasing need for clarity as the project preparation proceeds. These efforts, taken together with the country's involvement in the agreement process, provides for much greater transparency.

7. As part of the efforts to obtain direct feedback of this experience from the countries perspective, the Secretariat will again invite individuals or agencies executing projects to document their experiences, especially in relation to the agreement process. The dissemination of good practices will continue through GEF's outreach and communication strategy.

### *Empowerment and Training*

8. *Country Dialogue Workshops Project:* Work is well underway in preparation for these dialogue workshops which seek to raise awareness of GEF, build country co-ordination, identify country priorities, and improve capacity to participate in GEF activities. Material is under preparation for these workshops, and the team preparing the material is alert to the key recommendations relating to incremental costs arising from the earlier consultation and feedback. It is anticipated that the workshops will: -

- (a) enhance the skills of a broad-based national audience to participate in the agreement and negotiation process relating to incremental costs; and
- (b) provide specialized training on the estimation of incremental costs. In this latter case, the workshop will emphasize the use of the logical framework in project design as a critical element in incremental cost estimation. These workshops are to commence early next year, and an iterative approach will be adopted in organizing the first few workshops, improving the presentation of materials based on feedback and experience.

9. *GEF Familiarization Workshop:* The first such workshop was held in May 1999, to train staff of the GEF family (including Secretariat, Implementing Agencies, executing agencies, co-financiers and other stakeholders) with the objective of ensuring common understanding of the GEF's policies and procedures. A module presented on incremental cost provided an opportunity for training those directly involved in the estimation and negotiation of incremental costs (staff and consultants) with a view to ensuring that the dialogue with recipient countries is increasingly consistent. The next familiarization workshop will be held in December 1999.

### *Outreach and Communications*

10. To improve outreach, GEF will prepare material that is more "user friendly," translate materials more widely, and extensively disseminate best practice. The GEF Secretariat and the Implementing Agencies will take advantage of every opportunity to disseminate the new information that is being produced.

11. GEF is currently redesigning its website. As part of the new outreach strategy consideration will be given to having on-line project development advisory services, which would provide guidance on all relevant aspects of project development and management in accordance with GEF policies and procedures (including incremental cost). Such an interactive homepage would supplement country level outreach activities and would allow back-up support for local experts applying project development skills on-site.

#### *Conceptual Issue in Incremental Costs*

12. *Conceptual challenges:* As indicated in the earlier paper to Council, there are some conceptual issues that remain challenging to project proponents, especially the country counterparts. The Secretariat and the Implementing Agencies are cognizant of the fact that further clarifications on the conceptual aspects of incremental cost are critical to some of the process related issues discussed above (especially as it relates to the agreement process). These conceptual challenges and the process related issues are being pursued in parallel.

13. *Focal area specific approaches:* Earlier consultations indicated that there may be a need to look at focal area specific approaches for incremental cost estimation, and that the focal area task forces should be invited to explore these issues. To guide this process, the Secretariat and the Implementing Agencies prepared some terms of reference focusing on the conceptual challenges. Annex B sets out these terms of reference and summaries of the feedback from each of the task forces. These ideas are still being consolidated and will be critical in further simplifying the estimation of incremental costs, and in the preparation of the relevant material mentioned above. A consolidation of the main ideas, and proposed innovations, especially for medium sized projects, will be available at the time of the first Council meeting in 2000.

#### *Programmatic Focus for Determining Incremental Cost Financing*

14. As experience has been gained in the operations of the GEF, it has become clear that there are clear advantages to seeking the development of an integrated set of project activities through a focused programmatic approach. This section seeks to set out some broad principles for structuring project planning through a programmatic focus within the context of the GEF operational strategy and programs, and in particular, to provide some guidance on the application of the incremental cost approach at the programmatic level. Such a focus will not seek to replace the project approach but rather seek to complement it.

15. *Features of a programmatic focus:* A programmatic focus for determining incremental cost financing would be fully consistent with the ten operational principles for development and implementation of the GEF's work program approved in the GEF operational strategy. It would provide phased and sustained support for the implementation of a multi-year (medium to long-term) program that serves to better integrate global environmental objectives into national strategies and plans (e.g. biodiversity strategy and action plan or a sustainable energy plan). In

applying such an approach, it would be essential to work closely in partnership with the country counterparts, relevant donors and development agencies. GEF funding at a programmatic level, whilst fully consistent with the incremental cost principles, would emphasize the co-financing and leveraging aspects of program funding. GEF funding would capture the global benefits in the proposed plan (or program).

