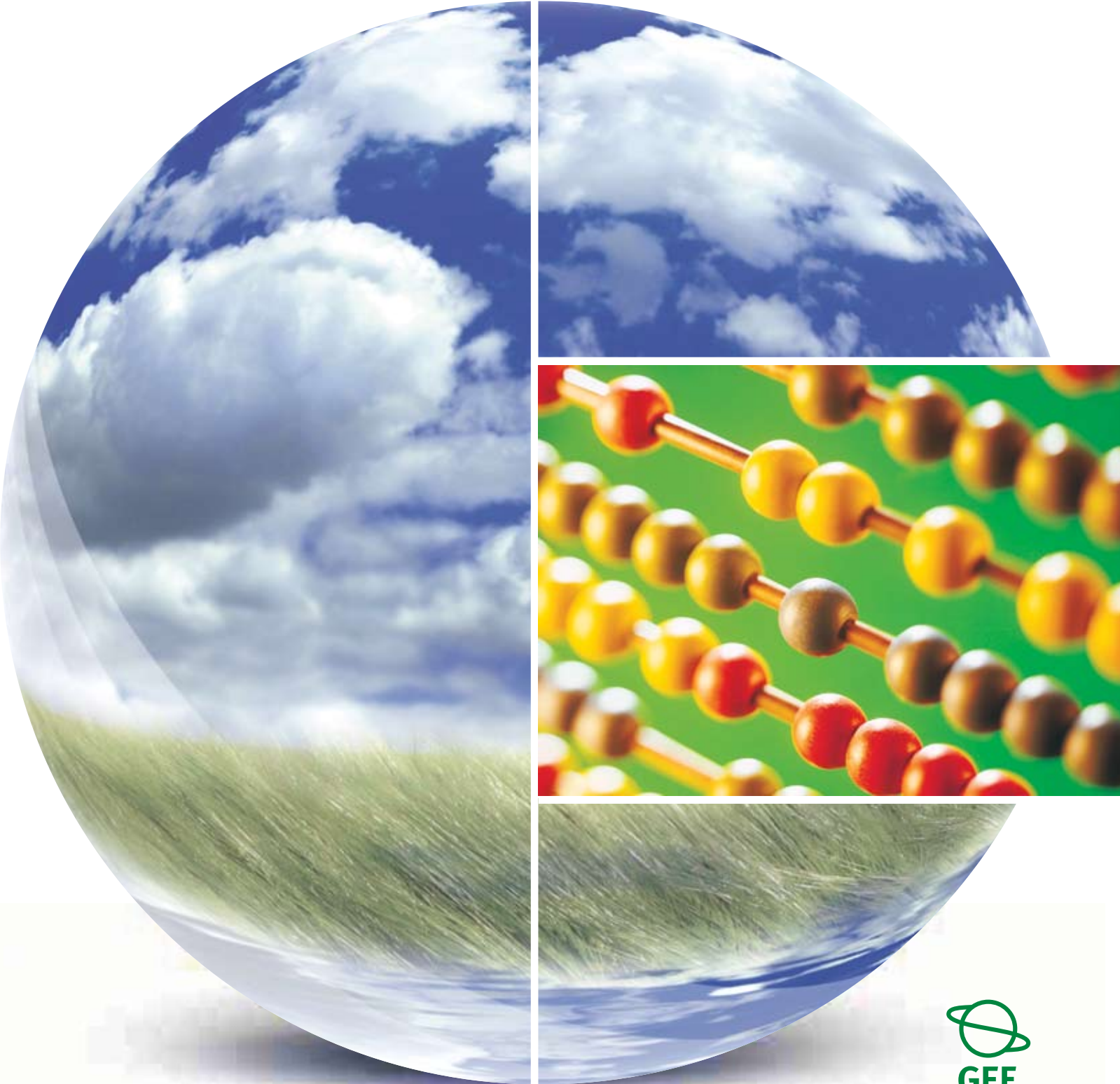


Evaluation of Incremental Cost Assessment



**Global Environment Facility
Evaluation Office**

Evaluation of Incremental Cost Assessment

May 2007

(The main findings and recommendations of this evaluation were presented to the GEF Council in December 2006.)

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Abbreviations

CAQDAS	computer-assisted qualitative data analysis	PMIS	Project Management Information System
CEO	Chief Executive Officer	POP	persistent organic pollutant
COP	conference of the parties	PRINCE	Program for Measuring Incremental Cost for the Environment
FAO	Food and Agriculture Organization of the United Nations	RAF	Resource Allocation Framework
FSP	full-size project	UNDP	United Nations Development Programme
GEF	Global Environment Facility	UNEP	United Nations Environment Programme
IA	Implementing Agency	UNCBD	Convention on Biological Diversity
MSP	medium-size project	UNCCD	United Nations Convention on Combating Desertification
NGO	nongovernmental organization	UNFCCC	United Nations Framework Convention on Climate Change
OPS	overall performance study		

One of the founding operational principles of the Global Environment Facility (GEF) is incremental cost—which is 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. Its application has been recognized as complex and not transparent by many, if not all, GEF stakeholders. Furthermore, it has been identified in several evaluations conducted by the GEF Evaluation Office as an issue that needs further clarification.

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

At the outset of the evaluation our Office expected that this evaluation was going to provide direct feedback to the development of new guidelines

by the GEF Secretariat, as requested by the negotiations for the fourth replenishment of the GEF. Furthermore, we expected that the evaluation would provide best practices, guidelines on how to improve the assessments, and how to deal with complex methodological issues.

However, the evaluation team quickly discovered that the methodological issues were irrelevant to the incrementality of GEF funding. Incrementality of the GEF is not achieved through the assessment, which is conducted mostly at the end of the project design (and does not usually affect the design), but through the initial negotiation that takes place between the GEF agents and the recipients in the definition of the baseline and the global environmental benefits that will be produced in the project.

The first chapter of the report provides the key findings and recommendations of the evaluation. This chapter was the basis for discussions in the December 2006 Council meeting. The Council in general agreed with the findings and recommendations, and concluded that the current process for incremental cost assessment and reporting does not add any value to the quality of GEF projects. The Council decided that the incremental reasoning in project objectives and design should be explicitly addressed in appropriate documentation; that the current incremental cost assessment and reporting requirements for GEF proposals should

be reformed; and that progress toward achieving global environmental benefits and for achieving cofinancing should be monitored throughout the life of the project, particularly at project end. The GEF Secretariat has been requested to present these reforms of incremental cost assessment and reporting at the June 2007 Council as part of the revised Activity Cycle.

The evaluation was undertaken by staff from the Evaluation Office, together with consultants. The managers were Claudio Volonte, Chief Evaluation Officer, and Lee Alexander Risby, Evaluation Officer; they led the evaluation design, data collection and analysis, and report writing process. The lead consultant for the evaluation was Lucy Emerton, Senior Natural Resource Economist with IUCN Sri Lanka. She participated in field missions and performed a key role in the analysis and report writing. Neeraj Negi, Evaluation Specialist from the GEF Evaluation Office, provided the quantita-

tive analyses related to the compliance questions. Other consultants dealing with analyses related to each of the GEF focal areas included Alain Lafontaine of Baastel Ltd, Laurence Mee and Tristram Wickham-Lewis of Plymouth University, and Sam Fujisaka of the Center for International Tropical Agriculture.

I would like to thank all stakeholders from the Implementing and Executing Agencies and representatives from recipient countries for providing their time to the team and helping us understand the issues involved in incremental cost assessment. The GEF Evaluation Office bears sole responsibility for this evaluation.

A handwritten signature in black ink, appearing to read 'Rob D. van den Berg', with a large, stylized flourish extending to the right.

Rob D. van den Berg
Director, Evaluation Office

1. Main Findings and Recommendations

1.1 Introduction

The Global Environment Facility (GEF) functions as a mechanism for international cooperation to provide new and additional funding to meet the agreed incremental costs of securing global environmental benefits. It works in partnership with the GEF Implementing Agencies (IAs)—the United Nations Development Programme (UNDP), the United Nations Environment Programme (UNEP), and the World Bank—seven Executing Agencies, national governments, and civil society.¹

Incremental cost is the fundamental operational principle of the GEF. The GEF funds the increment, or additional costs associated with transforming a project with national/local benefits into one with global environmental benefits. The 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. Its application has been recognized as complex and not transparent by the GEF Council, the Secretariat, and the IAs, as well as by project proponents, governments, and nongovernmental organizations (NGOs). Furthermore, it has been identified in several evaluations conducted by the GEF Evaluation Office as an issue that needs further clarification.

In June 2005, the Evaluation Office proposed to the GEF Council to carry out a short and focused

evaluation of how incremental cost calculations have been undertaken in GEF projects and what can be learned from the application of the methodology so far, building on findings from the focal area program studies and the recently completed evaluation of the Role of Local Benefits in Global Environmental Programs. The evaluation complements other activities in the GEF Evaluation Office's work program such as the Joint Evaluation of the GEF Activity Cycle and Modalities, and country portfolio evaluations.

The present evaluation is a response to recommendations from several previous studies (for example, the Second and Third Overall Performance Studies, the Biodiversity Program Study); the November 2005 Council decision regarding the evaluation of the role of local benefits; and the GEF-4 donor replenishment agreement that requests the GEF Secretariat and GEF Agencies to prepare for the June 2007 Council meeting clearer operational guidelines for the application of the incremental cost principle in GEF operations, taking into account the findings and recommendations of this evaluation.

1.2 Scope and Methodology

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. In line with these objectives, the following dimensions of incremental cost were evaluated:

- The **incremental cost annex reporting**, in terms of its quality and compliance to GEF guidelines
- The **process of incremental cost assessment**, in terms of its operational approach, conduct, and content (the process of conducting the incremental cost assessment)
- The **process of negotiation** according to who is involved and what is negotiable/negotiated at each of the key stages of project identification, preparation, and design
- 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 also conducted an assessment of the evolution of the incremental cost concept in relation to financing global environmental benefits (within the context of Agenda 21) and how its application evolved within the GEF.

Finally, the evaluation interpreted these findings in order to draw conclusions and make recommendations to be presented as feedback to the GEF Council and evidence-based inputs into the forthcoming work of the GEF Secretariat and Agencies.

The evaluation used a series of approaches and tools to collect and analyze information, including both quantitative (such as structured survey questionnaires) and qualitative (including semi-structured interviews) methods. The quantitative methodologies were primarily employed to solicit information on *what* the GEF Activity Cycle was doing with regard to the incremental cost assess-

ment (process) and annex (product). The qualitative methodologies were employed to obtain information on *how* and *why* certain processes or procedures were followed or not, and also on conceptual aspects such as incremental reasoning and use of project case law.

Both quantitative and qualitative data were analyzed in isolation and then verified in order to highlight similarities and differences across findings and reduce threats to validity. Particular attention was given to the assessment and interpretation of the qualitative data using computer-assisted qualitative data analysis (CAQDAS) software—Atlas-ti.

Five approaches were used that provided distinct but related data sets and covered a range of stakeholder groups, information types, and information-gathering techniques, so as to provide as comprehensive a picture as possible of incremental cost conduct and content (see annexes C and D).

- **Literature review.** A review of the incremental cost concept and non-GEF use of incremental cost assessment, as well as of existing evaluative and non-evaluative GEF reports, was done to establish key issues, advantages, and disadvantages of the incremental cost approach and its application. A review of other global programs' financial and economic decision-making tools was also conducted, including interviews with staff from the Global Fund to Fight AIDS, Tuberculosis and Malaria (see annex A).
- **Compliance review.** The compliance review assessed the extent to which projects are actually complying with the requirements for incremental cost assessment and reporting as established by Council guidance, especially by the GEF project review criteria (approved by the Council in 2000), at the point of Chief Executive Officer (CEO) endorsement or approval.

In all, 140 projects were reviewed, including 79 full-size projects (FSPs) that had been CEO endorsed and 61 medium-size projects (MSPs) that had been CEO approved in 2005.

- **Technical quality review.** Project documents and executive summaries were reviewed to conduct an in-depth assessment of the technical quality of incremental cost assessment and reporting. A stratified random sample of 86 projects was selected from among the biodiversity, climate change, international waters, land degradation, and multifocal area projects that had reached the stage of CEO endorsement. The sample represents 59 percent of all 2005 CEO-endorsed GEF-3 projects in these focal areas.
- **Online survey.** The online survey was designed using existing experiential information on incremental costs and data inputs from 8 to 10 semi-structured interviews. A questionnaire instrument based on these documents and data was developed to assess the perceptions of stakeholders on the various incremental cost elements. The instrument was administered online through www.surveymonkey.org. The target group for this survey comprised those involved in the design, review, implementation, and/or supervision of GEF projects. The targeted population was contacted primarily via an email request to fill out the survey. The survey was opened on June 13, 2006, and closed on July 31, 2006. During this period, 159 respondents participated in the survey. Of these, 119 respondents (75 percent) completed the survey, while 40 (25 percent) dropped out without completing it. Of the respondents that completed the survey, 30 percent were from IAs; 27 percent were from the Scientific and Technical Advisory Panel roster; 10 percent were independent consultants; 8 percent were national focal points; and the remaining

24 percent were split among respondents from the GEF Secretariat, international and national NGOs, national government agencies, and bilateral and other multilateral institutions.

- **Interviews.** Interviews based on a common protocol were conducted with 55 key people involved in GEF project design and review. The semi-structured interview protocol was designed to provide information on how incremental cost assessment was carried out, by whom, and why certain procedures were used. Interviews provided an interactive mechanism for “ground-truthing” and elaborating the results of the online survey and compliance and technical quality reviews: they enabled these findings to be explained, described, and verified in detail. A purposive/snowball sampling method was employed to ensure that there was representation of key stakeholders such as the GEF Secretariat, IAs, convention secretariats, incremental cost consultants, and project proponents. Interviews were conducted between May 1 and July 31, 2006. The evaluation team undertook three field missions to Kenya, Malaysia, Panama, and Thailand to solicit responses from IA staff and project proponents who had experience with preparing projects in those countries/regions.

1.3 Conclusions

Conclusion 1: 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, it also found that incremental reasoning underpins the global environmental focus of GEF project design. Incremental reasoning takes place at the concept phase, well before the process of

incremental cost assessment takes place (during project design and drafting of the project document). Incremental reasoning was confirmed to be used (mostly implicitly) to justify and agree on the global benefits—and the ways in which the proposed GEF project will secure these benefits—and provide additional funding to cover their incremental costs.

Most of the projects reviewed have satisfactorily incorporated incremental reasoning within the objectives, scope, and outcomes, including securing funding for global environmental benefits. This finding is based on qualitative assessments as well as on high levels of compliance and quality of reporting in project documents and incremental cost annexes on presenting global environmental benefits, linking the global environmental objective, GEF mandate, and focal area priorities.

Although the evaluation found that incremental reasoning is the guiding principle for GEF projects, the linkage to the process of incremental cost assessment as it is currently carried out is questionable.

Conclusion 2: There remains weak understanding and much confusion about incremental cost concepts and procedures.

There is great variation in understanding of the concepts and principles underlying incremental costs by the various stakeholders in GEF projects, and widely differing interpretations of the role of incremental cost assessment in project conceptualization, design, and implementation. A major area of confusion concerns whether incremental cost is a (primarily qualitative) form of logic or reasoning, or a quantitative, numerical calculation, with IA staff favoring the first interpretation, and other stakeholders—such as some Council members—

tending to emphasize quantitative aspects. Specific terms associated with incremental cost were also found to be poorly understood, most notably “incremental cost,” “alternative,” “system boundary,” and “additionality.” Furthermore, guidance developed after the initial policy has omitted fundamental components of incremental cost such as the reference to “full” incremental cost and the idea that incremental cost includes any cost savings on the replaced or redundant activity.

The 1996 policy sets out the basic steps required in incremental cost assessment and specifies reporting requirements (GEF 1996). Subsequent guidance was provided by the 1999 streamlined procedures and principles for the agreement of incremental costs (GEF 1999a, 1999b). In addition, GEF task forces have made efforts to provide focal area-specific guidance for international waters, climate change (adaptation), and land degradation. Stakeholder understanding of incremental cost assessment, already weak, has in many cases been further undermined by the accumulation of these multiple and additive sets of policies and guidelines which sometimes make conflicting or contradictory recommendations. Lack of clear Council or GEF Secretariat guidance on which policies or guidelines take precedence has exacerbated this confusion and left too much room for personal and institutional interpretation.

Few stakeholders (especially from government counterpart agencies and national NGOs, but also including IA staff) have received formal guidance or training in incremental cost concepts or procedures. The evaluation found little evidence that the GEF has attempted to coordinate and build understanding through training, outreach, and dissemination of documents to the IA staff, project proponents, and government agencies involved in project design and decision making.

Conclusion 3: Most project documents register low quality and compliance when measured against GEF requirements for incremental cost assessment and reporting.

Key incremental cost concepts and elements of assessment are frequently misrepresented or misunderstood, or suffer from weak analysis and description. The evaluation found that 64 percent of projects report on only half of the six aspects of incremental cost that are required by policy and guidelines (broad development goals and baseline, alternative, and costs). Furthermore, incremental costs are not always presented as a separate chapter or annex in project documents as is also required. Reporting on the process of agreement, scope of analysis (or system boundary), and global environmental benefits is absent or not dealt with adequately by more than 75 percent of the incremental cost annexes reviewed.² The evaluation also found weaknesses or omissions among a high proportion of projects in terms of poor or misrepresented baseline scenarios, sketchy treatment of socioeconomic and distributional concerns, lack of any economic analysis of costs, and failure to justify the project as the least-cost option.

Although there are few differences in the overall technical quality of incremental cost annexes among the different IAs and focal areas, it is clear that each has different areas of emphasis, strength, and weakness in incremental cost assessment. These differences are revealed in particular sections of the incremental cost reporting. For example, for the cohort of projects reviewed, UNDP was more systematic in preparing a separate incremental cost annex for MSPs (about two-thirds of these project documents had an incremental cost annex). Project proponents involved in biodiversity and land degradation projects reported challenges in creating baselines of “stand-alone” projects. The UNEP and biodiversity projects reviewed were particularly weak in analyzing the

redistributional and socioeconomic effects of the GEF alternative. Only half of the MSP project documents include an incremental cost matrix. Although projects rarely specified costs in present value terms, the few that did were prepared by the World Bank, and included financial and economic appraisals. About 90 percent of the IA staff interviewed were not aware that there was a requirement to report on the process of agreement of incremental costs, and only 17 percent of projects reported on this issue adequately or better.

One of the reasons the compliance quality is low is because the GEF incremental cost guidelines that set 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 practices for incremental cost assessment. The evaluation found that even when IA staff and proponents are aware of these guidelines, they did not consider them to be useful or relevant. The guidelines are perceived as too complex, academic, and jargon-filled, leading to difficulties in application; as well as exhibiting a persistent lack of transparency and clarity, leaving too much room for personal and institutional interpretation. At best, the policy and guidance seem to function only as an initial reference point for ascertaining conceptual terminology and definitions—but even then, there are problems in understanding the guidelines.

The application of the incremental cost principle has evolved by focal area, each of which has developed its own approaches for assessing incremental costs. No clear consistency in application was found, although all areas tried to deal with the issue of incrementality. The GEF Secretariat’s Program for Measuring Incremental Cost for the Environment (PRINCE), which had the objective of developing “a broad interpretation of incremental cost that is consistent across the GEF

focal areas” (King 1993) was canceled in 2003 (after being inactive since 1999) without achieving either this objective or its aim to disseminate its findings, although a large amount of financial resources was still available.

