



# Global Environment Facility

## Summary of Document GEF/ME/C.30/2

### Evaluation of Incremental Cost Assessment

#### **Recommended Council Decision**

The Council, having reviewed the document GEF/ME/C.30/2 Evaluation of Incremental Cost Assessment, and the management response (GEF/ME/C.30/3), takes note of the conclusions of the evaluation. The Council particularly welcomes the conclusion that the principle of incremental funding is being achieved throughout the GEF.

On the basis of the evaluation's conclusion that the process of incremental cost assessment and reporting does not add any value to the quality of projects, the Council agrees that:

1. the current incremental cost assessment and reporting should be dropped as requirements for GEF projects;
2. the incremental reasoning in project objectives and design should be explicitly recognized in appropriate documentation, particularly at the project concept stage, during implementation and at completion;
3. on-going efforts need to be strengthened to have a better identification of global environmental benefits in GEF activities, including improved dissemination and raising of awareness of the focal area strategic priorities and objectives.

The Council requests the GEF Secretariat to incorporate this decision into the paper on operational guidelines for the application of the incremental cost principle in GEF operations to be presented to Council in June 2007. The Council also requests the GEF Evaluation Office to record any follow up actions taken to implement these decisions and to report on these actions through the Management Action Record.

#### **Executive Summary**

1. Incremental cost funding is the fundamental operational principle of the GEF. The GEF finances the increment or additional costs associated with transforming a project with national/local benefits into one with global environmental benefits as well. The 'principle' of incremental cost funding was originally envisaged to ensure that GEF funds do not substitute for existing development finance but provide new and additional funding to produce agreed global environmental benefits. Its application has been recognized as complex and not transparent by all of those involved in the GEF.

2. The primary objectives of this evaluation were to evaluate the processes and methodologies used for incremental cost assessment, and the process of negotiation of incremental costs. In line with these objectives, the following dimensions of incremental cost were evaluated: the incremental cost annex reporting, the process of incremental cost assessment, the process of negotiation and the methodologies, approaches and requirements for incremental cost assessment and reporting in order to determine whether these are appropriate and sufficient. The evaluation also conducted an assessment of the evolution of the incremental cost concept in relationship to financing global environmental benefits (within the context of Agenda 21) and how its application evolved within the GEF.

3. The evaluation used a series of approaches and tools to collect and analyze information, including quantitative (e.g., structured survey questionnaires) and qualitative (e.g., semi-structured interviews): literature review, review of all projects approved in 2005 from the point of view of compliance with guidelines and procedures and technical quality of the incremental cost assessment and reporting, an on-line survey to gather opinions from a broader set of stakeholders, and interviews with fifty-five key people involved with GEF project design and review. The evaluation reached four main conclusions and three recommendations.

4. First conclusion: **the principle of incremental funding is alive and well in GEF projects.** Although the evaluation found many doubts and concerns expressed about the process of incremental cost assessment as it is carried out, the evaluation found that incremental reasoning underpins the global environmental focus of the design of GEF projects. This reasoning takes place at the concept phase, well before the process of incremental cost assessment, and it ensures agreement on the global benefits and the ways in which the project will secure these benefits and provide additional funding to cover their incremental costs.

5. Second conclusion: **there remains weak understanding and much confusion about incremental cost concepts and procedures.** Confusion still persists on whether incremental cost is a (primarily qualitative) form of logic or reasoning, or a quantitative, numerical calculation. Specific terms associated with incremental cost were also found to be poorly understood, most notably “incremental cost”, “alternative,” “system boundary” and “additionality”. GEF guidance throughout the years never clarified if they substitute for or add to previous ones, adding to the confusion of what is required.

6. Third conclusion: **most project documents register low quality and compliance when measured against GEF requirements for incremental cost assessment and reporting.** The evaluation found that 64 % of projects only report on half of the six aspects of incremental cost that are required by policy and guidelines (broad development goals and baseline, alternative, and cost). One of the reasons the compliance quality is low is because the GEF incremental cost guidelines that lay out the background to incremental cost assessment and the requirements for annex reporting in project documents are rarely used, and there is an absence of commonly-accepted “best practice” for incremental cost assessment.

7. Fourth conclusion: **as currently applied, incremental cost assessment and reporting do not add value to project design, documentation and implementation.** The bulk of effort is expended on reporting on incremental cost as a required part of the project document rather than connecting it to the project design. The preparation of the annex is usually carried out ex post facto, at the end of project formulation, by experts. The annex serves merely to summarize or repeat the information contained in the main text of the project document.

8. First recommendation: **incremental cost assessment and reporting should be dropped as requirements for GEF projects.** A shift is required away from the cumbersome, complex and not always useful steps of incremental cost assessment to a focus on integrating incremental reasoning into project objectives and design. Therefore, the incremental cost assessment and reporting requirements should be dropped from the project design and reporting process, in particular the requirement for an incremental cost annex, section, and incremental cost matrix in project documents.

9. Second recommendation: **incremental reasoning in project objectives and design should be acknowledged and recognized, in particular at the project concept stage, during implementation and at completion.** This evaluation shows that the current practice of projects in the GEF is to follow incremental reasoning to ensure that the GEF funding of these projects is (a) directed towards achieving global environmental benefits and (b) additional to existing funding levels. Full accountability for the incrementality of GEF funding would be achieved, during implementation and project completion by monitoring and evaluating for progress towards achieving global environmental benefits and for levels of co-funding.

10. Third recommendation: **the process towards better identification of global environmental benefits needs to be strongly supported, including improved dissemination and awareness-raising on focal area strategic priorities and objectives.** The only way to strengthening integration of incremental reasoning is by providing full clarity and transparency on global environmental benefits that are expected from projects through a better definition and focusing of the focal area objectives and strategies. If there are no clear global environmental benefits incremental reasoning cannot be done and the concept should not be considered a GEF project.

11. The rationale for these conclusions and recommendations is that as currently applied, incremental cost assessment and annex reporting procedures do not enhance either the technical quality of GEF projects, the process of negotiation and agreement that is fundamental to project design and decision-making, or the integration of incremental reasoning and other GEF principles. The original idea that it would be possible to develop a quantitative “methodology” which would be universally applicable and would meet the ambitious goals of determining incremental cost and structuring its negotiation was clearly unrealistic. In reality, and as currently required and applied, it has undermined (or at the best played little role in) the process of determining incremental cost in GEF projects. A great deal of time, effort and project preparation budget are expended on fulfilling minimum reporting requirements, rather than using incremental cost assessment as a tool to aid in the design of better projects. The evaluation finds that the projects reviewed satisfactorily incorporate the principle of incrementality through incremental reasoning, are targeted at securing global benefits and attracting additional funding – but this is in spite of incremental cost analysis, not because of it. There is no apparent value added from incremental cost assessment and annex reporting requirements as laid out by GEF.

12. The full evaluation report, containing detailed analysis and background information, is available at the GEF Evaluation Office website ([www.thegef.org](http://www.thegef.org), then go to Evaluation Office, On-going Evaluations and then Evaluation of Incremental Cost Calculation).