16. The delivery of the program would be assessed against programmatic indicators. Monitoring and evaluation will be essential to set specific benchmarks within defined time frames, build in assessments at each phase, and establish the next set of targets. Projects would continue to be structured within an agreed programmatic framework to deliver on specific outputs and outcomes contributing to the programmatic objectives, including securing global environmental benefits.

17. A programmatic approach will emphasize: -

- (a) the achievement of agreed development and global environmental outcomes as a result of the program;
- (b) agreed objectives and indicators of outcomes/impacts for each phase of the program;
- (c) sequencing of GEF disbursements for phased support of the program based on identified milestones in achieving the program's objectives; and
- (d) a monitoring and evaluation system.

18. *Scope:* The scope of a programmatic focus would be defined by country priorities and the global environmental benefits to be achieved. In this context the programmatic focus might encompass a single operational program, a single focal area, or if cross-fertilization among focal areas is essential to achieve the outcomes, multi-focal area objectives will constitute the programming framework. Projects would continue to be elaborated within an agreed programmatic framework to deliver on specific activities, outputs and outcomes contributing to the approved programmatic objectives.

#### *Not a New Paradigm*

19. It is important to emphasize here that a medium or long-term programmatic focus for financing is not a new paradigm to the GEF. The paper to GEF Council on "*Strategic Partnerships with the GEF Implementing Agencies*" (GEF/C.13/9) highlighted several situations which effectively reflect a programmatic focus. In the case of UNDP's *Small Grant Program* which aims to build long term support for the global environment at the local level, the need for a clear commitment and stability of support was seen as critical. This partnership has helped GEF, through UNDP, to leverage greater commitment from local partners by maintaining support for them long enough for effective engagement and to ensure the sustainability of SGP's. Recognizing the limited availability of resources at the local levels, and the scale of operations, the tact here was to adopt a flexible approach which called for at least a 1:1 ratio for funding at the

programmatic level. The assurance here was that GEF resources at the project level would be used for securing global environmental benefits.

20. The *Renewable Energy Partnership* with the World Bank was set up to help achieve shared programmatic objectives. Through this partnership GEF would commit about \$200 million while seeking World Bank Group commitments of at least \$600 million in co-finance. A strategic partnership of this form and magnitude would respond vigorously to countries that have made long-term commitments to promote renewable energy technologies. The more commercial nature of this operation and potential for private sector involvement justified the 1:3 ratio for funding.

21. There are ongoing discussions with a country to explore the possibility of using identified national priorities for biodiversity to develop a country programming framework. Such a programmatic focus would include multi-year government and donor (GEF and others) commitment, linked to specific project outputs . The proposed framework would seek to program resources in periods of five years, identifying key benchmarks and indicators to clearly identify progress made and projects to follow up. Financial resources would be committed based on completion of benchmarks. It is also likely that the elaboration of the GEF interagency multi-focal *Land and Water Initiative* will lead to a programmatic framework for achieving its goals.

22. *Advantages, Challenges and Safeguards of a Programmatic Focus:* An assurance of longer-term commitment through the GEF and other partners would provide some distinct advantages for all stakeholders. At the same time there are also distinct challenges to be faced when adopting a programmatic focus. Recognizing these advantages and challenges from the outset will enable such a focus to be applied in an effective and streamlined way.

23. Some of the advantages in adopting a programmatic focus include:

- (a) a better opportunity to integrate and mainstream global environmental issues in the national planning and development processes;
- (b) a better opportunity for implementing a national biodiversity strategy and action plan or an energy plan resulting from national communications;
- (c) increased country ownership and commitment to longer-term frameworks for sustainable development and global environmental benefits;
- (d) increased co-financing and leveraging of resources from a multiplicity of donors, including the private sector;
- (e) further strengthening of policy and regulatory frameworks in country;
- (f) further strengthening of financial and institutional sustainability of GEF funded activities;
- (g) an enhanced scale of intervention leading to improved scope for catalyzing action, replication and innovation;
- (h) improved co-ordination among Implementing Agencies/Regional Development Banks;
- (i) improved donor co-ordination, and;

- (j) key GEF review criteria (e.g. program and policy conformity, replicability, sustainability (financial and otherwise)) can be addressed more effectively.