In practice, incremental cost assessment and annex reporting are guided primarily by reference to previous project examples—often termed “case law.” Use of case-based learning has increased the opportunities for personal and context-specific interpretations of incrementality. While the use of previous project documents has clear advantages in terms of providing real-world examples, it cannot provide adequate guidance on how incremental cost assessment is carried out and reported. Widespread use of a relatively small number of “successful” project documents as a model for best practice has also, in some cases, exacerbated the perpetuation of particular misinterpretations and omissions in incremental cost assessment, resulting in a “cut-and-paste” approach to annex reporting. Case law examples are not available to the public at large, and their selection is based on the fact that they were successful in getting through the review process—which is not necessarily the best assurance of the quality of specific assessments.

Conclusion 4: 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 incremental cost assessment, as a process, and annex, as a product, do not necessarily reflect project objectives, overall design, and focus on sustainability.

Project Design and Preparation

The evaluation found that there was limited comprehension by those involved in project preparation of incremental cost assessment as a process that forms a part of project preparation and design. Rather, the bulk of effort is expended on reporting on incremental cost as a required part of the project document. The preparation of the annex is usually carried out ex post facto, at the end of project formulation, in a manner that is largely divorced from the project design and stakeholders. There is a widespread view that the incremental cost annex is a “hoop to be jumped through,” rather than a useful or influential tool in project preparation.

In the majority of cases, the incremental cost annex does not present new information or insights. It serves merely to summarize or repeat information contained in the main text of the project document. This brings into question its utility as a stand-alone component of the project document.

Estimating GEF Financial Support

As expected, the GEF is not the only source of funding to cover incremental cost; on average, the GEF contributes about 40 percent of the total incremental cost. The evaluation found that some focal areas have developed more formalized or standardized approaches to estimate the GEF contribution to the incremental cost of a project, such as cofinancing ratios (international waters), sliding scales (for funding adaptation to climate change projects under the Least Developed Countries Fund), and cost-sharing arrangements (land degradation). The incremental cost assessment itself is not used to determine either project funding requirements or contributions from the GEF and other sources. More commonly, it is retrofitted to decisions that have been made much earlier in the project development process, which depend on the availability of funds at that time, the country in which the project will be implemented, and

the capacity and interest of the IA in implementing the project. A common view expressed was that the available GEF contribution and required cofinancing ratios were, in most cases, decided far upstream in the Activity Cycle, at the early stages of project identification and conceptualization. The incremental cost and budgeting estimations carried out during the course of project design reflect this predetermined amount, rather than assisting in determining the magnitude of incremental costs and identifying the GEF and other contributions. Cofinancing ratios are widely perceived to be the main factor for project approval.

Cost Effectiveness

One of the fundamental reasons to conduct an incremental cost assessment is to estimate different alternatives and then select the most cost-effective one.³ Over a third of the projects reviewed do not describe more than one alternative to the baseline situation, meaning that they provide no evidence that the proposed alternative is the least-cost option to achieve a given global environmental objective (and about 40 percent of the projects reviewed have a weak presentation of the alternatives). In projects where analysis of cost effectiveness is provided, it is of strong or adequate technical quality in only half of the instances.

What Is GEF-able?

The splitting of local and global environmental benefits was perceived by many interviewees to be artificial and, in some cases, impossible to calculate and counterproductive to the sustainability of project objectives. Interviewees reported that this sometimes results in incrementality coming into conflict with other important GEF principles such as sustainability, replication (incentives for), and country drivenness. Chapter 4 highlights some specific cases where such conflicts have led to decision making that has been detrimental to project sustainability.

According to GEF policy, the incremental cost assessment process should provide the “basis for the negotiated technical estimates of agreed incremental cost for any given project” (GEF 1996); is meant to structure the negotiations and dialogue that are necessary to reach agreement; and are required to ensure fairness, credibility, and transparency in terms of host country participation. Previous evaluations and assessments of incremental cost have identified the concept, assessment process, and annex as lacking transparency and at times being in opposition to other fundamental principles of the GEF (such as sustainability, country ownership, and stakeholder participation). The current evaluation supports these conclusions.

Who Conducts the Incremental Cost Assessment and Who Prepares the Annex?

The evaluation found a widespread and often-stated belief that the ability to carry out a “successful” incremental cost assessment (one that results in a project that will be approved by the GEF Council) lies in the hands of a small number of international experts, usually either international consultants or IA staff. The perceived complexity of the incremental cost assessment process, combined with the difficult terms and concepts it uses, discourage “non-experts” from participating in the process. The exclusivity of case-based learning has also restricted proponent and country recipient involvement and perpetuated the use of international consultant experts and in-house IA staff specialists who possess the necessary “expert knowledge” to satisfy the minimum requirements and therefore achieve the main objective of obtaining the GEF funding.

In particular, negotiation of incremental costs does not take place, mainly because overall project financing and GEF contributions are often predetermined, and are presented to project proponents

and government counterparts as being based on nonnegotiable decisions that have already been made. The negotiation then takes place in terms of dividing this predetermined budget into “GEF-able” and “non-GEF-able” activities.

1.4 Recommendations

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 that would be universally applicable and meet the ambitious goals of determining incremental cost and structuring its negotiation was clearly unrealistic. In reality, and as currently required and applied, incremental cost assessment has undermined (or at 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 found that the projects reviewed satisfactorily incorporate the principle of incrementality through incremental reasoning, and are targeted at securing global benefits and attracting additional funding—but that this is in spite of incremental cost assessment, not because of it. There is no apparent value added from incremental cost assessment and annex reporting requirements as laid out by the GEF.

As an instrument, the GEF has evolved considerably since the incremental cost policy and guidance were first developed over a decade ago. GEF projects and focal areas now face changed circumstances, mandates, and conditions that cast

further doubt on current incremental cost assessment procedures and annex requirements. For example, the increasing importance of the need for the GEF to engage with the private sector will require a more tailored and flexible approach. Such an approach is also needed to place the global environmental agenda at the center of sustainable development, which means the artificial division of local and global benefits is counterproductive. Furthermore, the introduction of the Resource Allocation Framework (RAF) will, in some cases, reduce still further the relevance of the incremental cost assessment process. To a large extent, the RAF represents a global incremental assessment that has already been carried out far upstream: countries are provided with an indicative maximum of financial resources available from the GEF for biodiversity and climate change projects, mainly according to their global environmental benefits potential (and governance performance). Carrying out an incremental cost assessment at the project level thus becomes redundant—especially for countries with smaller allocations—provided that projects are directed at global environmental benefits and have adequate levels of cofunding.

For these reasons—changing circumstances and needs, lack of a clearly demonstrated value added, and continuing questions about clarity and transparency—it is clear that the time has come to rethink and reformulate GEF requirements concerning incremental cost processes and methodologies, while maintaining the core principle and underlying rationale of incremental reasoning.

Recommendation 1: 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 objec-

tives 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 matrix in project documents.

Recommendation 2: 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 (1) directed toward achieving global environmental benefits and (2) additional to existing funding levels.

The evaluation confirms that, on average, the GEF funds less than 40 percent of the costs of global environmental benefits. The fact that non-GEF cofinance comprises the majority of project funding in itself indicates that the GEF funding is additional. When developing a project concept, the additionality of GEF funding is established in principle through reasoning based on existing funding levels and additional funding needed to achieve global environmental benefits. In practice, the additionality is achieved through cofunding contributions. First of all, during the further preparation of the project, cofunding arrangements are secured. During implementation, this cofunding will materialize and will thus ensure that the GEF funding is additional. The 2005 Annual Performance Report examined actual levels of cofinancing during implementation, concluding that, in general, cofunding materialized according to plan (GEF EO 2006a).

Incremental reasoning is, thus, alive and well in the GEF. It could certainly be improved and

strengthened, but in principle it will be possible to ensure the additional nature of GEF funding in project design and preparation through

- better identification of global environmental benefits to be achieved in focal area strategies and operational programs, followed by
- identification and prioritization of global environmental benefits on a national level in the context of the RAF, leading to
- adequate attention to demonstrating clear global environmental benefits in the conceptual phase of project design, which will be funded through
- cofunding arrangements, showing that the proposal ensures the additionality of the GEF funding.

There will be projects in which the GEF may have to finance 100 percent of the cost of generating the agreed global environmental benefits—for example, enabling activities, initial phases of international waters projects, and projects in countries with unique situations (those with high potential for unique global environmental benefits but low capacity to generate cofinancing because they are considered highly risky for investments). In these cases, the total costs are incremental, but this will have to be demonstrated at the project concept level and then monitored throughout project implementation.

Full accountability for the incrementality of GEF funding would be achieved, during implementation and at project completion, by

- monitoring for progress toward achieving global environmental benefits and for achieving cofunding in project implementation reviews and the annual portfolio performance report;
- evaluating achievement of global environmental benefits and cofunding in the terminal

evaluations, followed by an independent assessment in the annual performance report of the GEF Evaluation Office.

Recommendation 3: 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 and objectives.

The GEF-4 policy recommendations (GEF 2005c) requested that the GEF Secretariat and Agencies develop clearer guidelines for the application of the incremental cost principle in GEF operations for each focal area, without changing the definition in the *GEF Instrument*.

The only way to strengthen integration of incremental reasoning is by providing full clarity and transparency on the global environmental benefits that are expected from projects through a better definition and focusing of the focal area objectives and strategies (this was already recommended by the Third Overall Performance Study [OPS3] and the most recent program studies of the Evaluation Office). If there are no clear global environmental benefits, incremental reasoning cannot be done, and the concept should not be considered a GEF project.

The role of local costs and benefits should be clearly explained, taking into account the findings and recommendations of the recent *Role of Local Benefits in Global Environmental Programs* evaluation (GEF EO 2006b). Furthermore, the concept of “full cost” from the 1996 policy on incremental costs should be reinstated. In this policy, it was recognized that generating global environmental benefits could lead to local costs that would need

to be included in the incremental funding (leading to “full cost” funding). As pointed out in the local benefits evaluation, a more narrow interpretation of which costs could be funded by the GEF has led to design flaws in projects, which in turn have led to diminished sustainability of project achievements (or in some cases, even a total lack of achievements). The inclusion of local costs for global benefits is of primary importance for the new focal areas of land degradation and persistent organic pollutants (POPs).

The GEF Secretariat, together with the Implementing and Executing Agencies, should develop a dissemination strategy to increase awareness of focal area strategic priorities and global environmental objectives to fully inform incremental reasoning at the concept phase. Particular attention should be paid to ensuring that language, terminology, and presentation are accessible, comprehensible, and useful to stakeholders, particularly country partners and project proponents.

Notes

1. The Executing Agencies are the four major regional development banks—the African Development Bank, the Asian Development Bank, the European Bank for Reconstruction and Development, and the Inter-American Development Bank—and three specialized agencies—the International Fund for Agricultural Development, the Food and Agriculture Organization of the United Nations, and the United Nations Industrial Development Organization.
2. On the other hand, the technical quality review found the treatment of global environmental benefits elsewhere in the project document to be adequate or better in 80 percent of the projects.
3. See GEF (1996), paragraph 8.

2. A Framework for Evaluating Incremental Costs

The primary objectives of this incremental cost evaluation are to evaluate the processes and methodologies used for incremental cost assessment and the process of negotiation of incremental costs. In addressing these objectives, the evaluation took into consideration the existing incremental cost policy, streamlined procedures, principles for agreement, and any guidelines—formal and informal—from GEF task forces. The evaluation has also taken account of the findings and conclusions of previous studies and evaluations with regard to the definition and generation of domestic (local) and global environmental benefits. The evaluation aims to provide feedback and evidence-based inputs to the GEF Council to further clarify incremental cost and its application in the GEF.

2.1 Incremental Cost: Concept, Process, and Product¹

Incremental cost is “the additional cost that the GEF funds between the cost of an alternative project that a country would have implemented in the absence of global environmental concerns, and a project undertaken with global objectives in mind.”²

There are three dimensions to incremental costs as they are understood, applied, and reported on in GEF projects and dealt with by this evaluation:

- **Incremental reasoning** is the core *principle* underlying the GEF: The GEF provides funding to cover the agreed incremental costs of mea-

asures to achieve agreed global environmental benefits. This reasoning is expressed through the global environmental objectives of a project, within the remit of the focal area strategies. It guides the identification, formulation, selection, and implementation of GEF projects. A description of the incremental reasoning underlying the project is required in the concept paper that introduces the project to the GEF Activity Cycle.

- **Incremental cost assessment** is an iterative *process* to operationalize and work through incremental reasoning as a project is designed. A series of assessment steps (such as baseline formulation and definition of project scope) are undertaken to prepare a project in line with the incremental cost policy and guidelines. Incremental cost assessment is required to be applied during the design and preparation stage of the Activity Cycle.
- The **incremental cost annex** is a *product*, a report on the incremental cost assessment that has been carried out during project preparation. It provides a written report against which project eligibility and quality can be reviewed.³ The incremental cost annex is written at the end of the project preparation process as part of the production of the project document, and is required for a project’s CEO endorsement or approval.

2.2 Scope

The evaluation looked at various dimensions of incremental cost as applied in GEF projects and provided recommendations based on its findings.

- It evaluated the product, the *incremental cost annex*, in terms of its quality and compliance to GEF guidelines. Assessment of the annex contents provided an indication of the extent to which GEF requirements pertaining to reporting on incremental costs are being complied with and the overall quality of the analysis presented in the annex.
- It evaluated the process, the *incremental cost assessment*, in terms of its operational approach. Appraisal of the process of incremental cost assessment provided an explanation for the content and quality of the resulting incremental cost annex, and signaled the extent to which incremental reasoning guided project formulation.
- It evaluated the *process of negotiation* according to who is involved and what is negotiable/negotiated at each of the key stages of project identification, preparation, and design, within the assessment and as reported in the annex. Review of the negotiation process provided information on how incremental costs, global benefits, and other aspects of the project alternative and baseline are negotiated and agreed; and whether the participation, process, and outcomes are in line with those envisaged by the GEF and consistent with the principle of incremental reasoning.
- It assessed the *methodology and requirements* for incremental cost assessment and reporting in order to determine whether these are appropriate or sufficient (both as they are reflected in GEF guidance documents and as they are actually applied in project design) to ensure that

GEF projects are based on the core concept of incremental reasoning, and to foster an open and transparent process of negotiation and agreement among project stakeholders.

- It interpreted these findings in order to *draw conclusions and make recommendations* to be presented as feedback to the GEF Council, and evidence-based inputs into the forthcoming GEF Secretariat and IA task force work, to clarify the incremental cost concept and its application in the GEF as requested by the replenishment negotiations for GEF-4.

The evaluation recognized the following limitations:

- The evaluation focused more on appraising incremental cost approaches, processes, and methods as they are currently applied to GEF projects. The evolution of these approaches and its effect on conducting the incremental cost assessment have not been addressed in detail, although chapter 3 presents an overview of the history of the policy and guidelines. Consequently, the evaluation was not able to provide much information on the temporal trends in incremental cost-related quality and compliance performance of GEF projects.
- The evaluation limited the scope to the project level to determine the extent to which cofinancing was incremental and additional. It would have been more informative if additionality of the non-GEF cofinancing could be ascertained at a higher systemic level. For example, the financing provided by a cofinancing partner agency of the GEF could be additional to the project, but this additional finance could have been provided by diverting funding from some other project or program geared toward producing environmental benefits. However, it would have been impossible to determine a

counterfactual to establish the additionality at the higher systemic level.

2.3 Evaluation Methodologies

The evaluation collected information via a mix of quantitative and qualitative methods. The quantitative methodologies were used primarily to gather information on *what* was happening in the project life cycle with regard to the incremental cost assessment (process) and the annex (product). The qualitative methodologies were used to obtain information on *how* and *why* certain processes or procedures were followed, and on conceptual aspects such as incremental reasoning. (For more information on the methodologies, see annex C; annex D contains the data collection instruments used.)

Both quantitative and qualitative data were analyzed in isolation and then triangulated in order to highlight similarities and differences across findings and reduce threats to validity. The qualitative data were assessed and interpreted using computer-assisted qualitative data analysis software—Atlas.ti.

Five tools providing distinct but related data sets were used: literature review, compliance review, technical quality review, interviews, and an online survey. These tools were designed and selected to solicit the opinions and experiences of a representative range of stakeholder groups, information types, and information-gathering techniques so as to provide a comprehensive picture of incremental cost conduct and content.

2.4 Literature Review

A literature review was carried out to gather information on GEF and other documentation of incremental cost, and to synthesize and review past experiences and lessons learned. The review included

- a review of the incremental cost policy, procedures, and requirements (as approved by the GEF Council) for project preparation at various stages in the Activity Cycle;
- GEF Council documents and decisions relating to incremental cost;
- convention articles and guidance;
- existing evaluative and non-evaluative GEF reports in order to establish key issues, advantages, and disadvantages of incremental cost assessment;
- a review of other global programs' financial and economic decision-making tools in order to provide an external comparison.

The information from the literature review was useful in sequencing and reviewing various developments within and outside the GEF that have informed the evolution of GEF incremental cost definitions and applications.

2.5 Compliance Review

The compliance review assessed the extent to which projects are actually complying with the requirements for incremental cost assessment and reporting as established by the policy and other procedural guidance, especially by the GEF project review criteria (approved by the GEF Council in 2000), at the point of CEO endorsement or approval. In all, 140 projects were reviewed, including 79 FSPs that had been CEO endorsed and 61 MSPs that had been CEO approved in 2005.⁴ The distribution patterns of the sampled projects (for both FSPs and MSPs) by IA and focal area mirror the distribution patterns of the GEF-3 projects.

The sample was selected from GEF-3 projects that were CEO endorsed or approved in 2005 so as to provide a current source of data on compliance. These projects were prepared under the

1996 incremental cost policy and 1999 streamlined procedures and principles for agreement, and should therefore reflect their recommendations and requirements (see forth in GEF 1996, 1999a, and 1999b). The focus was on projects that were successful in securing CEO endorsement or approval, as their project documents are presumed to have met the incremental cost assessment requirements.

A set of parameters—including those pertaining to reporting, costs and benefits, risk, and cofinancing—that could be used to assess compliance was identified, and an assessment instrument developed based on these parameters. Sections on incremental costs and cofinancing within project documents were assessed. For assessing compliance with the incremental cost reporting requirements, only the incremental cost annex section was considered. For assessing compliance with the requirements on specifying costs and benefits, risk, and financing, all sections in the project documents were considered.

Chi square and “F” tests were used to determine whether there was a difference in the performance of two groups—for example, projects in the biodiversity focal area compared to other focal areas or World Bank projects compared to those of other IAs. Where a difference in the performance of two groups has been reported, it is significant at the 90 percent confidence level.

2.6 Technical Quality Review

Project documents and executive summaries were reviewed in order to conduct an in-depth assessment of the technical quality of incremental cost assessment and reporting. The reviews were conducted by expert consultants in each of the focal areas.

The initial sample for the technical quality review was the same as that for the compliance review.

Of these 152 projects, 6 projects from the POPs and 1 from the ozone depletion focal areas were excluded from the technical quality review. Projects in the POPs focal area were considered too new, and too few, to have yet generated any meaningful lessons learned on the use and application of the incremental cost approach. From the remaining 145 projects, a random sample of 86 projects was drawn, stratified by focal area and project size.

Each project document/executive summary was assessed on 37 criteria pertaining to key stages and aspects of incremental cost assessment as specified in the GEF incremental cost reporting format;⁵ these include descriptions of development goals/baseline formulation, global environmental objective, alternative, scope of analysis, costs, and process of agreement, among others.

For each review criterion, projects were ranked as “strong,” “adequate,” “weak,” or “absent.” For each project, where appropriate, descriptive notes were provided in order to elaborate or qualify these rankings. In addition, for each project, good practices and significant shortcomings in incremental cost assessment were also identified.

Both quantitative and qualitative analyses were carried out. The quantitative analysis presents findings on the proportion of projects ranked “strong,” “adequate,” “weak,” or “absent” overall and according to each technical quality review criterion. The qualitative analysis compiles reviewer comments on individual review criteria, and on best and worst practices for each project and overall for focal area categories.

