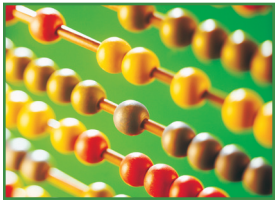


Evaluation of Incremental Cost Assessment



One of the founding operational principles of the Global Environment Facility (GEF) is incremental cost—the increment, or additional,

costs associated with transforming a project with national/local benefits into one with global environmental benefits. The operational principle of incremental cost 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.

The operationalization of the incremental costs principle has been one of the “black boxes” of the GEF for many country stakeholders. There has been much confusion concerning the interpretation of incremental cost assessment: is it a numerical calculation used to determine project funding or a qualitative assessment used to justify prearranged funding amounts? Moreover, the lack of transparency in the process and its frequent domination by international consultants was repeatedly cited by country stakeholders.

In June 2005, the GEF Evaluation Office proposed to and agreed with the GEF Council that a short and focused evaluation of incremental cost assessment be undertaken. This evaluation would build on the findings from the focal area program studies and the evaluation of the Role of Local Benefits in Global Environmental Programs. The evaluation would also complement other activities in the GEF Evaluation Office’s work program such as its Joint Evaluation of the GEF Activity Cycle and Modalities.

The primary objectives of the incremental cost evaluation were to evaluate the processes and methodologies used for incremental cost assessment and the process of negotiation of incremental costs. Four dimensions were evaluated: (1) incremental cost annex reporting, in terms of quality and compliance with GEF guidelines; (2) the process of incremental cost assessment, in terms of its op-

erational approach, conduct, and content; (3) the process of negotiation with regard to who is involved and what is negotiable/negotiated at each of the key stages of project identification, preparation, and design; and (4) the methodologies, approaches, and requirements for incremental cost assessment and reporting to determine whether these are appropriate and sufficient (both as they are reflected in GEF guidance documents and as they are actually applied in project design).

The evaluation used both quantitative and qualitative approaches to address the four dimensions and derive its findings.

Findings

Four major conclusions were drawn with regard to incremental costs.

- **The principle of incremental funding is alive and well in GEF projects.** A process of incremental reasoning or logic (a qualitative and implicit process) is used to justify and agree on (or negotiate) global benefits and the selection of actions that a project will take to achieve them. This occurs early in the project design phase and is related to the setting of objectives and outcomes. Interestingly, the evaluation found that the linkage between incremental reasoning and incremental cost assessment was questionable.
- **There remains weak understanding and much confusion about incremental cost concepts and procedures.** A great variation in understanding of concepts and principles underlying incremental costs exists among the various stakeholders in GEF projects, along with widely differing interpretations of the role of incremental cost assessment. A major area of confusion was whether incremental costs are primarily a qualitative form of reasoning or a quantitative numerical calculation. The GEF Secretariat has made several attempts

to provide guidance, but these multiple sets of guidance have exacerbated the confusion of stakeholders. Few stakeholders have received incremental cost training or outreach to the stakeholders involved in project design and decision making.

- **Most project documents register low quality and compliance when measured against GEF requirements for incremental cost assessment and reporting.** One of the main reasons compliance quality is low is because the GEF guidelines that set out the requirements for annex reporting in project documents are rarely used, and there are no commonly accepted best practices for incremental cost assessment. The evaluation found that even where Implementing Agencies and project proponents were aware of the guidelines they found them to be “academic,” “jargon-filled,” and “complex” and exhibiting a persistent lack of transparency and clarity; the guidelines were spurned in favor of the use of previous project examples (“case law”) in shaping projects to satisfy GEF requirements. While the use of case-based learning has increased the opportunities for personal and context-specific interpretations of incrementality, it cannot provide adequate guidance on how the assessment is carried out and reported.
- **As currently applied, incremental cost assessment and reporting do not add value to project design, documentation, and implementation.** Complying with minimum requirements for incremental cost reporting does not guarantee a quality project. Clarity of incremental reasoning at the concept phase and clear identification of global environmental benefits do. The evaluation found there was limited comprehension by those involved in project preparation of incremental cost assessment as a process that influences project design. Rather, most effort is expended on reporting on incremental cost as a requirement of the project document. Preparation of the assessment is usually completed ex post facto, at the end of project preparation, in a manner largely divorced from the project design and stakeholders. The incremental cost annex was widely seen as a “hoop to be jumped through” rather than a

useful tool in project preparation. Further, incremental cost assessment had very little influence on project negotiation and financing, as this is decided prior to the assessment.

Recommendations

The evaluation provided three recommendations:

- Incremental cost assessment and reporting should be dropped as requirements for GEF projects.
- Incremental reasoning in project objectives and design should be acknowledged and recognized, in particular at the project concept stage, during implementation, and at completion.
- The process toward better identification of global environmental benefits needs to be strongly supported, including improved dissemination and awareness-raising on focal area strategic priorities.

Follow-Up

The management response endorsed the recommendations. The GEF Council discussed the evaluation and management response and decided to request that the GEF Secretariat present reformed guidelines to result in a simplified demonstration of the project baseline, incremental costs, and cofunding. The Secretariat presented “Operational Guidelines for the Application of the Incremental Cost Principle” to the GEF Council in June 2007; these were endorsed by the Council. The guidelines focus on ensuring incremental reasoning during project design and respond to the evaluation recommendations.

The GEF Evaluation Office is an independent entity reporting directly to the GEF Council, mandated to evaluate the focal area programs and priorities of the GEF.

The *Evaluation of Incremental Cost Assessment* (Evaluation Report No. 34, 2007) is available on the GEF Evaluation Office Web site at www.thegef.org (in the Publications section). For more information, please contact the GEF Evaluation Office at gefevaluation@thegef.org.