24. Some of the challenges in adopting a programmatic focus include:

- a) specific activities to be carried out under a program are likely to be less defined at the time of Council approval than is presently true for approval of project proposals in the work program;
- b) government commitment to a long-term program could change due to a variety of factors (economic crisis, natural disasters, change of government);
- c) inherent risks and uncertainties associated with the design and anticipated objectives and outcomes of the program itself, and;
- d) immediate impacts and outcomes relating to the global environment may be difficult to assess.

25. *Safeguards*: It is important to have appropriate safeguards in place to address these challenges and to maximize the benefits. The challenges should initially be addressed on a case-by-case basis in an adaptive and flexible way. As more experience is gained it will allow further specification of the criteria relating to approval of a programmatic focus and the incremental cost application.

26. The importance of monitoring and evaluation (M&E) for a programmatic focus cannot be over-emphasized. M&E is essential to: -

- (a) set specific targets (or benchmarks or milestones) within defined time frames;
- (b) build in assessments at each phase, and
- (c) establish the next set of target.

This would provide management with the appropriate information to approve subsequent projects or tranches within a program. It also helps to ensure that projects (or tranches) within a program remain flexible and employ corrective actions, as required. Monitoring and evaluation should be used purposefully to emphasize improved likelihood of project and program success, recognizing the need for results-based monitoring and evaluation. A program approach also focuses M&E on the measurement of project impacts or results rather than just outputs, since project-level changes will have to be made based on the results being achieved.

#### *GEF financing in a Programmatic Focus*

27. A programmatic focus represents a significant innovation towards more pragmatic application of the incremental costs approach. The programmatic focus as outlined above seeks to maximize and scale up the global environmental benefits. GEF funding at the programmatic level should, while remaining consistent with the incremental cost principle, seek to further emphasize the co-financing and leverage aspects. Additionally, consistent with current practice for projects, a



programmatic focus could include grants and/or concessional funding, depending on the nature of the components within the program.

28. The financing package in GEF projects traditionally includes reference to co-financing, leveraging and associated financing. There is a need to examine some features of these financing aspects, especially in relation to the programmatic focus. First, it is important that each of these financing features be interpreted and understood in a broadly consistent manner. Although co-financing, and by extension leverage, is largely interpreted as new and additional resources to implement the GEF intervention, non-leveraged baseline financing is recognized to be equally important. The latter is important in two ways: -

- (a) as a sign of national commitment, and,
- (b) it may actually involve some substitutional activities which are critical to the GEF intervention and capturing of global environmental benefits.

29. Second, it is quite clear that with a programmatic focus, the importance of the associated financing becomes enhanced. GEF programmatic financing will have to be nested within given national (sustainable) development baselines, the absence of which would imperil flows of global environmental benefits. It would be critical, in this regard, to have a clear indication of such expenditures (termed associated financing). Even though this associated financing may not be directly leveraged by the GEF, it clearly represents the baselines upon which global environmental objectives can be accrued<sup>1</sup>.

30. Third, with a programmatic focus, the GEF is better able to play a critical role in catalyzing and mobilizing donor consultation and co-ordination. The development of clear and transparent criteria for GEF financing which are consistent with funding mobilization of other major donors would hence be both a clear pre-requisite and advantage, if the global environmental benefits are to be realized. Also it will allow the mobilization of funds for sustainable development.

31. As mentioned above, a programmatic focus for determining incremental cost financing is not a new paradigm to the GEF. This note sets out some features of this approach, especially in relation to GEF's role in financing and acting catalytically to leverage financing for sustainable development and the global environment. Recognizing the wide scope for applying a programmatic focus in the determination of incremental cost financing, there is a need to develop a range of options responding to different conditions under which the programmatic approach could be implemented. The criteria for the determination of GEF financing, and aspects of co-financing, leveraging and baseline associated costs would be set out for each of these options.

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<sup>1</sup> It is important, however to ensure that any request for associated financing does not either penalize or send perverse incentives to countries. Associated financing will need to be looked at on a case-by-case basis, against the other criteria/requisites for a programmatic approach.

These options will be explored and elaborated upon in the ongoing operational work at the programmatic level.