2.7 Interviews

Semi-structured interviews based on a common protocol were carried out with 55 people involved in GEF project design, review, and approval. The

interview protocol was designed to provide information on how incremental cost assessments were carried out and why certain procedures were followed (such as the use of project examples and case law). Such questions could not be effectively addressed from information from other data sources such as the compliance and technical quality reviews, which focus more broadly on what is happening.

A purposive/snowball sampling method was employed to ensure that there was representation of key stakeholders such as the GEF Secretariat, IAs, convention secretariats, incremental cost consultants, and project proponents.⁶ Interviews were conducted between May 1 and July 31, 2006. The evaluation undertook three field missions to Kenya, Malaysia, Panama, and Thailand in order to solicit responses from IA staff and project proponents who had experience with preparing projects in those countries and regions. Some groups, such as national focal points and project proponents, are underrepresented, and this may introduce some bias.⁷

The analysis of the semi-structured interviews was based on the principles of systematic selection and sorting of data, coding and breaking data down to reveal meaning, and reconstruction to reveal relationships. This process was conducted using the CAQDAS software package Atlas-ti.

2.8 Online Survey

The online survey aimed to gather information from a broad group of GEF stakeholders regarding the application of incremental costs in GEF project preparation and implementation. As an initial step in developing the questionnaire instrument, the evaluation reviewed all existing GEF information relating to incremental costs and data inputs from 8 to 10 semi-structured interviews.⁸ The resulting questionnaire was developed to assess

the perceptions of stakeholders on various incremental cost assessment concepts and processes. The instrument was administered online through www.surveymonkey.org.

The survey target group comprised those involved in the design, review, implementation, and/or supervision of GEF projects (no attempt was made to estimate the possible universe of responses nor to ensure sufficient responses to make the survey statistically representative of the universe or any particular group). The targeted population was contacted primarily through an email request to complete the survey (everyone received an initial email and then a reminder). The survey was opened on June 13, 2006, and closed on July 31, 2006. During this period, 159 respondents participated in the survey. Of these, 119 respondents (75 percent) completed the survey, while 40 (25 percent) dropped out without completing it. Of the respondents who completed the survey, 30 percent were from IAs, 27 percent were from the Scientific and Technical Advisory Panel roster, 10 percent were independent consultants, and 8 percent were national focal points; the remaining 24 percent were split among respondents from the GEF Secretariat, international and national NGOs, national government agencies, and bilateral and other multilateral institutions.⁹ Since the questions that ascertained the identity of the respondents were at the very end of the survey, the identities of the dropouts are not known. For any given question, all responses have been considered to provide an aggregate picture. However, where intergroup comparisons have been made, the dropouts have been excluded from the analysis.

Notes

1. The conceptual framework and basis to the evaluation evolved as data were collected. At the start of this evaluation, no distinction was made among the concept, process, and product of incremental

costs; but during the evaluation, it became clear both that there were different aspects of the incremental cost concept in the GEF, and that these should be understood and treated differently in relation to their role in project identification, formulation, selection, and implementation.

2. GEF, "Key GEF Terms," www.theGEF.org/Outreach/outreach-Publications/key_terms.html.
3. This report comprises annex A in the project executive summary for full-size projects and a specified section in the project brief for medium-size projects.
4. Of the total 152 projects approved during calendar year 2005, the assessment excluded 12 enabling activities (5 FSPs and 7 MSPs), as the GEF Secretariat does not expect these projects to include

a section on incremental cost assessment in the project proposal.

5. As specified by GEF (1996).
6. Incremental cost consultants are usually advisers to project development facility teams for the overall project preparation up to and including the incremental cost assessment.
7. These underrepresented groups include project development facility teams and government officials.
8. These interviews were conducted with World Bank and UNEP staff in Washington, D.C., and Nairobi in May 2006.
9. Only four respondents (3 percent) were from the GEF Secretariat.

3. Incremental Costs and the GEF

3.1 Development of the Incremental Cost Concept in Financing Global Environmental Benefits (1987–92)

In 1987, the Montreal Protocol on Substances That Deplete the Ozone Layer set the initial precedent for adopting incremental costs as a basis for financing global environmental benefits. It refers both to *incrementality* (aiming to secure funding to meet agreed incremental costs) and *additionality* (acknowledging the need for additional financial resources). The GEF was appointed a financial mechanism for the Montreal Protocol in 1992. Based on its focus on changing production processes and investment choices and the selection and substitution of chemicals, the protocol was able to develop a list of eligible activities for incremental cost financing (see annex B). On a project-by-project basis, the application of incremental cost assessments in Montreal Protocol projects has encountered few problems as baseline and alternative situations are relatively easy to determine; however, because the local benefits of the proposed changes are not (as a rule) subtracted, countries gain from side benefits, such as employment.¹

In 1992, the environment and development objectives of Agenda 21 affirmed the importance of incremental costs as a principle underlying the financing of actions to deal with global environmental problems and secure global environmental

benefits, and emphasized the need for a substantial flow of new and additional financial resources to developing countries. Chapter 33 on financial resources and mechanisms specifies the GEF as one source of funding (among many) and calls for a restructuring of the GEF so as to increase its flexibility, promote participation, improve governance, and enhance the flow of funds from developed to developing countries (UN 1993).

The United Nations Convention on Biological Diversity (UNCBD), United Nations Framework Convention on Climate Change (UNFCCC), and United Nations Convention on Combating Desertification (UNCCD) all subsequently adopted incremental costs as a core principle for project decision making, based on the belief that developed countries are responsible for paying the incremental costs of meeting convention objectives (see box 3.1). Both the UNFCCC and UNCBD call for new and additional resources to be used to finance the agreed “full” incremental costs of actions undertaken to meet their objectives, and name the GEF as the (then interim, and now confirmed) operating entity of their financial mechanisms. The UNCCD makes similar provisions, although it does not explicitly refer to full costs.

Like the Montreal Protocol, the UNCBD and UNFCCC developed indicative lists of activities that could be funded as agreed incremental

Box 3.1

Rio Conventions and Incremental Cost

United Nations Convention on Biological Diversity—Article 20, Financial Resources (ii)

The developed country Parties shall provide new and additional financial resources to enable developing country Parties to meet the agreed full incremental costs to them of implementing measures which fulfill the obligations of this Convention and to benefit from its provisions and which costs are agreed between a developing country Party and the institutional structure referred to in Article 21, in accordance with policy, strategy, program priorities and eligibility criteria and an indicative list of incremental costs established by the Conference of the Parties.

United Nations Framework Convention on Climate Change

- **Article 4, Commitments.** The developed country Parties and other developed Parties included in Annex II shall provide new and additional financial resources to meet the agreed full costs incurred by developing country Parties in complying with their obligations under Article 12, paragraph 1. They shall also provide such financial resources, including for the transfer of technology, needed by the developing country Parties to meet the agreed full incremental costs of implementing measures that are covered by paragraph 1 of this Article and that are agreed between a developing country Party and the international entity or entities referred to in Article 11, in accordance with that Article.
- **Article 12, Communication of Information Related to Implementation.** Developing country Parties may, on a voluntary basis, propose projects for financing, including specific technologies, materials, equipment, techniques or practices that would be needed to implement such projects, along with, if possible, an estimate of all incremental costs, of the reductions of emissions and increments of removals of greenhouse gases, as well as an estimate of the consequent benefits.

United National Convention on Combating Desertification—Article 20, Financial Resources (2)(b)

[The] developed country Parties, while giving priority to affected African country Parties without neglecting affected developing country Parties in other regions, in accordance with article 7, undertake to: (a) ... (b) promote the mobilization of adequate, timely and predictable financial resources, including new and additional funding from the Global Environment Facility of the agreed incremental costs of those activities concerning desertification that relate to its four focal areas, in conformity with the relevant provisions of the Instrument establishing the Global Environment Facility...

costs through the GEF. Articles 6 through 14 of the UNCBD indicate the types of activities that are eligible for incremental cost financing; the Intergovernmental Committee of the UNCBD (1994) also formulated draft guidelines and a list of eligible incremental activities. Similarly, article 4 of the UNFCCC refers to activities eligible for incremental financing. (See annex B.) These lists draw on a broad range of possible biodiversity and climate change mitigation/adaptation activities stated in the conventions and do not necessarily reflect GEF eligibility criteria.

In practice, many of the activities included in UNCBD, UNFCCC, and UNCCD projects have not proved to be easily amenable to incremen-

tal cost assessment because they address “softer” investments such as capacity building at individual, institutional, and policy levels where precise costs for baselines and alternatives are difficult to establish. Various deliberations acknowledge some of the difficulties involved in actually applying the incremental cost concept in projects. In 1994, the 10th session of the Intergovernmental Negotiating Committee of the UNFCCC recognized that incremental costs “were complex and difficult and further discussion was needed” (Wolfe 1994). It concluded that the concept of agreed full incremental costs should be applied on a “flexible, pragmatic and case-by-case basis,” and promised that guidelines would be developed by the UNFCCC Conference of the Parties (COP) at a later stage

“on the basis of experience.” Similarly, the Intergovernmental Committee of the UN CBD (1994) recognized that the “application of incremental costs might be more difficult to address in the context of biological diversity” and that the “cost calculation” was particularly difficult because of “uncertainty, risk and lack of information” on ecological processes and human interactions. Despite repeated calls to do so, the COPs of the UNFCCC and UN CBD have provided little explicit policy guidance to the GEF on incremental costs.

3.2 Incremental Costs and the GEF *Instrument and Operational Strategy* (1994–95)

As stated in the GEF *Instrument* in its 1992, 1994, and 2004 iterations, and reiterated in article 2 of the Operational Principles of the GEF (GEF 1995, p. 2), the mandate of the GEF (derived from the conventions) is to act as a “mechanism for international cooperation” to manage and allocate funds provided “to meet the agreed incremental costs of measures to achieve agreed global environmental benefits.” The principle of incremental cost is thus key to GEF operations. This principle has been further endorsed by the donors participating in the recently concluded negotiations for the establishment of the fourth phase of the GEF (2007–10).

The concept and workings of incremental costs are further elaborated in the *Operational Strategy* (GEF 1995), which lays out additionality and global benefits as key principles. Emphasis is given to GEF funding being used only to cover incremental costs, and to the GEF allocating its resources as new and additional funding (not as a substitute for regular sources of development finance). The *Strategy* distinguishes “global” from “domestic” (local) benefits, and promotes a flexible application of the “incremental” mandate of the GEF, based on

the notion of “environmental reasonableness as a guiding principle” (UNFCCC 1995). Incremental cost is thus applied to act as a filter to distinguish GEF funds from traditional development assistance and to ensure that they are earmarked for global aspects of environmental protection as opposed to domestic environmental benefits.

3.3 GEF Incremental Cost Policy and Reporting Format (1994–96)

The initial policy framework for incremental cost assessment was put in place after the end of the GEF pilot phase in 1994. Projects that were developed during the pilot phase did not use incremental cost assessment, and it was recognized that the concept of incremental cost was poorly applied and understood. The pilot phase evaluation therefore recommended that the GEF develop a set of “guidelines” and an “acceptable methodology” for calculating incremental costs (UNDP, UNEP, and World Bank 1994).

This demand was met with the November 1994 presentation to the Council of an initial paper, “Incremental Costs and Financing Policy Issues,” which set out a framework for assessing incremental costs in GEF projects (GEF 1994a). This policy document is referred to in the *Operational Strategy* statement: “GEF will follow the approach approved by Council.” The Council commented on the paper at its next meeting (May 1995) and recognized the need for a “flexible application of the concept of incremental costs.” The Council also requested that the GEF use the notion of “environmental reasonableness” when considering such issues as domestic costs and benefits, so as not to penalize progressive environmental actions in recipient countries (GEF Council 1995). However, this concept of environmental reasonableness subsequently seems to have disappeared from GEF discourse on incremental costs.

On the basis of Council comments, the paper was finalized and presented as an interim information document in February 1996 (GEF 1996), and disseminated by the GEF Secretariat as the GEF Policy on Estimating Agreed Incremental Costs. It provides the GEF conceptual understanding and definition of incremental cost, and sketches out the operational framework to structure incremental cost assessment, specifying mechanisms for reaching agreement through negotiation and outlining incremental cost reporting requirements in project proposals (see table 3.1). Therefore, the paper is a combination of a policy presentation and a set of guidelines for the GEF Secretariat, IA staff, and country recipients charged with conducting, negotiating, and reviewing project incremental cost assessments. Key elements of the policy include the following:

- **An emphasis on the principles of global benefits, additionality, and incrementality.** Additional actions to secure global environmental benefits impose “incremental” costs over and above the costs of actions that are strictly necessary for a country to achieve its own development goals. The purpose of the GEF is to provide new and additional financial resources to meet the agreed incremental costs of these measures to achieve agreed global environmental benefits.
- **Explanations of the need and rationale for applying procedures to estimate full incremental cost.** Incremental cost assessments are carried out and reported on in order to judge the level of GEF funding, structure the technical negotiations necessary to reach agreement on global benefits and incremental costs, provide a reference value for the required grant financing, choose the most cost-effective means of securing global benefits, and indicate the funds that will need to be mobilized.
- **Promotion of incremental cost assessment to ensure transparency in project preparation and avoid arbitrariness in project review.** Transparency is gained, and arbitrariness avoided, by adhering to a standardized framework for assessment that is based both on descriptive analysis and the quantification of baseline, alternative, and incremental costs.

The annex to the policy establishes clearly that all projects must (1) show how the approach to estimating incremental cost has been applied, and (2) provide preliminary (quantified) estimates of incremental cost, according to the following format:

- **Broad development goals and baseline description**—the relevant broad developmental goals of the country and the way the country can reasonably be expected to address the above development needs in its own economic interests
- **Global environmental objective**—the objective of the proposal to the GEF, namely to avert specified consequences for the global environment of the above baseline
- **GEF alternative**—a justification of the proposed way to meet the baseline developmental goals and the global environmental objectives simultaneously as the least-cost option
- **Scope of the analysis (system boundary)**—the scope of the matters taken into consideration
- **Costs (and incremental cost matrix)**—all the economic costs within the system boundary of the proposed alternative course of action and those avoided by not undertaking the baseline course of action, including preliminary estimates in present value terms presented in a matrix that shows the costs, the domestic benefits, and the global environmental benefits

Table 3.1

Incremental cost policy and guidance framework: 1996

General considerations in judging agreed full incremental costs	<ul style="list-style-type: none"> • Transparency • Pragmatic judgment of funding on a case-by-case basis • Avoidance of arbitrariness by adhering to a framework • Framework should provide reference value for the required grant funding • Cost effectiveness—alternative should be the lowest possible incremental cost
Incremental cost definition	<ul style="list-style-type: none"> • Relevant costs are incremental, not total. • Cost of GEF-eligible activity should be compared to that of the activity it replaces or makes redundant. The difference between the two costs—the expenditure on the GEF-supported activity and the cost saving on the replaced or redundant activity—is the incremental cost. It is a measure of the future economic burden on the country that would result from its choosing the GEF-supported activity in preference to one that would have been sufficient in the national interest.
Baselines	<ul style="list-style-type: none"> • To estimate incremental cost, the analyst must estimate both the expenditure on the activity in question and the cost saving on activities that, as a result of the GEF activity, will no longer be needed. Expenditure estimates are usually readily available for any fully prepared project, but cost savings present a more difficult operational problem. Cost savings pertain to the projected “baseline” of future activities for sustainable national development which does not explicitly take global considerations into account. • Reasonable baselines will be based on consultation with the GEF and the recipient government. Such dialogue will ensure that GEF-supported activities become part of the countries’ own environmental protection efforts. • Baselines will draw upon existing studies and plans at the country and sectoral levels, such that if incremental financing failed to materialize, the baseline course of action would still be followed. • A plausible baseline will have these characteristics: (1) address national goals, (2) technical feasibility, (3) economically feasible and attractive option, (4) environmentally reasonable, (5) financially realistic. • Recognizing that baselines are dynamic and evolving, in more complex cases, GEF projects would use an overall development baseline, rather than one especially prepared for a GEF intervention. Reasons for this are: (1) preparing a baseline involves considerable time and effort and may not be practical on a project-by-project basis; (2) consistent assumptions help to maintain overall development assistance coherence rather than preparing separate baselines for related activities; (3) the estimate of incremental costs is very sensitive to the baseline estimate, and it would be more credible and transparent to have one that is prepared independent of the project; and (4) baselines are required for all activities, including capacity building and all focal and cross-cutting areas.
GEF alternatives	<ul style="list-style-type: none"> • Must be country driven • Must deliver the same domestic benefits as the country planned under the baseline situation • Must deliver global environmental benefits over and above the baseline situation • Acceptable to the country in that they meet the first four of the five baseline characteristics • Domestic costs and benefits of the baseline and alternative situations may accrue to different groups; to ensure acceptability and sustainability of the proposed alternative, good project design would address any redistributive effects of the GEF alternative
Agreed full cost	<ul style="list-style-type: none"> • These activities are primarily communications and studies undertaken for conventions (enabling activities). • The GEF will develop an indicative list of agreed full cost activities.
Treatment of benefits and costs	<ul style="list-style-type: none"> • To estimate incremental costs, it is necessary to quantify costs. • It is sufficient merely to identify benefits and match domestic benefits between the baseline and the alternative. • The GEF project must achieve domestic benefits equivalent to the baseline situation, but these do not have to be monetized.

(continued)

Table 3.1 (continued)

Global environmental benefits	Whenever a global environmental objective is met, the activity has to that extent achieved a global environmental benefit.
Full cost	<p>The concept of “full incremental costs” implies several considerations for GEF projects:</p> <ul style="list-style-type: none"> • Domestic benefits are not to be subtracted from incremental costs. • Every effort should be made to identify all incremental costs. • No GEF activity should incur negative environmental and social costs. • Negative impacts must be mitigated. • Indirect costs (including opportunity costs) must be reflected in the incremental costs and should be included in the baseline vis-à-vis GEF alternative assessment.
Concept of “agreed”	<p>The grant would be agreed between the GEF and the recipient. Because projects are country-driven and because implementation is ultimately voluntary:</p> <ul style="list-style-type: none"> • A transparent process must be used to reach agreement. • Baselines would need to be derived in a transparent and credible way through dialogue with the country. • Baselines would either come from outside the GEF context (such as sectoral investment plans) or be independently verifiable, but would not be ad hoc. Other technical parameters would similarly have to be grounded in broader considerations. Reliance on just the identifiable monitorable expenditures and the planned baseline outlays avoids resorting to rather more controversial economic valuation methods (such as those for monetizing environmental benefits and for calculating opportunity costs). This makes agreement more likely.
Technical process for agreement	<ul style="list-style-type: none"> • The IA task manager will make an estimate in consultation with the technical counterparts in country at an early stage in the project cycle to expedite a “reasonable agreement” based on the application of the principles of incremental cost. • The country recipient and IA will confer on the process to be used for estimating incremental costs starting early in the project cycle. • Full documentation and disclosure will be followed in order to promote transparency on the application of incremental cost principles. • The agreement will then be reviewed by the GEF Secretariat (bilateral with the IAs) which will consider (1) technical aspects of the project proposal and (2) the financing plan. • The GEF Secretariat will make a final recommendation on financing at the time of CEO project approval.
Use of incremental costs in operational strategy and financing policy	<ul style="list-style-type: none"> • The reason for developing an approach for estimating incremental cost is that incremental cost is pivotal to the GEF operational strategy and financing policy. • The GEF does not finance non-incremental costs. • Lists of incremental costs are not specified. The approach is intended to be generally applicable, rather than restricted to specific types of incremental costs (such as capital, operating, transaction, learning, costs); the latter are not listed as explicitly eligible expenditures. Lists can be misinterpreted, since for any expenditure, it is only the increment that is eligible and not necessarily the whole amount. • Incremental costs are not the only consideration in operational strategy and financing. Incremental cost estimates are required for barrier removal, reducing long-run costs of sustainable development, selecting projects, choosing an appropriate financing modality, setting financing policy, and designing cost-effective measures.
Reporting format	<p>The reporting format in project documents will be:</p> <ul style="list-style-type: none"> • Broad development goals and baseline description • Global environmental objective • GEF alternative • Scope of the analysis (system boundary) • Costs (incremental cost assessment matrix)—costs should be estimated in present value terms; the matrix should show costs, domestic benefits, and global environmental benefits • Process of agreement

associated with the baseline course of action and the proposed alternative course of action, and the increment

- **Process of agreement**—the manner of reaching agreement with the relevant technical counterparts and authorities

3.4 Streamlined Procedures for Incremental Cost Assessment and Principles for Agreement (1997–99)

A year after the incremental cost policy was adopted, streamlined procedures for incremental cost assessment were issued to the IAs (GEF Secretariat 1997) and presented to the GEF Council in May 1999 in the document “Note on Incremental Costs” (GEF 1999a). Principles for the process of agreement were also presented for Council approval, in December 1999, via the “Report on Incremental Costs” (GEF 1999b).

