

The Adaptation Fund

AFB/B.2/10
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Adaptation Fund Board
Second Meeting
Bonn, June 16-19, 2008

Agenda Item 6(h)

DRAFT ROLE AND RESPONSIBILITIES OF THE ADAPTATION FUND TRUSTEE

(Prepared by Invited Trustee)

1. The purpose of this document is to describe the proposed role and responsibilities of the trustee for the Adaptation Fund and related financial and fiduciary issues.

I. The World Bank as Trustee

2. In order for the International Bank for Reconstruction and Development (the World Bank) to serve as trustee for the Adaptation Fund (the Trustee), the institutional arrangements would need to be concluded between the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol and the World Bank pursuant to paragraph 31 of the decision 1/CMP.3. It is proposed that such arrangements be concluded by way of decision by the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol and the World Bank of approval and acceptance of the terms and conditions of services provided by the World Bank as the Trustee (the Terms and Conditions). The Trustee would commence provision of its services upon effectiveness of the Terms and Conditions.

II. Overview of Core Trustee Functions for the Adaptation Fund

3. The Trustee would fulfill four core functions for the Adaptation Fund: (i) sales of certified emission reductions (CERs) for the Adaptation Fund, (ii) financial management of the resources of the Adaptation Fund Trust Fund, (iii) investment management; and (iv) accounting and financial reporting. The Trustee would perform its functions consistent with its policies and procedures, and would be accountable to the Adaptation Fund Board for performance of its fiduciary responsibilities.

4. The core functions would include, but not be limited to, the following activities:

- i) Sales of CERs: engage in sale of CERs and provide reports on sale activity.
- ii) Financial management: manage the inflow of receipts from the sale of CERs; administer contributions from donors, if any; record Adaptation Fund Board approvals of allocations; record commitments and make cash transfers; manage reflows and currency conversions; manage cash flow; manage financial risk, including currency and interest risk rate risk management; and provide financial and operational controls over the resources held in the Adaptation Fund Trust Fund.
- iii) Investment management: invest funds based on a benchmark; periodically review risk profile and asset composition of benchmark; and allocate investment income to the Adaptation Fund Trust Fund on a monthly basis.
- iv) Accounting and financial reporting: maintain accounting records and financial data; provide required financial reports; prepare annual, audited financial statements; coordinate external audit of the Adaptation Fund Trust Fund, and monitor the quality and consistency of specified financial data provided by the Adaptation Fund Secretariat.

III. Operating Procedures

5. **Management of incoming funds:** The Trustee would establish a trust fund for the Adaptation Fund (the Trust Fund) to hold the funds, assets and receipts on behalf of the Adaptation Fund in accordance with the Terms and Conditions and the relevant decisions of the Conference of the Parties.

6. The Trustee would sell CERs in accordance with the guidelines provided by the Adaptation Fund Board and in a manner agreed between the Trustee and the Adaptation Fund Board. The Trustee would receive and hold any proceeds of CER sales in the Trust Fund.

7. In addition to the proceeds of CER sales, the Trustee may accept monetary contributions from donors to support the operations of the Adaptation Fund, if so requested by the Adaptation Fund Board. The Trustee would enter into, with each donor, trust fund administration agreements, which would set out the terms and conditions applied to administration and management of the contributions.

8. **Investment management:** In accordance with the policies and procedures of the World Bank, the trust fund resources would be kept separate and apart from the assets of the World Bank, but may be commingled with other trust fund assets maintained by the World Bank for administrative and investment purposes. The World Bank would, however, keep separate accounts and ledgers for the resources held in the trust fund. Pending transfer of funds to recipients, the World Bank would invest funds held in the Trust Fund in such form as it may decide, including pooled investments (in which separate accounts shall be held for the funds of the Trust Fund) with other funds administered by it. Investment income earned would be credited to the Trust Fund, thereby increasing resources available to finance the operations of the Adaptation Fund.

9. **Allocation, Commitment and Transfer of Funds:** The Adaptation Fund Board may approve the allocation of Adaptation Fund resources for programs, projects, administrative budget, and such other activities, subject to the amount of unallocated resources held in the Trust Fund¹. To avoid approval of funding in excess of the resources held in the Trust Fund, the Trustee would prepare and furnish the Adaptation Fund Board with periodic reports on status of commitments and transfers of Trust Fund funds and such other financial information, as the Trustee may deem appropriate. The Trustee would, subject to the availability of resources held in the Trust Fund, record commitments and make transfers of funds from the Trust Fund, in a manner agreed between the Adaptation Fund Board and the Trustee. Further, such commitments and transfers would be made only at, and in accordance with, the written direction provided to the Trustee by the Adaptation Fund Board or such other person designated by the Adaptation Fund Board for this purpose. Upon transfer of funds, the Trustee would have no responsibility for the use of Trust Fund funds transferred and activities carried out therewith.