## ANNEX A

### PRINCIPLES FOR THE AGREEMENT PROCESS FOR INCREMENTAL COSTS

#### *Country involvement*

1. The Implementing Agency and in-country project sponsors, designers and local executing agencies should work collaboratively in calculating incremental costs. Incremental cost estimation should be a joint task of the GEF Implementing Agency and the in-country partners proposing or designing the project, or expected to implement the project locally. Agreement on incremental cost should be part of, and the result of, collaborative decision-making on project development and preparation, which should be done using the logical framework approach. Project briefs should describe the process used to determine incremental cost, a process that is intrinsic to good project design.

#### *Differentiated, but shared, responsibilities*

2. In the GEF project cycle, the following parties have roles in the process of determining of incremental cost:

- (a) *In-country project proposer/sponsor/designer/local executing agency*: The country partner should jointly undertake incremental cost determination with the Implementing Agency. In particular, the country partner could assume primary responsibility for the following tasks related to incremental cost negotiations: -
  - (i) collecting and analyzing relevant country data;
  - (ii) identifying stakeholders for broader consultations and organizing a log-frame or project development/consultation workshop, and;
  - (iii) conveying basic IC principles to stakeholders
- (b) *GEF Operational Focal Point*: The GEF Operational Focal Point can support the incremental cost negotiation process by: -
  - (i) reviewing projects, endorsing their consistency with respect to national programs, and confirming national priorities, and,
  - (ii) facilitating broad as well as project-related consultations, particularly with government agencies.
- (c) *Implementing Agencies*: The Implementing Agency is responsible for: -
  - (i) supporting the country's efforts to prepare projects, particularly with respect to implications of GEF policies and procedures, such as incremental cost, and;
  - (ii) facilitating the processing of these proposals through the GEF project cycle. The Implementing Agency is responsible for informing the project

proponent about the need to undertake an incremental cost assessment and the ways and means to do so, at the earliest stage of their dialogue on a project proposal.

- (d) *GEF Secretariat*: At entry into pipeline, the GEF Secretariat reviews the “incremental principle” of the concepts submitted by an Implementing Agency or Regional Development Bank and provides feedback on eligibility. At entry into the work program, the GEF Secretariat reviews the incremental cost assessment (baseline scenario, GEF alternative scenario, and incremental cost components). At CEO endorsement, the GEF Secretariat reviews the final incremental cost determination, and checks for consistency with the work program inclusion document.

#### *Early and substantive feedback*

3. The GEF Secretariat should provide early feedback on the incremental reasoning of projects at entry into the pipeline. This upstream consultation between the Implementing Agency and the GEF Secretariat should include specific comments on what minimum information will be expected at the next step in the project cycle – e.g. on domestic and global benefits, baseline scenario, and barrier removal in the project. The review should also identify any project design issues that might have implications for the incremental cost analysis.

#### *Transparency*

4. The GEF Secretariat’s reviews of projects, including the incremental cost section, should be shared with the project proposers in a timely fashion. In addition, the Implementing Agency and project proposer should jointly document the incremental cost negotiation and agreement process, a summary of which should be included in the project brief at the time of submission for work program entry.

#### *An emphasis on quality, not numbers*

5. The starting point for determining incremental cost should be the use of the “incremental reasoning” of projects, rather than quantification. Once the full set of project activities has been developed, the principles of incrementality can be applied to separate incremental from baseline activities. The GEF’s review of incremental costs should be based primarily on the qualitative presentation of the incrementality of project activities, rather than a quantitative analysis. At the time of entry into the work program, incremental cost may be presented as an estimate within a range approved by the GEF Secretariat, when additional discussion is needed on the issue and the constraints and challenges to estimating incremental cost are described in the project brief.

*Integrate incremental cost estimation with logical framework analysis during project development*

6. The process of estimating incremental cost should start early in project development, as part of the log-frame process of participatory, iterative and multi-stakeholder development of projects. A log-frame workshop, or similar collaborative project development consultation, should provide the forum for identifying stakeholders in the incremental cost negotiation; conveying the basic principles of IC; stimulating participating of in-country partners in IC estimation; and, discussing baseline and alternative scenarios.

*Informed agreement*

7. In-country project partners should have access to certain minimum information on the GEF's procedures for calculating incremental costs, including GEF project review criteria, guidelines for estimating global and domestic benefits, and guidelines for estimating baseline costs. This information should be readily available at the GEF reference library in each country and through the GEF website. The Implementing Agency should advise project partners about the availability of such information.