The streamlined procedures were the GEF Secretariat response to the First Overall Performance Study’s finding that incremental cost assessment was unclear, and lacked transparency and country involvement (GEF 1998a). The study called for “simpler, more straightforward guidance.” This stance was affirmed by the First GEF Assembly and the Council in 1998, which requested that the application of the incremental cost principle and process be made more “pragmatic” and “transparent.”

Additionally, the GEF Secretariat conducted several studies involving outside experts and the joint GEF Secretariat-IA focal area task forces to report on incremental cost practices focusing on stakeholder involvement and negotiation, and the more technical aspects of estimating costs. The paper reporting on these studies, “Progress on Incremental Costs,” was presented at the October 1998 GEF Council meeting, and called for the

process of determining incremental costs to be made more transparent and its application more pragmatic; it also included a number of proposals to improve the process of determining incremental costs (GEF 1998b). Although these processes did not influence the development of the streamlined procedures (which had already been in use informally since 1997 and brought to the Council’s attention in 1999), they did result in a more detailed set of principles for agreement.

While both the “Note on Incremental Costs” (which outlined streamlined procedures) and the “Report on Incremental Costs” (which outlined principles for agreement) introduced important changes in focus and emphasis in relation to the 1996 incremental costs policy (see tables 3.2 and 3.3), neither was intended to replace the original policy. Rather, they aimed to “show how the approved approach can be applied pragmatically in different situations by drawing on lessons of experience” (GEF 1999a and 1999b). However, they introduce two important changes in the requirements and procedures for incremental cost assessment:

- They place far greater emphasis on qualitative aspects of incremental reasoning than on quantitative incremental cost assessment.
- They allow for certain types of projects to conduct a simpler form of incremental cost assessment than that outlined in the annex to the 1996 policy, which involves far less rigorous and cumbersome reporting requirements.

The principles for agreement introduce, for the first time, a more overarching and conceptual process of incremental reasoning, in addition to earlier quasi-economic interpretations of incremental cost assessment. At the same time, they change the terminology from incremental cost “analysis” to “assessment,” reflecting this softer

Table 3.2

Streamlined procedures for incremental cost assessment: 1997

<p>Operational programming of incremental cost procedures: upstream consultations</p>	<ul style="list-style-type: none"> • The project concept alone will be sufficient, without consideration of incremental cost implications, because getting the “strategic fit and right project design” are what facilitates subsequent discussion on incremental cost. <ul style="list-style-type: none"> – IAs may wish to discuss strategic fit (for example, how the project conforms to the operational program) with the GEF Secretariat. This will facilitate subsequent discussion of incremental cost. – The project must make “a difference” to the global environment. – The logical framework should be used to facilitate discussion. • Project design: <ul style="list-style-type: none"> – <i>Activities</i>. It is useful to identify a small number of major activities at the outset to make it easier to estimate their incremental costs. – <i>Baseline</i>. A clear understanding of the course of events threatening the global environment is required so that the alternative is easier to define. • Types of incremental activity: <ul style="list-style-type: none"> – For each activity, it would be necessary to understand whether it was intended to add something without changing the baseline (complementary activity), or whether it is intended to change the baseline for something better (substitutional activity). – Knowing whether an activity is complementary or substitutional makes it easier to define how it will benefit the global environment, determine its catalytic effect, and show any financial leverage. – <i>Complementary activity</i>. This type of activity has no direct effect on the baseline or major impact on other economic activities (for example, it may include capacity building, protected area management, barrier removal for renewable energy or efficiency). – <i>Substitutional activity</i>. This type of activity changes the way of doing business to one that is “friendly” to the global environment (for example, modifies economic activities, substitutes or modifies a regular official development assistance project, removes a socioeconomic cause of degradation—alternative livelihood, support planning for an economic sector—yields economic benefits for the local population).
<p>Bilateral review</p>	<ul style="list-style-type: none"> • It is necessary to draw out the incremental cost implications of the decisions taken early in project design and provide guidance on the steps necessary to complete incremental cost assessments. Incremental cost should be considered for each major activity whether it is complementary or substitutional. • Issues to be addressed: <ul style="list-style-type: none"> – Is baseline financing secured? – Is the alternative the least cost? • Questions for complementary activities: <ul style="list-style-type: none"> – What evidence is there that GEF financing is genuinely additional, with no de-leveraging or crowding out? – What assurances are there for the continuance of existing levels of finance by the government or others (for example, for national park management)? – What cost sharing with beneficiaries would be appropriate, and how could cost-recovery mechanisms be built into the project to encourage environmental responsibility and financial sustainability in the absence of GEF support? – What level of IA, bilateral, private, or NGO cofunding is available in light of the benefits enjoyed by the local population? • For substitutional activities: <ul style="list-style-type: none"> – The emphasis will be on describing and costing the baseline. – The system boundary of the project that addresses all effects will need to be described, and an incremental cost matrix produced in accordance with the reporting format.
<p>Work program</p>	<p>The proposal must include an incremental cost assessment made in accordance with the guidance given at the bilateral review.</p>

Table 3.3

Principles for the agreement process for incremental costs: 1999

<p>Country involvement</p>	<p>The IA and in-country project sponsors, designers, and local executing agencies should work collaboratively in calculating incremental costs.</p> <ul style="list-style-type: none"> • Incremental cost estimation should be a joint task of the GEF IA and the in-country partners proposing or designing the project, or who are 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.
<p>Differentiated and shared responsibilities</p>	<ul style="list-style-type: none"> • The in-country project proponent/sponsor/designer/local executing agency should jointly undertake incremental cost determination with the IA. In particular, the country partner could assume primary responsibility for the following tasks related to incremental cost negotiations: <ul style="list-style-type: none"> – Collect and analyze relevant country data. – Identify stakeholders for broader consultations and organize a logframe or project development/consultation workshop. – Convey basic incremental cost principles to stakeholders. • The GEF operational focal point: <ul style="list-style-type: none"> – Reviews projects, endorsing their consistency with respect to national programs and confirming national priorities. – Facilitates broad as well as project-related consultations, particularly with government agencies. • Implementing Agencies: <ul style="list-style-type: none"> – Support country efforts to prepare projects, particularly with respect to the implications of GEF policies and procedures, such as incremental cost. – Facilitate the processing of these proposals through the GEF Activity Cycle. – Inform 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. • The GEF Secretariat: <ul style="list-style-type: none"> – At pipeline entry, reviews the incremental principle of the concepts submitted by an IA or regional development bank and provides feedback on eligibility. – At work program entry, reviews the incremental cost assessment (baseline scenario, GEF alternative scenario, and incremental cost components). – At CEO endorsement, reviews the final incremental cost determination and checks for consistency with the work program inclusion document.
<p>Early feedback</p>	<p>The GEF Secretariat should provide early feedback on the incremental reasoning of projects at pipeline entry:</p> <ul style="list-style-type: none"> • This upstream consultation between the IA and GEF Secretariat should include specific comments on what minimum information will be expected at the next step in the project cycle—for example, on domestic and global benefits, baseline scenario, and barrier removal in the project. • The review should identify any project design issues that might have implications for the incremental cost assessment.
<p>Transparency (and negotiation)</p>	<ul style="list-style-type: none"> • The GEF Secretariat’s reviews of projects, including the incremental cost section, should be shared with the project proposers in a timely fashion. • The IA 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.

(continued)

Table 3.3 (continued)

<p>Emphasis on quality, not numbers</p>	<p>The starting point for determining incremental cost should be the use of the incremental reasoning of projects, rather than quantification.</p> <ul style="list-style-type: none"> • 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 work program entry, 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.
<p>Integration of incremental cost with logical framework analysis</p>	<ul style="list-style-type: none"> • The process of estimating incremental cost should start early in project development as part of the logframe process of participatory, iterative, and multistakeholder development of projects. • A logframe workshop, or similar collaborative project development consultation, should provide the forum for the following: <ul style="list-style-type: none"> – Identifying stakeholders in the incremental cost negotiation. – Conveying the basic principles of incremental cost. – Stimulating participation of in-country partners in incremental cost estimation. – Discussing baseline and alternative scenarios.
<p>Informed agreement</p>	<ul style="list-style-type: none"> • 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 Web site. • The IA should advise project partners about the availability of such information.
<p>Incorporation into the Activity Cycle</p>	<p>The above principles for the agreement process will be incorporated into the updated Activity Cycle as follows:</p> <ul style="list-style-type: none"> • <i>First GEF decision point—pipeline entry.</i> The Secretariat reviews the proposal against the relevant project review criteria, and applies the criteria for conceptual conformity only. <ul style="list-style-type: none"> – The incremental reasoning of projects at pipeline entry 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, IA, and the in-country partners proposing or designing the project or who are 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. • <i>Second GEF decision point—approval.</i> The project brief should describe the process used to jointly determine incremental cost, a process that is intrinsic to good project design. <ul style="list-style-type: none"> – At the time of work program entry, 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. • <i>Third GEF decision point—endorsement.</i> The Secretariat reviews the project document for consistency with the project brief approved by the GEF Council. <ul style="list-style-type: none"> – 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.

approach. The principles for agreement stress that “the starting point for determining incremental cost should be the use of incremental reasoning for projects, rather than quantification” (GEF 1999b).

The streamlined procedures similarly state that “at the upstream consultations, discussion of the project concept alone would be sufficient, even without explicit consideration of any ‘inremen-

tal cost' issues" (GEF 1997). Only a qualitative presentation of incrementality (in line with conceptual conformity) is therefore required for GEF Secretariat review, with "increasing need for clarity" as project preparation proceeds. Agreement on incremental cost is then seen as part of, and the result of, collaborative decision making during project preparation. The project brief is required to describe the process used to jointly determine incremental cost, and estimates of costs (if prepared—see below) are demanded only at work program entry. If incremental costs are presented as a quantified figure, they are required to be finalized by the CEO endorsement stage.

Thus, whereas the 1996 policy requires unambiguously that "each project proposal submitted to GEF will show how the approach to estimating incremental cost would be applied and will provide preliminary estimates of the incremental cost," the principles merely state that "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."

The streamlined procedures provide a filter for choosing between "complex" and "simple" incremental cost assessment by distinguishing between "substitute" and "complementary" projects, allowing that a simpler analysis of incremental cost is appropriate for complementary projects and that full complexity of analysis is required only where there is substitution or generation of additional (nonglobal) benefits. Until the bilateral review meeting (the meeting between the GEF Secretariat and the IA to discuss a project proposal), incremental cost assessment is stated to remain "a way of thinking about the proposed project...not yet a 'calculus' of incremental costs." The streamlined procedures specify that it is at the bilateral review meeting that the most streamlined way of estimating incremental cost is identified. Here,

the decision on whether incremental costs are complementary or substitutional is linked to each major activity, not the project as a whole.

The streamlined procedures determine that certain requirements apply to all projects—namely that baseline financing must be secured, and the alternative being proposed should be the least-cost option. For complementary activities, the emphasis would then be on demonstrating additionality and continued baseline financing, cost sharing and cost recovery, cofunding, and a project budget (not a quantified incremental cost estimate). It is only substitutional projects that have to describe and cost the baseline, describe the system boundary, and produce an incremental cost matrix. The streamlined procedures recognize that many biodiversity projects and medium-size projects can be treated in this simpler way. They include an annex addressing specific incremental cost issues in the biodiversity focal area, and significantly provide an illustrative list of complementary and substitutional activities that could be considered eligible for incremental cost financing. The climate change mitigation and international waters focal areas were supposed to develop similar procedures "over time," but these have not yet been produced by the GEF Secretariat. Although there is internal understanding of how these focal areas apply incremental cost, no public information is available.²

At the same time, other important, but less immediately discernible, shifts are articulated in the streamlined procedures and principles for agreement. Various components of incremental cost assessment as originally conceived disappeared from the GEF documentation—such as a reference to full incremental costs and the idea that incremental cost includes (along with the expenditure on the GEF-supported activity) any cost saving on the replaced or redundant activity. This

is one of the main confusions in the application of incremental cost, the idea that the GEF should not pay for any local benefits.

The GEF documents on process for agreement and streamlined procedures thus represent a significant departure from earlier policy and guidelines that demand a rigorous, cumbersome, and quantified analysis of incremental costs. These new elements, and the relaxation of requirements, are meant (according to the streamlined procedures) to be applicable to all new projects—and retrospectively to projects already under preparation. However, despite this relaxation in requirements and introduction of new elements, no new GEF guidelines were prepared to address how incremental cost assessments should be carried out and what reporting would be required. In fact, it is explicitly stated that neither the annex on streamlined procedures nor that on principles of agreement replaces the 1996 policy and reporting format (GEF 1999a and 1999b), and reference continues to be made to the “standard reporting format” as set forth in the 1996 policy document. Thus, a basic inconsistency arises in the GEF guidance provided for identifying and estimating incremental cost. The earlier, far more quantitative and prescriptive, policy and associated guidelines no longer match recommended policy and practice.

3.5 PRINCE (1993–98)

The Program for Measuring Incremental Cost for the Environment was implemented between 1993 and 1998, and was led by the GEF Secretariat. It aimed to

develop a broad interpretation of incremental cost that is consistent across the GEF focal areas—climate change mitigation, ozone layer protection, biodiversity protection, and prevention of pollution of international waters. It should be possible for each of the GEF implementing agencies to apply this interpretation uniformly in all participating countries (King 1993)

This goal was related primarily to the need for the GEF to make its operational decision making simpler and more transparent, to standardize its funding procedures at the end of the pilot phase, and to provide a clear technical justification (or guarantee) of the concept of additionality of funds.

PRINCE intended to carry out a series of methodological studies that would refine the procedures for key operational concepts in incremental cost and conduct field tests to apply these methodologies and ensure that they met GEF criteria. The program was also intended to disseminate information about incremental cost methodologies through best practice workshops, training programs, and codes of practice. Research focused on a series of climate change mitigation case studies, as this was seen to be the most transparent context (after ozone depletion), and because of the perceived analytic simplicity associated with the physical capital investment required to reduce greenhouse gases.

A review of PRINCE documents shows that the program did produce methodological studies in climate change that were of practical relevance to the GEF climate change focal area during its early development, when it focused on technology transfer and subsidization. However, work in the more challenging areas of biodiversity, land degradation, and international waters—where investments are rarely based on physical capital changes—were less detailed and more hypothetical, and, in consequence, were of less practical relevance. PRINCE is currently still incomplete, and the trust funds supporting the program were closed in 2003 (they had been non-operational since 1999).³

To date, the program has failed to achieve many of its objectives. The GEF Web site dedicated to PRINCE does not appear to have been updated in

many years, still promising training material and further work and with no active links to PRINCE documents. Furthermore, no record could be found of any serious attempt to disseminate information on methodologies through workshops, training programs, or codes of practice beyond the initial set of activities conducted in 1998–99.

3.6 Conceptual and Practical Problems in the GEF Application of Incremental Costs

Unclear Concepts and Guidelines

Incremental cost policy and guidelines have been criticized repeatedly for a lack of clarity, transparency, and consistency across focal areas—and even across similar projects in the same focal area. Most of these criticisms are still valid and may be traced to the problem of additive guidelines, unclear and jargonistic explanation of basic concepts, and an apparent move into the use of project-based examples or “case law.”

The GEF Secretariat and focal area task forces (both formal and informal) have developed multiple and additive sets of policy and guidelines, with no clear distinction of which takes precedence. For example, given that the 1999 documents emphasize incremental reasoning and qualitative judgment, are the 1996 policy and guidelines relevant as they emphasize quantitative valuation and measurement? Different focal areas have developed guidelines, some of them internal (for example, those for international waters, which have not been published) and others published as Council documents (for example, those for land degradation). These guidelines deal with how to apply the concept of incremental cost, such as through cofinancing ratios, sliding scales, and cost-sharing approaches. Neither the Council nor the GEF Secretariat have clarified where or when these

different guidelines should be used, nor have they stated whether they replace earlier versions. Under such circumstances, project proponents, country recipients, and even Implementing and Executing Agencies do not have clear, transparent, and consistent understanding of how incremental cost assessments should be conducted.

Moreover, several incremental cost concepts have no clear definition and are thus subject to wide interpretation by stakeholders. Two key concepts in particular have not been clearly defined by the GEF:

- **Environmental reasonableness** has no definition, but it is to be applied when considering domestic costs and benefits in order not to penalize progressive environmental protection at the national level. The concept of environmental reasonableness has implications when distinguishing between local and global benefits, and determining their applicability for GEF funding.
- **Incremental reasoning** has no definition, but is related to qualitative assessment of the global environmental objectives or focus of the proposed GEF project. Procedurally, it implies logical argumentation and case-based reasoning, which has implications when ascertaining the basic rationale for GEF projects.

The Council has emphasized flexibility, pragmatism, and transparency in the application of incremental costs on a case-by-case basis which practically implies case-based reasoning but also entails a risk in terms of inconsistency and apparent arbitrariness at a portfolio scale, particularly when the global environmental strategies of the GEF have been imprecise.

The traditional economic approach to incremental cost assessment as it relates to physical capi-

tal investments would result in more deductive reasoning. There are, however, fundamental differences among GEF projects and the types of projects that conventional economic appraisal techniques have been designed to address.⁴ The GEF seems to have abandoned more economics-based approaches in favor of **qualitatively reasoned arguments based on experience and case law**. Under such circumstances, it is not possible to develop a standardized deductive approach to incremental reasoning, as in each project case the reasoning will be dependent on a number of complex context-specific (such as geographical or political) factors as well as previous experience and personal interpretation. This approach may be appropriate given the complex set of nonlinear problems the GEF is mandated to address, but it is currently not endorsed by the Council.

Juxtaposing Economic Methods with a Qualitative Process: A Confused Mismatch?

The GEF methodology and procedure for incremental cost assessment draws heavily on conventional approaches to the economic appraisal of projects and borrows extensively from their terminology and methods. However, there is a fundamental difference in focus:

- **Economic techniques for project appraisal are typically used to choose among projects**, to indicate the net benefit, profitability, or economic desirability of choosing one particular course of action over another or over a nonproject situation.
- **The application of incremental cost assessment to GEF projects is used to estimate the additional costs of undertaking actions to secure global benefits, as compared to the current situation** (which would have been sufficient in the national development interest)—at least in principle, even if not as it is applied

in practice. Assessment indicates the required grant financing, and provides a framework for structuring the negotiations necessary to reach agreement on global benefits and incremental costs. Although it was originally conceptualized that, among other things, incremental cost assessment would provide a means of identifying the least-cost option for generating a set of given global environmental benefits, this has not been the case in practice. GEF incremental cost assessment has never been intended to be used as a tool to compare profitability or economic returns, or to weigh the monetary costs and benefits of one project or different projects against each other.