10. The Adaptation Fund Secretariat would ensure that the Trustee receives all information necessary in order to carry out its responsibilities

¹ These resources include liquid assets derived from the sales of CERs, donor monetary contributions, and realized investment income.

IV. Limited Fiduciary Responsibilities by the Trustee

11. The role and responsibilities of the Trustee would be limited to the World Bank's policy and standards to manage trust funds as well as auditing and financial reporting.

12. In its role as trustee for the Adaptation Fund, the Trustee's responsibility would be limited to the prudent management of the funds held in its trust, including sales of CERs, financial management and sound investment of funds from CER sales, recording commitments and making cash transfers of these funds at the instruction of the Adaptation Fund Board or such other person designated by the Adaptation Fund Board for this purpose, and the provision of regular reports and maintenance of accounting records and financial data, in accordance with the Terms and Conditions. The Trustee would not supervise activities of implementing or executing entities, or any other recipients of Adaptation Fund resources, nor would it supervise the use of funds by such entities. Accordingly, the Trustee would have no responsibility for the use of resources once they are transferred by the Trustee.

13. The Conference of the Parties serving as the meeting of the Parties to the Protocol would agree that the trustee would be indemnified, out of the assets held for the Adaptation Fund, including the Adaptation Fund resources, from any liabilities, claims, losses, costs and expenses brought against or suffered by the Trustee, without gross negligence or willful misconduct on its part, in connection with carrying out its activities as the trustee, including sales of CERs.

Budget for Trustee Services for the Adaptation Fund

1. The Trustee would provide a range of standard services to the Adaptation Fund. These services include as needed: (a) sales of CERs; (b) financial management; (c) investment management; (d) management of partner relationships; (d) accounting and reporting; (e) legal services; and (f) provision of infrastructure and systems.
2. Reasonable expenses incurred by the Trustee performing its functions would be reimbursed on a full cost recovery basis from the Adaptation Fund. This is consistent with the World Bank's policy to recover its full costs in the provision of trustee and administrative services. The reimbursement would be made on the basis of estimated cost, subject to end-of-year adjustment.
3. The World Bank will contribute the costs associated with its work undertaken up to June 30, 2008, currently estimated at \$377,000.

Proposed Budget for Trustee Services: July 1, 2008 to June 30, 2009

4. Presented to the Adaptation Fund Board in Table 1 below is the projected budget for trustee services between July 1, 2008 and June 30, 2009.
5. The proposed budget represents the following assumptions:
 - i) Sales of CERs: Estimates would be provided as more information is available;
 - ii) Financial management: The amount required to cover costs for this activity would be dependent on whether sales of CERs begin in FY09, the level and financing and the number of projects approved by the Adaptation Fund Board, and the complexity of operational procedures for recording allocations, commitments and making cash transfers to recipients;
 - iii) Investment management: Investment management fees would be calculated based on a cost of 3.5 basis points against the average, annual balance of the portfolio; the projected average portfolio size for the Adaptation Fund Trust Fund for FY09 is \$30 million;
 - iv) Relationship management: These costs would include staff time related to participation in meetings; collaboration with the Adaptation Fund Board and the Secretariat to develop best practice operational policies relating to financial transactions; and development of robust and efficient reporting and transactional processes and procedures for the Trust Fund. These costs are normally higher in the early years of a trust fund when significant senior staff time is required;

- v) Accounting and reporting: Costs would be based on the assumption that an audited financial statement would be required for FY09; also included would be costs associated with establishing the accounting model to be used for the Adaptation Fund;
- vi) Legal services: Costs would include the establishment of the Trust Fund and for legal advice on sales of CERs. Also included would be the cost of contractual services for outside legal counsel on the issues of providing legal personality to the Adaptation Fund and selling CERs under security trading regulations;
- vii) External audit: This assumes that the Bank would arrange for an external audit of the financial statements of the Trust Fund during FY09;
- viii) Travel: 4 staff to attend 2 Board meetings each; 4 staff to attend COP/MOP meeting in December 2008.

Table 1: Budgetary Requirements for Services Provided by the Trustee in USD

Trustee Services	FY09 Proposed Budget
Sales of CERs ***	***
Financial Management	140,100
Investment Management	10,500
Relationship Management	274,200
Accounting and Reporting	147,500
Legal Services	157,800
External Audit	90,000
Estimated travel costs	124,000
<u>Total Costs</u>	<u>944,100</u> ***
*** This does not include a projection for sale of CERs	