8. The above principles for the agreement process will be incorporated into the updated project cycle as follows:

- (a) *First GEF Decision- Pipeline Entry:* The Secretariat reviews the proposal against the Project Review Criteria that are relevant for that type of project, and applies the criteria for *conceptual conformity* only. The incremental reasoning of projects at entry into pipeline should be clear. This will be followed by Phase I; Preparation and Development, where incremental cost estimation should be a joint task of the GEF Implementing Agency and the in-country partners proposing or designing the project, or expected to implement the project locally. Agreement on incremental cost should be part of, and the result of, collaborative decision-making on project development and preparation, which should be done using the logical framework approach.
- (b) *Second GEF Decision - Approval:* The project briefs should describe the process used to jointly determine incremental cost, a process that is intrinsic to good project design. At the time of entry into the work program, incremental cost may be presented as an estimate within a range to be approved by the GEF Secretariat. When additional discussion is needed on the issue, the constraints and challenges to estimating incremental cost are described in the project brief.

- (c) *Third GEF Decision – Endorsement:* The Secretariat reviews the project document for consistency with the project brief approved by Council. Any outstanding requirements should be satisfied. For example, if at the approval stage incremental cost was presented as an estimate within an approved range, the cost should be final at this stage.

## ANNEX B

### CONCEPTUAL CHALLENGES OF INCREMENTAL COSTS – TERMS OF REFERENCE FOR THE FOCAL AREA TASK FORCES AND THEIR INITIAL FEEDBACK

#### *Terms of Reference*

1. The RESOLVE study had indicated that there may be a need to look at focal area specific approaches for incremental cost estimation. In response to this, we had as part of the preparation of the London workshop commissioned focal area specific papers to look at the issue of incremental cost. Further, at the IIED/GEF London workshop we had breakout groups looking at the incremental cost issues specifically from the focal area perspective. Although the London workshop was less conclusive on the need for focal area specific approaches, it had recommended that this needed to be looked at further. In this context, we invited each focal area task force to look at this issue.
2. The recommendation was for each of the focal area task forces, in light of the practical experience gained up to now, to consider the conceptual challenges faced in designing projects, and to provide some simple guidelines or principles, specific to the focal areas.
3. The main conceptual challenges identified in applying incremental cost (summarized from the London report) are: -
  - (a) How do you judge whether a particular activity/action generates: -
    - (i) primarily domestic/local benefits;
    - (ii) primarily global benefits;
    - (iii) joint benefits?
  - (b) In the case of joint benefits what guidance can we give project proponents on cost-sharing of such activities?;
  - (c) How do you determine the baseline and sustainable development baseline? How does this relate to the application of the principles of leveraging, co-financing, cost-sharing and associated costs to incremental cost in the focal area? Should the baseline be defined in a qualitative or quantitative way?;
  - (d) Are there special challenges to incremental costs estimation in projects with the private sector? Do we need to consider ranges of incremental cost estimates as opposed to a single number?;
  - (e) How can incremental cost estimation (which is driven by a focus on global benefits) be made more compatible with GEF's public involvement policy that emphasizes local community participation?;
  - (f) How can the streamlined procedures be applied to the focal area? What specific modifications, if any, are needed to make these procedures widely applicable?
4. *Task for focal area task force:* to discuss the "conceptual" challenges faced in applying incremental cost in practical context in your focal area.

5. *Outputs:* provide simple guidelines and/or principles which could be applied to:
- (a) the project design module to facilitate estimation of incremental cost (using a log-frame approach) in your focal area; and
  - (b) the process for reaching agreement on the incremental cost with the key stakeholders.
6. The input from the focal area task forces will be reviewed, discussed and consolidated to see how best we can move forward on this issue. This input on conceptual side is critical for furthering our work on several of the other recommendations.

*Feedback from the Biodiversity Task Force*

7. The Biodiversity Task Force addressed issues underlying the conceptual challenges posed in the terms of reference provided to them. Much of the discussion focused on Question 1: How do you judge whether a particular activity/action generates: -

- (a) primarily domestic/local benefits;
- (b) primarily global benefits;
- (c) joint benefits?

8. In meeting the challenge of distinguishing global and local benefits it was emphasized that while this distinction will always be difficult in the biodiversity context, it was important that the focus should be in identifying and funding activities associated with biodiversity of global importance. We should get away from global benefits versus local benefits and focus instead on "unique biodiversity from a global perspective". There were three suggestions made by the group to assist project proponents in the estimation of incremental costs.