In economic project appraisal, the common unit of measurement for both costs and benefits is usually money.⁵ However, GEF incremental cost assessment describes (in qualitative terms) the global benefits and quantifies (in monetary terms) the incremental costs of a project for the baseline scenario and the GEF alternative.⁶

Economic appraisal expresses future streams of costs and benefits in present value terms—that is, as single, current values.⁷ By so doing, the appraisal can treat costs and benefits that accrue irregularly over time as measures that are comparable with each other over the entire project lifetime. However, the GEF requirement of using present value remains a somewhat spurious one, as at no point are costs compared with each other over time in order to judge their relative profitability or economic desirability, and because costs expressed at present value do not provide an indicator of actual funding requirements (a basic aim of carrying out incremental cost assessment in GEF projects).

Conventional project appraisal techniques make a clear distinction between *economic* and *financial* analysis:

- **Economic analysis** examines the effects of projects on the economy as a whole, adjusting market prices to reflect full costs and benefits to society.⁸ As such, they are primarily carried out by the public sector and donor agencies, which are concerned with broad development impacts.
- **Financial analysis** looks only at the private returns to a particular individual or group and calculates costs and benefits at market prices, reflecting the actual profits and expenditures that people face.

In contrast, the understanding and application of the terms “economic” and “financial” in GEF incremental cost assessment is somewhat confused. There is a fundamental mismatch between the requirement that GEF funds be used to cover the “future economic burden on the country” (GEF 1996) of securing global benefits, versus the financial cost estimates that are actually provided in the incremental cost annex and matrix. In practice, it is the short-term costs of direct project expenditures (not the future economic burden or opportunity costs to a country), expressed at market prices (not at adjusted economic prices), that are calculated in the incremental cost assessment and represented in the matrix.

Thus, in practice, the juxtaposition of economic techniques and quantitative tools with what is primarily a descriptive process of GEF incremental cost assessment has led to misinterpretation and confusion—particularly as incremental cost assessment as required by the GEF has increasingly become a qualitative reasoning process. Incremental cost assessment also imparts a false objectivity by suggesting that GEF projects are subjected to a level of rigorous economic or financial analysis akin to that followed in the appraisal of other development projects. Despite being based nominally on economic techniques for

project appraisal, incremental cost assessment is not a process of economic analysis, even though it borrows widely from economic jargon. At a practical (and even pragmatic) level, the case for applying incremental cost assessment in the strict economic sense to GEF projects is problematic, probably unachievable, and largely unnecessary (Wolfe 1994, Heinzerling and Ackerman 2003).

Experiences across Focal Areas: Strengths, Limitations, and Recommendations

Application of incremental cost varies across GEF focal areas. The documentation of incremental cost at both the hypothetical and real-world levels has been concentrated on ozone and climate change projects, rather than biodiversity and international waters projects, for which systematic data are generally lacking.

Both the conceptual and practical strengths of incremental cost assessment have been noted. At a very broad level, the concept is widely accepted as attractive for determining projects and policy interventions, although most evaluations recognize that practical limitations make it difficult to apply the concept to environmental projects. The practical strengths of incremental cost assessment have been recognized in climate change and ozone mitigation projects. These projects have mostly addressed technological changes with well-defined physical infrastructure components that lend themselves to more straightforward baseline and alternative scenarios, making the quantitative and qualitative estimation of incrementality relatively easy to establish in order to justify the projects on global environmental grounds. The GEF document, “The Incremental Cost of Climate Change Mitigation Projects” (Ahuja 1994), is used as a guideline for this type of project. However, as the climate change portfolio evolves toward barrier removal and technical assistance (capacity building), the guideline is becoming less appli-

cable and the focal area is encountering problems similar to those for biodiversity with regard to incremental cost assessment.

Some studies (IIED 1999, GEF 2001) have noted that where incremental cost assessment has been applied rigorously from the beginning of project development through to approval, it has been useful in focusing objectives on global environmental benefits and leveraging cofinancing for baseline activities—thus strengthening project design. With the introduction of the logical framework approach, it has been possible—in some cases—to link incremental costs to global environmental threat analyses and identify specific activities that are eligible for GEF financing distinct from the national (local) baseline. But such links are largely dependent on the personal interpretations of IA staff, and their use is not standard practice.

The limitations of incremental cost assessment have been consistently reported in overall performance studies of the GEF since 1994 and through to the most recent OPS3. The most commonly cited limitations or problems highlighted by evaluative reports and other studies follow:

- Lack of transparency and clarity related both to estimation methods; negotiation of incremental costs; problems in establishing baselines, particularly in biodiversity, land degradation, and international waters projects; and arbitrariness of the determination of incremental costs
- Perception (particularly among country recipients) that incrementality is open to significant manipulation due to a lack of clear guidelines
- Limited negotiation among stakeholders—primarily with recipient countries (project proponents)
- Lack of understanding among countries of incremental cost assessment

- Lack of in-country expertise and capacity to carry out incremental cost assessment
- Lack of guidelines
- Lack of motivation/initiative, leading to self-exclusion
- Use of international incremental cost consultants, which creates an expert process and reduces participation

Table 3.4 provides a summary and ranking of the strengths and limitations as reported in evaluations and other reports, and shows that reporting of limitations outweighs the reported strengths of incremental cost assessment.

Since the GEF pilot phase evaluation (UNDP, UNEP, and World Bank 1994), all subsequent overall performance studies have provided a recommendation on incremental cost assessment. The pilot phase evaluation, OPS1 (GEF 1998a) and OPS3 (GEF 2005) requested that the GEF Secretariat develop improved guidance on incremental cost assessment. OPS2 (GEF 2002) requested that the GEF Secretariat develop a negotiating framework to “agree” on incremental costs in a more participatory way. Analyses of previous evaluation reports indicate that most recommendations have focused on general project design procedures relating to incremental costs, financing, guidelines, and negotiation. Unfortunately, none of the evaluations have provided specific recommendations on how to solve the problems found.

The GEF Secretariat response to recommendations has been inconsistent. Between 1994 and 1999, the GEF Secretariat invested significant attention in developing and refining incremental cost guidelines in response to recommendations of the pilot phase evaluation and OPS1, and GEF Council decisions. However, since 2000, little progress has been made in resolving outstanding

Table 3.4

Incremental cost assessment: strengths/limitations

	Factor	Reporting frequency
Strengths	Application in ozone and/or climate change projects	5
	Concept/principle has theoretical attractiveness	4
	Useful in strengthening project design ^a	2
	Assists in leveraging cofinancing	2
	More effective when applied early in project design cycle	2
	Baseline estimation improves if linked to threat analysis/logical framework	2
	Incremental cost assists countries in guiding timing/sequencing of policy changes	1 ^b
Limitations	Lack of clarity and transparency (in estimation and/or negotiation)	11
	Difficult to establish baseline	10
	Arbitrariness (caused by lack of guidelines and differing interpretations of incremental costs)	8
	Lack of negotiation among stakeholders ^c	7
	Relationship between global and local benefits unclear, leading to confusion over what is GEF-able	7
	Lack of knowledge/understanding and awareness	7
	Lack of accountability and responsibility	4
	Leads to retrofitting (incremental cost driven by availability of cofinancing)	4
	Encourages a narrow project design and/or approach	3
	Reduces incentives for stakeholder participation	3
	Weakens country ownership/partnership	2
	Difficult to estimate alternatives	1

Note: Table is based on content analysis of GEF overall performance studies, cross-cutting evaluations (for example, the Role of Local Benefits in Global Environmental Programs), external expert reviews, and country case studies.

- Improves logical reasoning and focus on global environmental benefits in project preparation.
- Reported in one country case study.
- Recipient country (project proponents—communities, NGOs, government departments, and institutions), IAs, and GEF Secretariat.

limitations in incremental cost assessment. Notably, there was no response to the OPS2 recommendations or to the Second GEF Assembly (2002).⁹ The replenishment negotiations for GEF-4 have included a request to the GEF Secretariat and IAs to prepare new guidelines on incremental costs by June 2007. The request also indicated that the present evaluation findings and recommendations should be taken into account.

The interest of the GEF Council and Assembly in incremental cost assessment has been fairly consistent. For example, between 1995 and 2005, 15 decisions were made with regard to incremental

cost assessment, of which 6 repeated overall performance study recommendations for improvements in negotiation, clarity, and simplicity of application in projects. The remainder expressed the importance of the principle to the GEF with regard to new activities such as land degradation/sustainable land management and adaptation to climate change. Indeed, more recent GEF Council decisions and discussions of incremental cost have tended to focus on the principle with regard to preserving the GEF global environmental benefits mandate vis-à-vis new operations in areas where the distinction among global, national, and

local is becoming increasingly difficult to define conceptually and/or practically.¹⁰

Notes

1. This indicates that projects were funded on a “gross incremental cost” basis. Source: www.multilateralfund.org.
2. During this evaluation, the GEF Evaluation Office requested each focal area task force to provide a note on how incremental cost is applied in its focal area. International waters, biodiversity, and land degradation provided notes. Only one of these—that on land degradation—is a public document, since this focal area is discussing the issue with the GEF Council; the others have not been made public by the respective task forces.
3. The budget for PRINCE was divided into two trust funds: Trust Fund 1, \$2.6 million; and Trust Fund 2, \$450,000. Trust Fund 1 disbursed \$1.814 million, and Trust Fund 2 disbursed \$135,661. A total of \$1.104 million was not disbursed at the closure of the funds in 2003. (All dollar amounts are current U.S. dollars.)
4. GEF projects predominantly tend to address the required human capital changes of the global environmental—a development nexus that does not lend itself to incremental cost assessment because of problems in establishing baselines and alternative economic and financial values.
5. Various forms of appraisal that are based on qualitative indicators or that combine monetary and nonmonetary measures may also be used, including multicriteria analysis, decision analysis, and risk-benefit analysis.
6. The lack of any requirement to quantify global benefits is reasonable. Conventional economic and financial appraisal tools were designed primarily to deal with infrastructure projects, where both costs and benefits can be measured easily through observable physical inputs and outputs, and economic pricing requires relatively few adjustments to market prices. GEF projects, however, are primarily concerned with improving environmental status (rather than generating commodities or physical outputs) and with capacity building and barrier removal (rather than with capital investments). These variables are typically much harder to quantify, because they tend not to be expressed via markets and prices, or are undervalued by the market.
7. This applies a discount rate (essentially the inverse of applying a compound interest rate) to future costs and benefits, and values relatively less weight the further into the future they accrue. It accounts for the fact that people generally prefer to enjoy benefits now and costs later, and that any funds tied up in a project could be used productively to generate returns or profits elsewhere.
8. In practice, this mainly involves eliminating the effects of taxes, subsidies, and other distortions, and quantification of those components of the costs and benefits that are not monetized by the market.
9. OPS3 confirmed the lack of action with regard to incremental costs (GEF EO 2005).
10. For example, the recent discussions of the “scope and coherence of land degradation activities” at the June 2005 Council Meeting and of the local benefits evaluation in November 2005 highlighted the uneasy (and perhaps untenable) distinction made between global and local benefits, when in many cases they are inexorably linked (GEF 2005a and 2005b).

4. Incremental Costs in Practice

4.1 Compliance and Quality of Incremental Cost Reporting

The GEF Council and Secretariat have provided guidance about the procedures that should be used for estimating incremental costs and have laid out how incremental cost should be reported in project documents. In particular, the annex to the 1996 GEF policy on incremental cost establishes that each project proposal must report on six specific aspects of the incremental cost assess-

ment: broad development goals and baseline, global environmental objective, alternative, scope of the analysis, costs, and process of agreement (see table 4.1 and chapter 3).

As all of the projects reviewed have been CEO endorsed, it might be concluded the GEF review system has agreed that the projects' incremental cost annexes are compliant in terms of content and acceptable in terms of the quality required for project approval. The evaluation does not sup-

Table 4.1

Incremental cost policy requirements for incremental cost reporting: 1996

Broad development goals and baseline	The relevant broad developmental goal of the country; the way the country can reasonably be expected to address the above development needs in its own economic interests.
Global environmental objective	The objective of the proposal to the GEF, namely to avert specified consequences for the global environment of the above baseline course of action.
Alternative	The proposed way to meet the baseline developmental goals and the global environmental objectives simultaneously. The alternative will generally be the least-cost option. If the domestic benefits of the proposed alternative and the baseline accrue to different groups of people, this section should briefly discuss how any redistributive effects of the alternative would be addressed.
Scope of the analysis (system boundary)	This includes all the significant differences between the alternative and the baseline course of action. Any changes caused by the alternative—not only in the project itself but also in terms of any major downstream impacts, sectoral shifts, system adjustments, additional domestic benefits, and side effects.
Costs	Costs and benefits and cost effectiveness (represented in a matrix); all the economic costs within the system boundary of the proposed alternative course of action and those avoided by not undertaking the baseline course of action. This section will identify and provide preliminary estimates for the relevant costs. Costs should be estimated in present value terms. Assumptions about discount rate, time horizon, and so on, should be stated, and divergence from standard figures used elsewhere mentioned.
Process of agreement	Proposed manner of reaching agreement with the relevant technical counterparts and authorities.

port this conclusion; the reviewed projects are less than satisfactory on both counts. Half of the required subsections are missing from the majority of project documents, and most annexes contain notable weaknesses in technical quality in four out of the six specified incremental cost elements (see table 4.2).

Although there are few differences in the overall technical quality of incremental cost annexes among the various Implementing Agencies and focal areas, it is clear that each has different areas of emphasis, strength, and weakness with regard to incremental cost assessment (see table 4.3).

All projects are required to include a separate annex or section on incremental cost assessment

Conclusion: Most project documents register low quality and compliance when measured against GEF requirements for incremental cost assessment and reporting.

in the project document, dealing individually with each of the six specified steps.¹ Although almost all FSPs provide a separate section (and/or annex

on incremental costs, this is present in only half of MSPs. A relatively higher proportion of UNDP MSPs (two-thirds) include a separate annex on incremental costs as compared to the project documents submitted by the other IAs.

In specifying six required steps in incremental cost assessment, and outlining the formats that are required for reporting on them, the 1996 incremental cost policy provides a series of convenient “check boxes” which can be followed in project preparation, reflected in project documents, and assessed by reviewers. Half of these six boxes can be checked for most of the reviewed project documents (development goals/baseline, global environmental objective, alternative); the remaining three steps in incremental cost assessment (scope of analysis, costs, and process of agreement) commonly remain unreported in the majority of projects. The technical quality of assessment of the alternative, scope of analysis, costs, and process of agreement is weak—or missing altogether—in most incremental cost annexes reviewed. Key incremental cost elements and concepts are frequently misrepresented or misunderstood, or suffer from weak assessment and description; and

Table 4.2

Compliance and technical quality of incremental cost reporting (percentage of projects)

Criterion	Compliance/inclusion			Technical quality Strong/adequate
	FSPs	MSPs	All projects	
General aspects				
Incremental cost annex/section	96	51	76	55
Incremental cost matrix	92	44	71	56
Specific aspects				
Broad development goals/baseline	96	48	75	63
Global environmental objective	59	6	36	80
Alternative	95	55	78	48
Scope of the analysis	36	3	22	49
Costs	96	68	84	46
Process of agreement	0	0	0	17

Table 4.3

Technical quality of incremental cost reporting by project IA and focal area

IA/focal area	All criteria	Broad development goals/baseline	Global environmental objective	Alternative	Scope of the analysis	Costs	Process of agreement	Coherence and fit
Percentage of criteria ranked strong/adequate								
UNDP	55	64	79	50	58	43	14	65
UNEP	51	67	80	43	19	45	15	49
World Bank	57	62	80	49	50	51	22	74
Biodiversity	53	62	81	43	37	47	2	69
Climate change	62	68	89	66	46	53	27	64
International waters	40	47	91	32	25	23	9	52
Land degradation	52	63	41	33	92	44	29	70
Multifocal	84	89	100	82	100	69	50	100
Percentage of criteria ranked weak/absent								
UNDP	40	33	21	44	42	43	86	34
UNEP	41	30	20	38	62	44	65	51
World Bank	35	35	20	39	48	32	70	20
Biodiversity	41	38	19	49	55	39	90	29
Climate change	32	27	11	27	54	33	73	36
International waters	45	45	9	41	75	56	73	32
Land degradation	43	36	59	60	8	42	67	30
Multifocal	12	11	0	14	0	17	50	0

Note: The sum of strong/adequate and weak/absent does necessarily total 100 percent, as not all criteria are applicable to all projects.

some of the most important elements of incremental cost are treated in a cursory manner.

Baseline Scenario

Although three-quarters of the project documents reviewed contain a description of the baseline scenario, these are often inconsistent and/or misrepresented. More than a third of the projects present a baseline scenario that is not justifiable in terms of technical feasibility (although projects in the biodiversity focal area are markedly stronger in this respect), leading to questions about the credibility of the baselines described. This conclusion is reinforced by interviews carried out with GEF Secretariat and IA staff, who state that there is a

tendency to “construct” or “manipulate” baseline situations to suit the purposes of a particular project (for example, to satisfy cofinancing ratios or justify the intended course of alternative action after the project has been designed; this is commonly referred to as “retrofitting”). At the extreme, the requirements of incremental cost assessment provide perverse incentives for countries to reduce the baseline to as low a figure as possible, in order to maximize cofinancing and GEF funding.

While the majority of survey respondents and interviewees claim to understand the concept of “baseline,” there remains confusion about how to assess, represent, and define it in practice. The

data collection required to assess baseline costs is seen as one of the most difficult aspects of incremental cost assessment, both because of the problems involved in accessing sometimes confidential or politically sensitive budgetary and financial data as well as the somewhat blurred and indefinite nature of “business as usual.” This difficulty pertains particularly when projects start as a GEF concept (or alternative) rather than, as originally anticipated, as a development project for which a GEF alternative is added. Trying to create a baseline for a “stand-alone” GEF project was reported to be challenging. Difficulties in distinguishing a clear baseline were flagged most often by respondents involved in preparing projects in the biodiversity and land degradation focal areas. Climate change projects, too, are beginning to face similar challenges, as strategic priorities change from a focus on technology transfer and capital investment to market transformation and capacity building. Baselines for the latter are considerably “softer” and difficult to assess accurately. Under such circumstances, opportunities for baseline manipulation or misrepresentation are likely to increase.

GEF funding is based on the rationale that if the unmodified baseline status quo is maintained, the global environmental benefits will either reduce or accrue at a less than desirable level. In reality, this is articulated very poorly in many incremental cost assessments. More than a third of the project documents reviewed do not make explicit the threats arising from an unmodified baseline (this includes half or more of UNEP and international waters projects), and almost half do not describe these threats in terms of global environmental effects (including two-thirds of international waters and land degradation projects).

Global Environmental Objective

Although a relatively low proportion of projects (just over a third, and only 6 percent of MSPs)

explicitly state the global environmental objective in the incremental cost annex, where this is missing it is included elsewhere in the project document (interviewees often considered this to be an unnecessary duplication). For most projects, the global environmental objectives as presented in the main part of the project document or in the annex, are clear and focused, and linked to the GEF mandate and focal area strategic priorities—thus demonstrating incremental reasoning.

Alternative

The vast majority of FSPs describe a GEF alternative that meets both baseline goals and the global environmental objective and that claims to overcome the threats implied by an unmodified baseline. More than a third of the projects reviewed, however, do not make explicit what these threats, or their global environmental effects, are. Further, more than a third do not describe more than one alternative to the baseline situation, meaning that they provide no evidence that the proposed alternative is the least-cost option to achieve a given global environmental objective. Even in projects where assessment of cost effectiveness is provided, it is of strong or adequate quality in only half of the instances.

Scope of the Analysis

Only a fifth of the projects reviewed identify or describe the system boundary within the annex. The reasons for this omission are related primarily to a lack of awareness of the policy and guidelines, and hence poor understanding. For example, over half of the online survey respondents did not understand the term, and most interview respondents were unaware of the need to include this section in the incremental cost annex.

Costs

Ninety-two percent of FSPs and 44 percent of MSPs include an incremental cost matrix, and

almost all provide a section on costs, but these routinely miss key elements. Only half of the projects reviewed describe incremental benefits in the matrix, and almost a fifth do not describe baseline and alternative situations. According to the compliance review, project costs are rarely specified in present value terms (although the incidence of net present values being presented is much higher among projects prepared by the World Bank, which also tend more frequently to refer to financial and economic appraisals of the development/investment project to which the GEF actions are linked).²

Analysis of project funding and additionality is weak, as are general levels of understanding about the categorizations of different sources of funds according to GEF definitions of “cofinance,” “leveraged,” and “associated” funding.³ Almost a third of the projects reviewed (including 80 percent of those in international waters) provide an inadequate rationale for project cofinancing, and less than half identify associated and leveraged funding or are clear about how they are distinguished from cofinance. More than half of the projects do not provide sufficient evidence that GEF funding is genuinely additional (with no crowding out or substituting for other preexisting sources of funds), reflecting the generally weak understanding of the term “additionality” expressed among survey and interview respondents.⁴

Incremental cost sections also are required to identify and analyze baseline threats in terms of their socioeconomic and distributional effects, and discuss how any redistributive effects of the alternative will be addressed. In practice, only half of the projects reviewed describe baseline threats adequately, just a third describe the socioeconomic and redistributive effects of the alternative, and more than half contain no plan at all for mitigating negative redistributive effects.

UNEP projects are particularly weak in analyzing the redistributive and socioeconomic effect of the GEF alternative (60 percent absent), as are projects in the biodiversity focal area (62 percent).⁵ This analysis is absent overall for 62 percent of the projects (including almost three-quarters of climate change and international waters projects).

Process of Agreement

Descriptions of the process of agreement on incremental costs is the weakest aspect of incremental cost reporting. None of the projects reviewed contain a specific section within the annex, or anywhere else in the project document, on process of agreement. Of those projects that made some mention of the process of agreement elsewhere in the annex or project document, more than 83 percent were weak on the point. Nearly a third of the survey respondents stated that they were unaware that a description of the process of agreement is required, and three-quarters of those who were aware of this requirement (including over 90 percent of IA staff) reported that they do not include a subsection on the process of agreement in incremental cost reporting.

4.2 Conduct of Incremental Cost Assessments

The “who,” “how,” and “when” requirements for conducting incremental cost assessments are provided in the 1996 incremental cost policy and further elaborated in the streamlined procedures and principles for agreement (GEF 1996, 1999a, and 1999b) (see table 4.4).

The streamlined procedures and principles for agreement specify that the country partner should jointly undertake the incremental cost determination with IA support. The evaluation found that incremental cost assessment and reporting are almost always conducted by international con-

Table 4.4

Roles and responsibilities in the incremental cost assessment process

Stakeholder	Role	Responsibility
Country partner/ recipient agency	Project sponsor/ originator	<ul style="list-style-type: none"> Jointly undertakes incremental cost determination with the IA and Collects and analyzes relevant country data Identifies stakeholders for broader consultations and organizes a logframe or project development/consultation workshop Conveys basic incremental cost principles to other stakeholders
GEF operational focal point	Project reviewer/ facilitator	<ul style="list-style-type: none"> Reviews projects, endorsing their consistency with respect to national programs, and confirming national priorities Facilitates broad as well as project-related consultations, particularly with government agencies
Implementing Agency	Assists in project preparation/ information provider	<ul style="list-style-type: none"> Supports country efforts to prepare projects, particularly with respect to implications of GEF policies and procedures, such as incremental cost Facilitates the processing of these proposals through the GEF Activity Cycle Informs 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
GEF Secretariat	Project reviewer	<ul style="list-style-type: none"> Upon entry into the pipeline, reviews the incremental reasoning of the concepts submitted by an IA or regional development bank and provides feedback on eligibility At entry into the work program, reviews the incremental cost assessment (baseline scenario, GEF alternative scenario, and incremental cost components) At CEO endorsement, reviews the final incremental cost determination and checks for consistency with the work program inclusion document

sultants or IA staff. There are some differences among IAs. The World Bank mostly conducts the assessment as an internal/in-house exercise as part of the project design process; UNEP follows a similar practice, but also uses international consultants in new focal areas such as land degradation; UNDP tends to use a small group of international consultants who are usually also involved in advising national proponents/governments on project design as well as in writing the project document.

In reality, then, there is little direct participation of the country partner in carrying out the incremental cost assessment. In practice, the role of recipient governments and project proponents is primarily to provide information and data (particularly information on the baseline situation). This is a passive form of participation rather than the

country's serving as an active partner. Although in some countries with significant GEF portfolios, in-country expertise, and willing IA staff (see box 4.1), participation was reported to be more active, this remains the exception rather than the rule.

Factors that are claimed to reduce broader stakeholder involvement in incremental cost assessment

Conclusion: As currently applied, incremental cost assessment and reporting do not add value to project design, documentation, and implementation.

include poor understanding and low awareness, and the absence of clear guidelines—meaning that incremental cost assessment remains the domain of “experts.” Many IA respondents stated that, for

Box 4.1

Brazil: Participation of Country Recipients in Incremental Reasoning and Assessment

For the World Bank project Ecosystem Restoration of Riparian Forests in São Paulo, state government officials have been actively involved in project incremental reasoning and incremental cost assessment. Incremental reasoning was used to agree on (negotiate) GEF-eligible activities with the state government officials during concept and project development facility workshops. Working with government officials, staff from the World Bank and the Food and Agriculture Organization of the United Nations (FAO) were then able to identify the necessary local aspects for which cofinance would be required from them, and global aspects for which the GEF would pay. Brazil has a significant GEF portfolio, and Bank-FAO staff reported that incremental cost assessment and reasoning is more widely understood because many government officials have been involved in preparing previous projects. Furthermore, the Bank-FAO staff involved reported that they try to introduce incremental reasoning early in project formulation so it can be used in guiding project design.

these reasons, they feel it to be quicker and more cost effective to use either their own staff or tried-and-tested international consultants to carry out incremental cost assessments.⁶ This results in a lack of transparency, which was reported by two-thirds of survey respondents and many project proponent interviewees—a finding consistent with previous GEF overall performance studies.

There is wide variation in understanding of the nature of incremental cost assessment among the various stakeholders in GEF projects, and confusion about its role in project conceptualization, design, and implementation. While nearly half of the respondents to the online survey and the overwhelming majority of those interviewed (particularly IA staff) see incremental cost assessment as a (primarily qualitative) form of logic or reasoning, just under a third (mainly non-IA staff)

perceive it to be a quantitative, numerical calculation. A quarter of survey respondents felt they did not understand the term “incremental cost” itself very well (although most interviewees disagreed with this perception, claiming that the

Conclusion: There remains weak understanding and much confusion about incremental cost concepts and procedures.

term is well and widely understood). Most of the online survey respondents reported that they have good understanding of the terms “baseline” and “cofinancing” and of the concepts of national and global benefits; but they reported a much weaker understanding of other concepts such as alternative, additionality, and system boundary.

Low awareness of incremental cost guidelines among recipient governments and project proponents exacerbates their lack of participation in incremental cost assessment. Although there is a high knowledge of the existence and content of GEF incremental cost guidelines among key operational stakeholders (such as the GEF and IAs), far fewer government partners/proponents and focal points are aware of their existence. Awareness and use of PRINCE documents was particularly low—nearly three-quarters of survey respondents did not know of their existence or did not consider them useful.

One factor responsible for low awareness and use of guidelines on incremental cost is the very weak communication and outreach conducted by the GEF Secretariat since the introduction of the incremental cost requirement into project design. Few concerted efforts have been made to disseminate guidelines, to translate them into languages other than English, or to raise awareness and understanding about their content and use. The

National Dialogue Initiative workshops included two or three slides on incremental cost concepts, but these were reported by interviewees to be insufficient for raising awareness and of no use for guiding country recipients and proponents in how to do incremental cost assessment. Furthermore, although the GEF Web site provides a series of documents on incremental cost (primarily in English), given the overlapping and additive nature of the guidelines (as described in chapter 3), it is difficult for the public to discern on its own what incremental cost is about and what documents to use for guidance.

Even where there is awareness and knowledge of GEF incremental cost guidelines, they are widely perceived as not being useful. Common reactions are that the documents are not clearly written, are full of GEF jargon, and are too conceptual and/or academic to be useful in an operational sense. Furthermore, those interviewed often reported that incremental cost is not an easy concept to explain to a non-English audience (see box 4.2); GEF documents and guidelines on incremental cost have never been translated from English into any of the other GEF languages. At best, the guidelines seem to function only as an initial reference point for conceptual terminology and definitions; even then, there are problems in understanding the guidelines as a practical tool. PRINCE, Council documents, and the National Dialogue workshops have not been successful in increasing understanding and clarity of the incremental cost concept or of assessment and reporting requirements.

Model project documents, not GEF guidelines, are used to guide incremental cost reporting. Nearly three-quarters of survey respondents cited already approved project examples as their main (and most useful) source of reference. Although the use of project examples has clear advantages in terms of providing real-world applications, it cannot

Box 4.2

Lost in Translation

One of the key barriers to a wider understanding of the incremental cost concept and process is associated with difficulties in cross-cultural understanding and translation. IA and GEF Secretariat staff involved with National Dialogue Initiative workshops stated that the concept does not translate well into many local languages such as Arabic, Chinese, Russian, and Swahili. This forces proponents and IA staff to either think up creative ways of translating and explaining the concept to stakeholders, or avoiding using the terms altogether with country recipients and other local stakeholders. In many cases, IA staff reported that they minimized the use of incremental cost terms in workshops, preferring instead to emphasize global environmental benefits/significance as the key rationale for GEF support (equating to incremental reasoning). Some proponents did develop creative ways of bridging the cross-cultural gap. For example, World Wildlife Fund staff in Nairobi preparing a UNDP-GEF project for East African Coast Forest Conservation explained incremental reasoning to stakeholders in Swahili in these words: “GEF is coming to make life a bit better and make you work a bit harder...doing what you do now but better.” The word “incremental” was never used, as it is seen as “GEF or donor-driven language” and not the language of country recipients or other local stakeholders.

adequately provide guidance on *how* incremental cost assessment needs to be done. Widespread use of a relatively small number of “successful” project documents as a model for best practice also runs the risk of perpetuating particular myths, misinterpretations, and omissions in incremental cost assessment, resulting in a “cut-and-paste” approach to reporting.

4.3 Role of Incremental Costs in Project Design

The concept of incremental reasoning (first documented in GEF 1999a and 1999b) is held up as the starting point for determining incremental cost

and the key element in determining conceptual conformity when a project first enters the pipeline, but this term has never been defined explicitly. By implication, *reasoning* encapsulates the basic rationale for a project seeking GEF funding: the global environmental objectives and use of GEF funds to contribute to the additional cost of actions required to secure these global benefits. Incremental reasoning should thus be applied in designing a project that will transform a scenario with national benefits into a course of action that generates global benefits, where GEF funding will cover the incremental cost.

The evaluation found that this kind of big-picture thinking or logic is, indeed, an important factor in the design of GEF projects, and incremental reasoning remains the guiding concept, despite the almost total absence of any explicit definition of the term in GEF documentation. Although there is widespread confusion about the steps, terminology, and reporting requirements for incremental cost assessment, there is a common agreement that key principles of global benefits, incremental cost, and additionality drive the conceptualization and design of GEF projects from the earliest stage of the Activity Cycle. IA and GEF Secretariat staff who are primarily responsible for formulating the initial scope and focus of GEF projects reiterate the importance of such a qualitative form of logic or reasoning to inform and justify the selection of GEF-able projects and activities. Interviewees repeatedly referred to incremental reasoning in relation to the process of thinking about GEF projects associated with the global environmental mandate and objectives of the GEF and focal area strategies. In essence, incremental reasoning implicitly informs strategic choices made by country recipients under the guidance of IA staff.

In principle, incremental cost assessment provides a mechanism or framework for applying

incremental reasoning during project design. However, as currently applied, incremental cost assessment and reporting procedures do not enhance GEF project design or the integration of incremental reasoning.⁷ Incremental cost assessments are not seen as integral to project design, but rather—in most cases—as a separate justificative end component. They are largely perceived as a one-off exercise, carried out to fulfill reporting requirements and gain project approval. Rather than incremental cost assessment being seen as something that drives GEF projects and is continuously interwoven into project design, it is commonly perceived as a bureaucratic procedural and reporting requirement for project documents—a hoop to be jumped through if a project is to be

Conclusion: The principle of incremental funding is alive and well in GEF projects.

approved by the GEF Secretariat and Council. Notably, the majority of interviewees reported that the incremental cost assessment is never revisited or used during project implementation or evaluation. On the other hand, incremental reasoning and the global environmental mandate of the GEF project *is* implicitly used to keep the project on the right track, particularly if adjustments in the design and selection of activities are required during implementation.

4.4 Use of Incremental Cost Assessment to Determine GEF Funding and Cofinancing

The 1996 policy envisaged that incremental cost assessment would serve to “judge the level of GEF funding,” provide “a reference value for the required grant financing,” and “indicate the funds that will need to be mobilized” (GEF 1996). Incremental cost assessment is also termed the frame-

work that “structures the technical negotiations necessary to reach agreement in each case.”

The evaluation found little evidence that incremental cost assessment is used to determine GEF funding and cofinancing, or to structure negotiations and agreement. In reality, the amount of GEF funding for a project tends to be set (within a range) early in the Activity Cycle, and primarily involves negotiation between the GEF Secretariat and IA staff (rather than between the GEF and the recipient, as specified in the policy). These negotiations are typically based on overall GEF focal area budget allocations, availability of funds in the GEF, country context (including IA discussions with the government or other proposed recipients), and cofinancing—rather than on the incremental cost assessment, as specified in the 1996 policy and the 1999 streamlined procedures and principles of agreement. At this stage, no assessment has been carried out of the baseline situation, and there is limited information on cofinancing availability or on the costs of producing global environmental benefits in the particular country context.

As well as bringing into question the ideal of incremental costs being “negotiated” and “agreed” between the GEF and the country recipient, this predetermination of GEF funding early in the Activity Cycle means that there is a tendency to use the subsequent incremental cost assessment to verify this initial figure, rather than have it serve as a reference value to determine project funding, GEF contributions, and amount of cofinance. Interviews clearly indicated that respondents consider that incremental cost estimation tends to take as a starting point the predetermined amounts for GEF funding, and then fits the project budget around this amount.

Once the project budget has been calculated, donors are approached to provide cofinancing

to cover the balance of costs over and above the amount of GEF funding available. An additional filter is applied through the use of preset cofinance ratios, based on the predetermined GEF funding figure. The interview respondents believed that securing these ratios was a critical determinant of project approval, and perceived significant pressure to raise specified levels of funds. To a certain extent this implicit use of cofinance ratios has been formalized for climate change projects.

There is a very broad interpretation of what should be included in cofinancing. In 2003, the GEF Council approved a document containing definitions of “cofinancing” as well of as other related terms such as “leveraged financing” and “associated financing” (GEF 2003). The definitions are vague, and leave much room for case-by-case interpretation. Typical examples include large World Bank projects in which an entire sector adjustment reform—for example, in energy—is considered cofinancing; the GEF component may include a small demonstration site for renewable energy.

The application of preset amounts of GEF funding and cofinance ratios undermines the utility of incremental cost as a framework for broader negotiation or as a methodology for calculating incremental costs and funding contributions from GEF and other financiers. It promotes a situation where the project budget is fitted around the total figure of available funds (that is, the predetermined GEF figure plus the amount of cofinance required according to the application of cofinancing ratios). The need to reach certain ratios also introduces incentives for baseline/cofinance manipulation (commonly referred to by interviewees as “baseline fudging”) in order to inflate or deflate the cofinance and/or baseline to suit the demand for a particular ratio vis-à-vis the programmed GEF funding and specified cofinance ratios (see box 4.3).

Box 4.3

**Incremental Cost Assessment:
Waving a Magic Wand**

The following quote from an interview with a long-standing staff member from one of the IAs summarizes a common view: that incremental cost assessment is used to retrofit rather than determine GEF funding decisions in projects. “In my view, baseline and cofinance calculations are a bit of higgledy piggledy and jiggery pokery. When does baseline become baseline and cofinance become cofinance? You wave your magic wand and decide. It is what suits your purposes in a given context.”

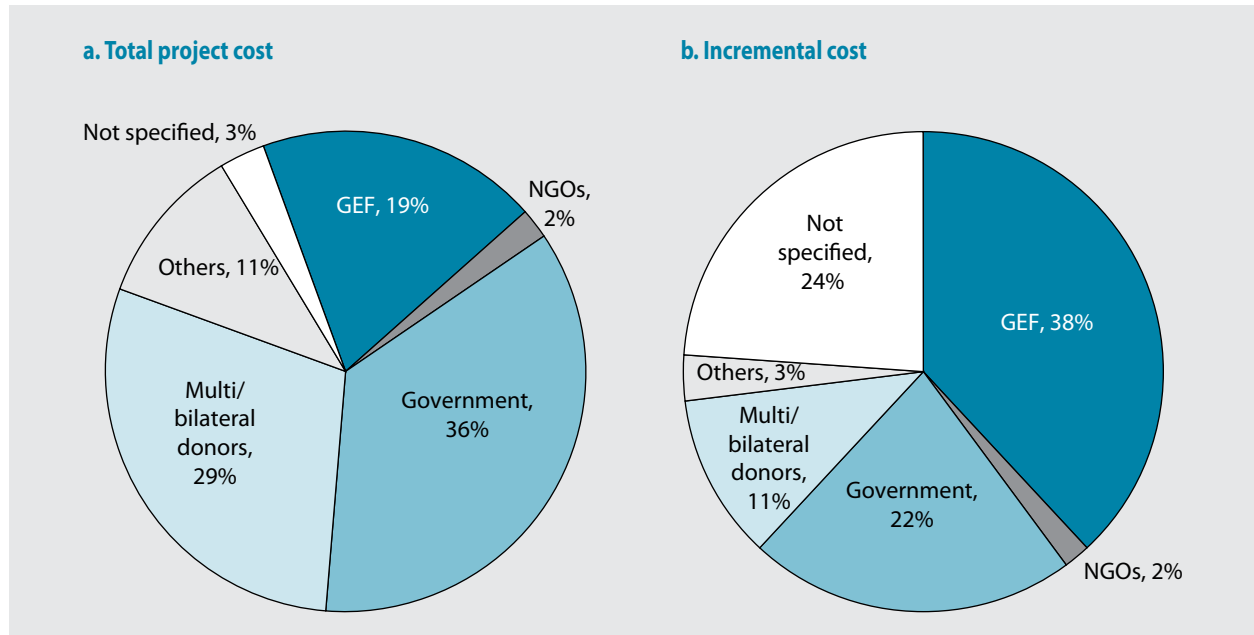
The evaluation found evidence that GEF claims of leverage have been overestimated. For the projects reviewed, the GEF contributed an average of 18.5 percent of total project funding (alternative plus baseline) (see figure 4.1a), with markedly higher contributions to smaller projects of less than \$5 million (40 percent), UNEP projects (34 percent), biodiversity projects (27 percent),

and multifocal projects (28 percent). This corresponds to the figure, generally cited for the GEF, of there being four times as much cofinancing as GEF funding.⁸ The prevailing impression—that every GEF dollar generates four additional dollars from other donors—is not borne out by analysis of financing of incremental costs. GEF funding for incremental costs is, on average, just under 40 percent (see figure 4.1b); this translates to a leverage ratio of just 1:1.6.⁹

The evaluation found that governments are the most important source of cofinance for project costs and incremental costs. For the incremental cost of actions required to produce global environmental benefits, governments on average contribute over half (58 percent) of non-GEF cofinance for which sources are known (all projects); multi-lateral and bilateral sources contributed just under a third (29 percent). For the non-GEF cofinancing of incremental costs among medium-size projects for which the source of cofinance had been speci-

Figure 4.1

Sources of cofinance



fied, governments make a relatively larger contribution (61 percent), while bilateral and multilateral donors contribute much less (just 14 percent). Of total project costs, governments contribute just under half (44 percent) of non-GEF funding, and bilateral and multilateral donors just over a third (36 percent). For MSP total costs, the figures are around a third each for government and bilateral/multilateral contributions to non-GEF costs.