9. The first suggestion was to have illustrative lists of activities, such as:
- (a) Activities which can be entirely attributed to securing global benefits (i.e. complementary/additional to the country) for which GEF will bear full costs;
  - (b) Activities which are entirely in the national interest for which GEF will not bear the costs;
  - (c) Activities which provide joint nature of benefits (burden, benefit and cost sharing called for): GEF will share in the cost of these through a negotiation and agreement process taking into account the information at hand.

These lists will be developed from a sample of existing project documents, and should be seen as "living lists" to which activities may be added or removed as experience is gained. It is recognized that ultimately it is the context that will decide whether the activities fall in one list or



the other, and these lists should be seen as “guides” and “not set in stone”. These lists should help simplify the application of the principle.

10. A second suggestion was made to take into account the time dimension. The rationale is that while all biodiversity will eventually generate national benefits (even if only in the form of existing or option values) in the short-term, GEF assistance is necessary and will produce global benefits. Therefore, the time dimension affects what is "GEFable" and what is not. A proposed definition is: "activities that generate a national benefit in the short term" (baseline) vs. "activities that do not generate a national benefit in the short term" (incremental). Evidently, this last category will allow for national benefits to be generated in the mid to long term (for example, strengthening parks which eventually may generate income via fees).

11. A third suggestion made by the group was that the French GEF experience should be explored further as a possibility of informing this process.

12. The group did not feel that the public involvement policy conflicted with incremental costs or vice-versa and that they followed two separate tracks.

#### *Feedback from the Climate Change Task Force*

13. The Climate Change Task Force discussed the following two questions posed by the Incremental Cost Task Force.

- (a) Are there special challenges to incremental cost estimation in projects with the private sector? Do we need to consider ranges of incremental cost estimates as opposed to a single number?;
- (b) How does one determine the baseline and sustainable development baseline? How does this relate to the application of the principles of leveraging, co-financing, cost-sharing and associated costs to incremental cost in the focal area? Should the baseline be defined in a qualitative or quantitative way?

14. The group spent more time discussing the first question than the second. The draft summary is presented below.

15. The primary hurdle with incremental cost estimation in projects with the private sector is the distinction between financial incremental costs (which are faced by the private sector) and the economic incremental costs which are faced by the country. The GEF finances the latter. Depending on the structure of national taxes, duties and subsidies, these two figures will generally be different.

16. The task force seemed to express a clear preference for presenting a range of incremental cost estimates at the time of work program inclusion rather than a single estimate. Projects would come in as a point estimate at the time of endorsement. The present system gives project

proposers an incentive to present projects at the top of the range. However, upon some reflection, it seems that presenting a range preserves the same incentive to come in at the top of the range at the time of endorsement. Finally, if there is residual uncertainty at the time of endorsement, a suggestion was made that the lower end of the range could be a grant and the difference between the top end and the bottom end could be offered on a contingent basis, However in practice the transactions cost of introducing contingent financing modalities that late in the project design may be intractable. The institutional arrangements required to monitor and disburse/collect the funds are non-trivial.

17. On the second question, the task force agreed that the procedure followed by the climate team--i.e., defining the cost of removing barriers to the movement from a business-as-usual baseline to a nationally sustainable development baseline as incremental costs could be adopted by the biodiversity focal area both in the interests of consistency and of harmony.

#### *Feedback from the IW Task Force*

18. The International Waters Task Force discussed the six conceptual challenges posed in the terms of reference toward the shared goal of simplified approaches to incremental cost. The task force felt that its approach with complementary and substitutional categories of projects and incremental cost analysis by component was pragmatic and relatively simple. The task force questioned the use of “sustainable development” baseline. In pragmatic terms, there is the “real baseline”, often zero or a minimal level of activities, there is the “leveraged baseline”(referred to as the “expected baseline” in the GEF Operational Strategy for international waters, and then there is the increment to solve the transboundary problem consisting of agreed activities with agreed incremental costs.

19. Answers to the 6 questions are as follows: -

- (a) by definition in the Operational Strategy if a transboundary issue is addressed, then primarily global benefits accrue;
- (b) in the case of joint benefits, the percentage of cost would be equivalent to the percentage of the problem that is being caused by the activity;
- (c) no feedback as yet;
- (d) yes, a range would be appropriate but the focal area has no experience with these;
- (e) many international waters projects do not involve local communities so this may not be applicable in many cases;
- (f) more use of complementary projects, such as Global International Waters Assessment.