There was significant variation among interviewees (particularly IA and GEF Secretariat staff and project proponents) about which activities (or even projects) are eligible for GEF funding. Some IA staff held the view that incremental reasoning could not include local costs or incentives for global environmental benefit generation. In contrast, others held the more pragmatic view (within the context of changing GEF focal area strategies) that the GEF could fund local activities such as alternative livelihoods and/or demonstration projects for communities. This was particularly the case in land degradation and biodiversity projects. In practice, decisions about the GEF-ability of project activities seemed to depend largely on the personal interpretations of IA task managers and international consultants. It was acknowledged that such aspects had to be carefully supported in the project rationale with incremental reasoning in order to get through the GEF Secretariat and Council review procedures. Several IA and GEF Secretariat staff members highlighted instances where unorthodox perceptions of local and global benefit linkages in climate change and biodiversity projects came into conflict with project sustainability and replication (see box 4.4).

The lack of operational guidance and clarity regarding the relationship between local and global benefits has already been noted (GEF EO 2006b). This evaluation supports that conclusion, and finds that there is widely varying interpreta-

tion (and much confusion) about what is and is not eligible for GEF funding and can therefore be considered de facto incremental. In practice, project proponents and IA staff pointed out that incremental costs occur at different scales from the local and national. It is therefore unrealistic for incrementality to be used to reduce or not to fund local incentives and cover costs needed to support global environmental benefit generation in instances when these cannot be partially or fully funded by cofinance.

Notes

1. GEF operational guidance for the preparation and approval of projects, project review criteria, and annotated outlines for proposals all demand that both FSPs and MSPs include a separate section on incremental cost assessment in the project document.
2. Only 2 percent of the FSPs (two projects) and none of the MSPs present incremental costs in present value terms, including specification of the rate of discount. The projects that do so are climate change projects jointly developed by the World Bank and the International Finance Corporation.
3. GEF (1999b) emphasizes that the financing package in GEF projects traditionally includes reference to cofinancing, leveraging, and associated financing and that it is important that each of these financing features be interpreted and understood in a consistent manner. Although cofinancing, and by extension leverage, is largely interpreted as new and additional resources to implement the GEF intervention, nonleveraged baseline financing is recognized as equally important. With a programmatic focus, the importance of associated financing is enhanced. GEF programmatic financing will have to be nested within given national (sustainable) development baselines; in this regard, it is critical to have a clear indication of such associated financing. Even though this financing may not be directly leveraged by the GEF, it clearly represents the baselines upon which global environmental objectives can be accrued.
4. The evaluation was unable to assess GEF mandate requirements for funds to be “new and additional,”

Box 4.4

To Fund or Not to Fund?

Many IA interviewees noted that the most complex part of applying incremental reasoning was separating global and local activities for the purpose of making decisions on funding. In many cases, this is a rather difficult and artificial process, in which national proponents and/or governments are not always actively involved.

In most cases, to generate global environmental benefits, local incentives are required in order to promote changes in human behavior and improve sustainability in the long run (after projects have been completed); hence, separating GEF grant contributions and baseline costs is not always relevant or possible. This is exemplified in the types of incremental reasoning/assessment that have been applied in past and present projects.

In 1996, during the preparation of the World Bank Ghana Natural Resource Management project, the Bank invested a significant amount of project development facility funds in conducting an economic analysis of incremental costs. The results of the study found that incremental costs of setting up forest conservation were primarily distributed at the local level—in essence, the local communities would be paying for global environmental benefits because of restrictions on access. The GEF Secretariat refused to accept “this nonstandard incremental costs analysis” that did not conform to its interpretation, and asked the Bank to remove the analysis from the project appraisal document. The result was a synthetic incremental cost assessment that showed the bulk of costs falling at an institutional (national) level, which was what the GEF Secretariat was willing to define as incremental (that is, anything but local-level costs). The Bank team held the view that they had to conform to what the GEF Secretariat wanted in order to get the project approved, and so the incremental cost field assessment was removed from the project document—despite the perception that the sustainability of the intervention was weaker. The project failed to achieve many of its conservation objectives.

More recently, several climate change sustainable transport projects for Ghana and Vietnam have included minor sidewalk and traffic management improvements as incremental costs payable by the GEF—to enable strong incentives for people to use public transport in Accra and Hanoi to produce global environmental benefits (emission reductions). These costs have been challenged by GEF Council members on the grounds that they are local benefits and should be paid for out of the baseline. This judgment caused the project design to be restructured, and the improvements dropped. This restructuring in turn fundamentally undermined the sustainability of the project’s overall objective—encouraging modal shifts through public transport. The GEF should be paying to catalyze local incentives that will lead to global environmental benefits—but, if it does not, incremental reasoning can go against sustainability.

The above cases indicate that incremental costs can and do fall at the local scales, as well as at national and international scales, and that a narrow interpretation of incremental reasoning by the GEF Secretariat and/or Council members can jeopardize sustainability and the possibilities for replication—and thus global environmental benefits.

- since this would require a different evaluative exercise such as review of government, bilateral, and multilateral funding coming into a country before a project is prepared.
5. Most biodiversity projects involve restricting access to resources, and this can have negative impacts on the livelihoods of rural communities. These issues were highlighted by GEF EO (2006b).
 6. Several interviewees also noted that there are few incentives for country recipients and proponents to get involved with incremental cost assessment as, in many cases, countries will develop only one or two GEF projects.
 7. The process of incremental reasoning is not something that can be prescriptively guided, as it relates to broader strategic aspects and the integration of other GEF operational principles required for good project design.
 8. See, for example, GEF EO (2005), pp. 108–09, exhibits 33, 34, and 35; and GEF EO (2006a), p. 18, table 4.1.
 9. On average, incremental costs were \$13.3 million per project; the GEF financed \$5.2 million of the total, with the remaining \$8.1 million financed from other sources, corresponding to a leverage of 1:1.6.

Annex A. Global Programs and Financing Methodologies

There are several other donor-funded programs that have global mandates similar to the GEF:

- The Global Fund to Fight AIDS, Tuberculosis and Malaria
- Global Integrated Pest Management Facility
- Consultative Group to Assist the Poor
- Global Water Partnership
- Consultative Group on International Agriculture Research
- Multilateral Fund for the Implementation of the Montreal Protocol

In each program, dependent on available data, the financing methodology was assessed for similarities and differences vis-à-vis incremental costs (see table A.1).

Of the global programs reviewed, only one, the Multilateral Fund for the Implementation of the Montreal Protocol, uses incremental cost methodologies in project financing decisions.

The Global Fund to Fight AIDS, Tuberculosis and Malaria requires projects to demonstrate “additionality” over and above existing financing for

activities to prevent and/or combat AIDS, tuberculosis, and malaria. Proposals have to establish “existing financing plans” (a baseline) and describe how the project will be in addition (an alternative). The cost of the project is then calculated on a component-by-component basis as the difference between the existing finance and the proposed interventions (an increment). The Global Fund does not term this “incremental cost assessment.” The Global Fund has some major differences vis-à-vis the GEF on the timing of the gap analysis, which is conducted prior to any upstream decisions on overall project/program funding. Hence, there is a strong incentive for the knowledge gained by carrying out gap analysis to influence funding decisions. In contrast, the timing of incremental cost assessment in GEF projects is applied too late in the project cycle to significantly influence overall project funding.

In conclusion, incremental cost methodologies are not used in the majority of global programs, with the exception of the Montreal Protocol. The Global Fund has the most similar financial decision-making tool, but the timing of its application is different from the GEF’s—that is, prior to any decision on overall project financing. It thus has a greater influence on and use in project design.

Table A.1

Global programs and financing methodologies/mechanisms

Program	Financing methodology/mechanism
Global Fund to Fight AIDS, Tuberculosis and Malaria	<ul style="list-style-type: none"> • Voluntary funding contributions from bilateral and multilateral donors and foundations for AIDS, tuberculosis, and malaria prevention and/or treatment projects (based on additionality principle) • Global financing must be in addition to, not in place of, existing efforts; efforts to secure additionality should be described in the projects/programs • Current planned expenditures: A gap analysis should start with a comprehensive assessment of funding from all relevant sources, whether domestic or external or from debt relief; previous grants from the Global Fund should also be included in the analysis • Estimated costs of meeting overall goals and objectives should be included to enable the calculation of gaps in financing • Calculation of gaps: The difference, or gap, between estimated costs and current and planned expenditures should be stated • Projects/programs should build on, complement, and coordinate with existing programs (not substitute for existing programs)
Global Integrated Pest Management Facility	Voluntary funding contributions from bilateral and multilateral donors for technical assistance projects (non-incremental cost basis)
Consultative Group to Assist the Poor	Voluntary funding contributions from bilateral and multilateral donors for micro-finance projects (non-incremental cost basis)
Global Water Partnership	Voluntary funding contributions from participating donor bilateral and multilateral donors, European Union, and Inter-American Development Bank for capacity building, knowledge dissemination, and water projects (non-incremental cost basis)
Consultative Group on International Agriculture Research	Voluntary funding contributions to Consultative Group on International Agriculture Research centers from members for research-based projects (non-incremental cost basis)
Multilateral Fund for the Implementation of the Montreal Protocol	Voluntary funding contributions from bilateral donors; funding for ozone phaseout projects based on incremental cost methodology (same approach as the GEF's)

Sources: www.theglobalfund.org; www.fao.org/ag/AGP/AGPP/IPM/gipmf/en/01_facility/01b.htm; www.cgap.org; www.gwpforum.org/servlet/PSP?chStartupName=_organisation; www.cgjar.org/pdf/cgjar_charter_2004_nov8.pdf; and www.multilateralfund.org/achievements/1070981582237.htm.

Annex B. Convention Activities Eligible for Incremental Financing

Montreal Protocol, Article 10: Financial Mechanism¹

- Supply of substitute chemicals
- Cost of converting existing production facilities
- Establishing new production facilities and retiring obsolete facilities
- Use of substitutes in manufacture of intermediate goods and associated plant conversions and retraining
- End uses including modification of existing equipment and provision of recycling facilities

UNFCCC, Article 4: Activities Eligible for Incremental Financing²

- Develop, update, and publish national inventories of sources and sinks mentioned in article 12
- Formulate, implement, publish, and update national programs to mitigate climate change by addressing either sources or sinks and to facilitate adaptation to climate change
- Promote and cooperate in the development, application, and diffusion of technologies, practices, and processes that control, reduce, or prevent anthropogenic emissions of greenhouse gases not covered by the Montreal Protocol
- Promote sustainable management, including conservation and enhancement of sinks and reservoirs of greenhouse gases not covered by the Montreal Protocol
- Prepare adaptive responses to climate change, including the development of integrated management plans for coastal zones, water resources, and agriculture; and protect and rehabilitate areas affected by drought, desertification, and floods
- Take climate change into account in social, economic, and environmental policies; and use appropriate methods to minimize the adverse effects of measures implemented to mitigate or adapt to climate change on national economics, public health, and the environment
- Promote scientific, technological, socioeconomic, and other research intended to further the understanding of climate change and socioeconomic consequences of various response strategies
- Promote the exchange of relevant scientific, technological, technical, socioeconomic, and legal information related to the climate system and climate change
- Promote education, training, and public awareness related to climate change and encourage

the widest participation in this process, including by NGOs

- Communicate to the UNFCCC Conference of the Parties information related to implementation

UNCBD Activities Eligible for Incremental Financing³

- Develop national strategy for conservation and sustainable use of biological diversity—*article 6(a)*
- Integrate conservation and sustainable use into relevant plans—*article 6(b)*
- Identify important components of biological diversity—*article 7(a)*
- Monitor components to identify urgent conservation needs and greatest potential for sustainable use—*article 7(b)*
- Identify significant adverse impacts—*article 7(c)*
- Establish protected areas—*article 8(a)*
- Regulate biological resources with a view to conservation and sustainable use—*article 8(c)*
- Promote protection of ecosystem and surrounding area—*article 8(d), (e)*
- Rehabilitate degraded ecosystem and support threatened species recovery—*article 8(f)*
- Regulate the release of living modified organisms—*article 8(g)*
- Endeavor to provide the conditions needed for compatibility between present uses and the conservation of biological diversity and the sustainable uses of its components—*article 8(i)*
- Maintain indigenous knowledge and lifestyles relevant for conservation and sustainable use

and promote wider applications of such knowledge—*article 8(j)*

- Provide for ex situ measures, primarily to complement in situ measures—*article 9(a)*
- Research facilities for ex situ conservation—*article 9(b)*
- Rehabilitate and reintroduce threatened species—*article 9(c)*
- Integrate conservation and sustainable use into national decision making—*article 10(a)*
- Adopt measures to minimize adverse impacts—*article 10(b)*
- Adopt economically and socially sound measures that act as incentives for conservation and sustainable use of components of biological diversity—*article 11*
- Provide for scientific and technological education and training for conservation of biological diversity—*article 12(a)*
- Promote research, particularly in developing countries—*article 12(b)*
- Promote and encourage understanding of the importance of biological diversity, including educational programs—*article 13(a)*
- Prepare environmental impact assessments—*article 14(1)(a)*

Notes

1. Montreal Protocol on Substances That Deplete the Ozone Layer. 2000. <http://hq.unep.org/ozone/Montreal-Protocol/Montreal-Protocol2000.shtml>
2. United Nations Framework Convention on Climate Change. 1992. <http://unfccc.int/resource/docs/convkp/conveng.pdf>.
3. United Nations Convention on Biological Diversity. 1992. www.biodiv.org/doc/legal/cbd-un-en.pdf.

Annex C. Notes on Methodology

The available *literature* on incremental costs, especially the GEF Council documents, was reviewed to assess the guidance for and requirements pertaining to incremental cost assessment in projects. The *compliance review* focused on determining the extent to which documents submitted for project endorsement or approval comply with GEF requirements. The *technical quality review* assessed the technical quality of the incremental cost assessment presented in the project documents. The *semi-structured interviews* and *online survey* focused on generating information on the process-related issues of incremental cost assessment.

The GEF Secretariat's Project Management Information System (PMIS) and the Project Lifecycle database were used to collect information on the characteristics of the projects considered in the compliance and technical quality reviews.¹ The PMIS and the project database maintained on the GEF Web site were used to assess the relevant documents of the sampled projects.

C.1 Literature Survey

A review of the incremental cost concept and non-GEF use of incremental cost assessment was done alongside a review of the existing evaluative and non-evaluative GEF reports in order to establish key issues, advantages, and disadvantages of incremental cost assessment. The GEF

Council documents were reviewed to determine the requirements pertaining to information on incremental costs that need to be included in the project documents at various stages in the project life cycle. A review of financial and economic decision-making tools in other global programs was also conducted.

C.2 Compliance Review

A set of parameters—including those pertaining to reporting, costs and benefits, risk, and cofinancing—that could be used to assess compliance was identified. An assessment instrument was developed based on these parameters (see instrument 1 in annex D). In some cases, the identified parameters were further refined to facilitate consistency and objectivity in the instrument's application. Certain parameters, even though important, were not included, as this would have required specialized technical expertise on individual project clusters and/or would have introduced greater subjectivity into the review process.² Such parameters were, however, addressed in the technical quality review.

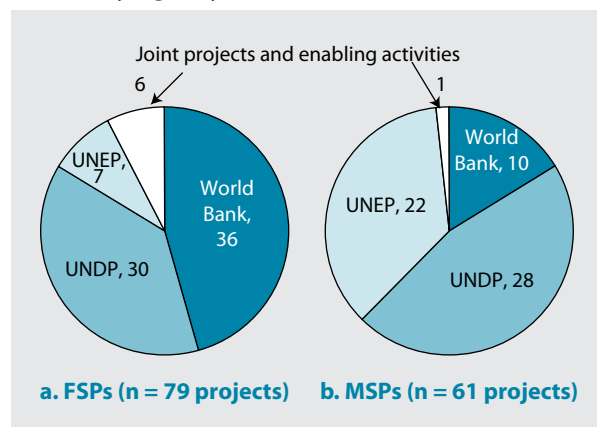
The assessment instrument was used to determine projects' level of compliance. Sections on incremental costs and cofinancing within project documents as presented to the CEO for endorsement or approval were assessed. For assessing compliance with incremental cost assessment

reporting requirements, only the incremental cost assessment section was considered. For assessing compliance with the requirements on specifying costs and benefits, risk, and financing, all sections in the project documents were considered.

In all, 140 projects that were CEO endorsed or approved in calendar year 2005 were reviewed.³ The sample was selected from GEF-3 projects that were CEO endorsed or approved in 2005 so as to provide a current source of data on compliance. These projects were prepared under the 1996 incremental cost policy and 1999 streamlined procedures and principles for agreement, and should therefore reflect their recommendations and requirements.⁴ The focus was on projects that were successful in securing CEO endorsement or approval, as their project documents are presumed to have met the incremental cost assessment requirements.

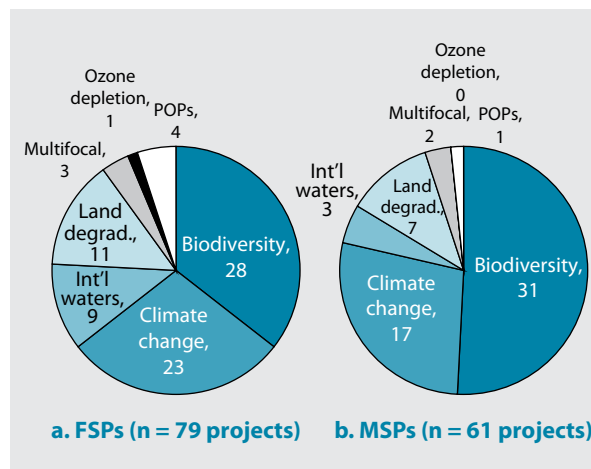
The frequency distribution of the sampled cohorts by Implementing Agency (see figure C.1) mirrors the distribution pattern for GEF-3 projects for both FSPs (projects over \$1 million) and MSPs (projects up to \$1 million).⁵

Figure C.1
Distribution of projects sampled for compliance review, by Agency



The frequency distribution of the sampled projects by focal area (see figure C.2) closely mirrors the distribution pattern for GEF-3 FSPs and broadly mirrors the GEF-3 pattern for MSPs.⁶

Figure C.2
Distribution of projects sampled for compliance review, by focal area



Chi square and “F” tests were used to determine whether there was a difference in the performance of two groups. Where a difference in the performance of two groups has been reported, it is significant at the 90 percent confidence level. Stata software was used for quantitative analysis.

C.3 Technical Quality Review

In 2005, 152 projects, which include 84 FSPs and 68 MSPs, had been CEO endorsed or approved. Of these, six projects from the persistent organic pollutants focal area and one from the ozone depletion focal area were excluded from further consideration because the number of projects in these focal areas was too few to allow for comparison with other focal areas, and it was estimated that the technical quality review would not have been cost effective.⁷ However, this exclusion has implications in terms of whether the review’s findings

could be used to determine the overall performance of the portfolio. The evaluation team was of the opinion that, since projects from the POPs and ozone depletion focal areas comprise less than 5 percent of the total portfolio, their exclusion will not fundamentally change the overall conclusions of the review. From the remaining 145 projects, a random sample of 86 projects was drawn, stratified by focal area, project size, geographic area, and IA (see tables C.1 through C.4).

A list of technical review questions appears in annex D (instrument 2). Each project document/executive summary was reviewed according to 37 criteria pertaining to key stages and aspects of incremental cost assessment as specified in the GEF incremental cost reporting format;⁸ these include descriptions of development goals/baseline formulation, global environmental objective, alternative, scope of analysis, costs, and process of agreement, among others. Additional review criteria were included to assess specific technical quality aspects, which varied for different focal areas.

For each review criterion, projects were ranked as “strong,” “adequate,” “weak,” or “absent.” For each project, descriptive notes were provided where appropriate to elaborate on or qualify these rankings. Also for each project, good practices and significant shortcomings in incremental cost assessment were identified.

Both quantitative and qualitative analyses were carried out. The quantitative analysis presents findings on the proportion of projects ranked “strong,” “adequate,” “weak,” or “absent” overall and according to each technical quality review criterion. Each project was reviewed by an evaluator with expertise in the relevant focal area. Other than in the biodiversity focal area, where four experts reviewed different sets of projects, a single expert assessed the technical quality of all the

sampled projects of that focal area. Even though the assessment criteria were well defined, there is an element of judgment involved in appraising the technical quality of the incremental cost assessment. Therefore, the manner in which experts appraised projects may have variances. Consequently, there is a possibility that the performance of each individual focal area other than biodiversity may be masking differences introduced by individual evaluators. Nevertheless, the findings of the technical quality review are consistent with the findings of the compliance review on criteria where there is overlap between the two reviews. Since the compliance review, which was done by a single evaluator, did not have an “evaluator bias” affecting the comparative performance of focal areas and IAs, the bias in the technical quality review findings would be marginal, if present at all.

C.4 Semi-Structured Interviews

Semi-structured interviews based on a common protocol were carried out with 55 people involved in GEF project design and review (see table C.5). The interview protocol (see instrument 3 in annex D) was designed to provide information on how incremental cost assessments were carried out and why certain procedures were followed (such as the use of project examples and case law or retrofitting). Such questions could not be effectively addressed from information from other data sources such as the compliance and technical quality reviews which focus more broadly on what is happening.

A purposive/snowball sampling method was employed to ensure that there was representation of key stakeholders such as the GEF Secretariat, IAs, convention secretariats, incremental cost consultants, and project proponents. Interviews were conducted between May 1 and July 31, 2006.

Table C.1**Distribution of sampled projects by focal area**

Focal area	Total number of projects CEO endorsed/approved in 2005	Population considered for sampling	Number sampled	Sample as % of population considered
Biodiversity	64	64	31	48
Climate change	42	42	26	62
International waters	12	12	12	100
Land degradation	19	19	13	68
Multifocal	8	8	4	50
Ozone depletion	1	0	0	—
POPs	6	0	0	—
Total	152	145	86	59

Table C.2**Distribution of sampled projects by geographical area**

Geographical region	Total number of projects CEO endorsed/approved in 2005	Population considered for sampling	Number sampled	Sample as % of population considered
Africa	39	37	25	68
Asia	20	19	16	84
Europe and Central Asia	39	36	20	56
Latin America and the Caribbean	32	32	20	63
Global/regional	22	21	5	24
Total	152	145	86	59

Table C.3**Distribution of sampled projects by Implementing Agency**

Implementing Agency	Total number of projects CEO endorsed/approved in 2005	Population considered for sampling	Number sampled	Sample as % of population considered
UNDP	65	63	40	63
UNEP	31	29	11	38
World Bank	48	46	31	67
Other/multiple IAs	8	7	4	57
Total	152	145	86	59

Table C.4**Distribution of sampled projects by project size**

Project size based on GEF grant	Total number of projects CEO endorsed/approved in 2005	Population considered for sampling	Number sampled	Sample as % of population considered
MSP	68	66	30	45
FSP	84	79	56	71
Total	152	145	86	59

Table C.5**Interview respondents, by geographical coverage**

Geographical area	Number of respondents
Africa	12
Asia	5
Europe and Central Asia	1
Latin America and the Caribbean	8
Global/regional	29
Total	55

The evaluation team undertook three field missions to Kenya, Malaysia, Panama, and Thailand in order to solicit responses from IA staff and project proponents who had experience with preparing projects in those countries and regions. Some groups, such as national focal points and project proponents, were underrepresented.⁹

The interviews covered the following issues:

- Awareness and use of GEF and other incremental cost guidelines
- Understanding of incremental cost terms and advantages and disadvantages of terms
- Conduct of/process involved in incremental cost assessment
- Influence on project design
- Use of incremental cost in implementation and evaluation
- Relationship to cofinance/baseline funding
- Stakeholder involvement in incremental cost assessment/negotiation
- Other comments (such as respondent background/experience)
- Respondent recommendations

Each issue was discussed in an open-ended manner, and questions often triggered discussion of following issues without further questioning being required. This approach allowed each respondent to muse and introduce examples organically rather than being consciously guided by the evaluation team. Furthermore, it allowed the team to probe issues in greater depth without being constrained by an exact sequence of questions.

The analysis of the semi-structured interviews was based on principles of systematic selection and sorting of data, coding and breaking data down to reveal meaning, and reconstruction to reveal relationships. This process was conducted using computer-assisted qualitative data analysis. This approach offers several advantages for evaluation. First, efficient and easy data management and sorting allow intensive browsing and searching of data. Second, CAQDAS saves time and maximizes *analysis* as opposed to *data management*. Third, it can improve the rigor and creativity of evaluation. Finally, because it provides precise trails of analysis that can be replicated, CAQDAS tends to improve validity and reduces the charge that evaluation of the how and why is based on a number of selective provocative quotes.

The CAQDAS software package selected was Atlas-ti.¹⁰ The first stage of data processing and analysis commenced with converting Microsoft Word interview files into text files before loading into Atlas-ti. Files were then sorted into relational sets according to respondent type—GEF Secretariat, UNDP, UNEP, World Bank, project proponent, convention secretariat, focal point.

These sets were entered into one incremental cost hermeneutic unit, consisting of 49 primary interview documents.¹¹ Each primary document was reread and marked up for quotations. The selection of quotations was not a random process but was based on the systematic questioning of each

primary document, which was developed iteratively from the analysis.¹² For example, these key questions emerged from the analysis related to relationships among semi-structured topics:

- Why are part of the guidelines ignored or not used (for example, system boundary)? Conversely, what terms are most well understood by respondents?
- What influences use of the existing guidelines?
- How is the conduct and timing of incremental cost assessment related to influence on project design and other decision making?

These are not questions that were or could be explicitly asked during the interview process but that can only be answered by breaking down responses through quotation selection (n = 954) and open coding (n = 118) to provide an overview of how key issues relate to one another. After initial coding for issues, which generated 148 codes, the code list was revised to merge or delete codes with similar meanings. For each code, Atlas-ti records the number of quotations associated with it—for example, the code “IC: Definitions” has 38 quotations associated from 36 primary interview documents. Interprimary document code comparisons were possible; for example, codes related to quotations citing limitations in the use of incremental cost guidelines were followed by references to “usefulness of case law” or project examples 22 times, indicating a strong correlation between poor quality of guidelines and the use of case law. Being able to run simple queries in order to assess code relationships greatly improves the certainty of evaluator statements beyond citation of anecdotes or quotations.

Codes were also grouped together into relational “families.” For example, all codes relating

to advantages and disadvantages of incremental costs were grouped into two families. Obviously, the more quotations that a code or family group is associated with, the more analytically significant or grounded it is as an input to evaluation findings.

The final stages of the analysis involved linking codes or code families together in networks to form and explain relations.

C.5 Online Survey

The online survey was aimed at gathering information that could be useful in understanding the experiences and views of various GEF stakeholders regarding the application of incremental cost assessment in GEF project preparation and implementation. As an initial step in developing the survey (see instrument 4 in annex D), the evaluation team reviewed all existing GEF information relating to incremental costs and data inputs from 8 to 10 semi-structured interviews.¹³ The resulting questionnaire was developed to assess the perceptions of stakeholders on various incremental cost assessment concepts and processes. The instrument was administered online through www.surveymonkey.org.

The survey target group comprised those involved in the design, review, implementation, and/or supervision of GEF projects. The targeted population was contacted primarily through an email request to fill out the survey. The survey was opened on June 13, 2006, and closed on July 31, 2006. During this period, 159 respondents participated in the survey. Of these, 119 respondents (75 percent) completed the survey, while 40 (25 percent) dropped out without completing it. Of the respondents who completed the survey, 30 percent were from IAs, 27 percent were from the Scientific and Technical Advisory Panel roster, 10 percent were independent consultants, 8 per-

cent were national focal points, and the remaining 24 percent were split among respondents from the GEF Secretariat,¹⁴ international and national NGOs, national government agencies, and bilateral and other multilateral institutions. Analysis of the responses to the questions that were completed by all the respondents shows that those who completed the survey had a better self-reported level of understanding of GEF concepts. Since the questions that ascertained the identity of the respondents were at the very end of the survey, the identities of the dropouts are not known. In this report, for any given question, all responses have been considered to provide the aggregate picture. Where intergroup comparisons have been made, the dropouts have been excluded.

The online survey has some major limitations that need to be considered. To begin with, of a large pool of people associated with GEF projects, only 159 participated in the survey. Additionally, the respondents may not be representative as they were self-selected. The survey findings should thus only be seen as supportive evidence to the findings of the other components of the GEF incremental cost evaluation.

Notes

1. The PMIS maintains information on all projects that enter the GEF Activity Cycle. The Project Lifecycle database was created for an evaluation of the project life cycle of GEF projects. While the PMIS is more comprehensive on certain aspects, the Project Lifecycle database provides more and/or more accurate information overall.
2. The excluded parameters include: has a gap analysis been incorporated, have economic implications of risks been discussed, does the baseline meet national development goals, does the incremental cost assessment show that the baseline is an attractive course of action for the host countries, and is the baseline environmentally or socially acceptable.
3. Of the total 152 projects approved during calendar year 2005, the assessment excluded 12 enabling activities (5 FSPs and 7 MSPs), as the GEF Secretariat does not expect these projects to include a section on incremental cost assessment in the project proposal.
4. This guidance is contained in GEF (1996), (1999a), and (1999b).
5. The GEF-3 distribution for FSPs has 39 percent of projects implemented by UNDP, 38 percent by the World Bank, 9 percent by UNEP, and 15 percent joint projects or enabling activities. The GEF-3 distribution of MSPs has 42 percent of projects implemented by UNDP, 29 percent by UNEP, 20 percent by the World Bank, and 9 percent joint projects or enabling activities.
6. The GEF-3 FSPs comprised 38 percent of projects in biodiversity, 28 percent in climate change, 12 percent in international waters, 8 percent in land degradation, and 15 percent in other focal areas. The MSPs had 50 percent of projects in biodiversity, 20 percent in climate change, 7 percent in international waters, 9 percent in land degradation, and 13 percent in other focal areas.
7. The enabling activities that had been excluded in the compliance review were included in the technical quality review, since the latter focused more on the overall incremental cost assessment and less on the incremental cost annex.
8. As specified in GEF (1996).
9. These include project development facility teams and government officials.
10. www.atlasti.com; this package was familiar to one member of the evaluation team.
11. This is less than the actual number of respondents, because several joint interviews were conducted in which two or more respondents participated.
12. For more information, see www.atlasti.com.
13. These interviews were conducted with World Bank and UNEP staff in Washington, D.C., and Nairobi in May 2006.
14. Only four respondents (3 percent) were from the GEF Secretariat.

Annex D. Evaluation Instruments

Instrument 1: Compliance Review

GEF Project ID:

Parameter	Response ^a	Comments
1. Do project documents ^b include a separate ICA section (ICA annex) or have the major ICA components been included in other sections? ^c	Yes, a separate section..... 3	
	Yes, in other sections..... 2	
	ICA not addressed 1	
2. Do project documents include a separate section on baseline?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
3. Do project documents include a separate section on global environmental objective?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
4. Do project documents include a separate section on alternative?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
5. Do project documents include a section on scope of the analysis or system boundary?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
6. Do project documents include a section on costs?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
7. Do project documents present incremental costs and benefits in a matrix form?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	
8. Do project documents include a section on process of agreement?	Yes, in ICA and other sections..... 4	
	Yes, in ICA 3	
	Yes, in other sections..... 2	
	No 1	

9. Does the IC matrix present incremental costs?	Yes.....	3	GO TO 12
	Yes, but not very clearly	2	
	No	1	
10. CHECK POINT: What is the expected effect of the alternative on total costs?	Total costs increase	1	GO TO 12
	Total costs remain the same.....	2	
	Total costs decrease	3	
11. If costs decrease or remain the same, then has the rationale of asking for GEF finance been explained?	Yes.....	3	
	No	1	
12. Does the IC matrix present incremental global benefits?	Yes.....	3	GO TO 15
	Yes, but not very clearly	2	
	No	1	
13. CHECK POINT: What is the expected effect of the alternative on total global benefits?	Global benefits increase	1	GO TO 15
	Global benefits remain the same.....	2	
	Global benefits decrease	3	
14. If global benefits decrease or remain the same, then has the rationale of asking for GEF funding been explained?	Yes.....	3	
	No	1	
15. Does the IC matrix present incremental local benefits?	Yes.....	3	GO TO 21
	Yes, but not very clearly	2	
	No	1	
16. CHECK POINT: What is the expected effect of the alternative on total local benefits?	Local benefits increase	1	GO TO 18
	Local benefits remain the same	2	GO TO 21
	Local benefits decrease.....	3	
17. If local benefits decrease, has it been explained that this decrease has been incorporated in the incremental cost?	Yes.....	3	
	No	1	
18. Do the project documents describe some of the local benefits accruing from the GEF-supported activities as not of national priority?	Yes.....	3	
	No	1	
19. CHECK POINT: If local benefits increase, is the increase sufficient to compensate for the additional costs that will be incurred?	Yes.....	3	GO TO 21
	Has not been discussed.....	2	
	No	1	
20. If the incremental local benefits are sufficiently large to compensate for the incremental cost incurred by the country, has the rationale for asking the GEF funding been explained?	Yes.....	3	
	No	1	
21. Has the project been defended on grounds of being the least-cost option?	Yes, in ICA and other sections.....	4	
	Yes, in ICA	3	
	Yes, in other sections	2	
	No	1	
22. Does the project specify the incremental costs in quantifiable terms?	Yes.....	3	GO TO 26
	No	1	
23. Are the costs specified in the IC matrix consistent with the outlay given in the project budget or financial modalities section?	Yes.....	3	
	More or less the same	2	
	Major differences	1	
	Unable to assess	99	
24. Is there an indication in the project documents that the costs have been estimated in present-value terms?	Yes.....	3	GO TO 26
	No	1	

25. Have the assumptions for determining present value of costs—discount rate, time horizon—been specified?	Yes..... 3 No 1	
26. Do project documents describe the risks involved in the project?	Yes..... 3 No 1	GO TO 30
27. Do project documents specify the probability of occurrence of risk?	Yes..... 3 Yes, for some risks..... 2 No 1	
28. Is there any explicit discussion in the project documents on economic implications of such risks?	Yes, an explicit discussion..... 3 Yes, but only implied 2 No 1	
29. Have risk-mitigation measures been described in the project documents?	Yes..... 3 Yes, for some risks 2 No 1	
30. CHECK POINT: Based on the description in the project documents do the project activities complement or substitute the baseline activities?	Complement..... 1 Substitute 2 Stand-alone 3 Baseline financing not relevant 4	
31. Is the baseline financing secure?	Yes, confirmed..... 3 Yes, partially confirmed..... 2 No 1 Doesn't provide information 99	GO TO 33 GO TO 33
32. Has evidence of baseline funding being secured been included in the project documents?	Yes..... 3 Yes, for some sources 2 No 1	
33. Is a part of the alternative supported by the GEF being cofinanced?	Yes..... 3 No 1	GO TO 36
34. Has the cofinancing been confirmed for all the sources?	Yes, confirmed..... 3 Yes, for some sources 2 Not confirmed for any source..... 1 Doesn't provide information 99	GO TO 36
35. Has evidence of the cofinancing being secured been attached for all the sources for which the claim has been made?	Yes..... 3 Yes, for some sources 2 No 1	
36. Which costs have been claimed to be covered by the non-GEF cofinancing (circle all that are applicable)?	Only incremental costs..... 3 Part of baseline 2 Complete baseline..... 1 Unable to assess 99	

Note: ICA = incremental cost assessment

- The numbers corresponding to each response to a question are codes. They do not denote scores.
- Project documents include project appraisal document, executive summary, annexes, letter of support for cofinancing, and other documents that were available at the point of CEO endorsement or approval.
- Major ICA components imply subsections such as baseline, alternative, and incremental cost matrix.

Instrument 2: Technical Quality Review

1. Project data	
	<ul style="list-style-type: none"> • Project name • Country • Operational program(s) • Implementing Agency(s) • Partners involved • GEF financing • Cofinancing • Total project cost
2. Project objectives and components as proposed	
	<ul style="list-style-type: none"> • Global environmental objectives • Focal area strategic priorities addressed • Development objectives • Expected outcomes • GEF-funded activities (incremental) • Cofinanced activities
3. Generic aspects of incremental cost quality	
Development goals/baseline formulations	<ul style="list-style-type: none"> • Is the country's commitment to the global environmental objectives and support for the project via national strategies, policies, and plans and/or the market context clearly described? • To what extent is the baseline related to national development plans (energy, industrial, economic, sustainable development, and so on)? • To what extent is the baseline justifiable in terms of technical feasibility? • Does the baseline adequately capture the way in which the country will address development needs in its own economic interests and or how the current market works and how it would evolve? • To what extent is the national development/market baseline described relevant to the focus of the project? • Are the threats arising from an unmodified baseline made explicit? • Are the threats arising from an unmodified baseline described in terms of their environmental effects? • Are the threats arising from an unmodified baseline described in terms of their socioeconomic/distributional effects? • Are the threats arising from an unmodified baseline described in terms of their global environmental effects?
Global environmental objective	<ul style="list-style-type: none"> • Is the global environmental objective clear and focused? • Is the global environmental objective linked to overcoming the threats arising from an unmodified baseline? • Does the global environmental objective link to the GEF mandate and focal area objectives and priorities?
Alternative	<ul style="list-style-type: none"> • Does the alternative overcome the threats implied by an unmodified baseline? • Does the alternative meet both baseline goals and the global environmental objective? • Is the proposed alternative justified in terms of global benefits? • Is a convincing case made that the alternative is the least-cost option to achieve the objective(s)? • Are project components not related to the global environmental objective adequately identified and justified? • Is there an adequate analysis of redistributive (environmental and socioeconomic) effects of the alternative? • Are negative redistributive effects to be mitigated?

Scope of analysis	<ul style="list-style-type: none"> • Are all aspects of the system boundary identified and described? • Is the specified system boundary consistent with the project focus and approach?
Costs	<ul style="list-style-type: none"> • Are both economic and financial costs adequately identified and described? • If net present value is calculated, are assumptions about discount rate, time horizon, and so on, specified, and are they properly applied? • Is the incremental cost matrix easily understandable, and does it capture the key elements? • Are the descriptions of the baseline and alternative situations in the incremental cost matrix adequate? • Are the different sources of financing for the alternative clearly specified? • Is there a rationale for cofinance? • Are associated and expected leveraged projects identified and described? • Is there clarity in the distinction among cofinance, associated finance, and expected leveraged funds? • What evidence is there that the amount of GEF financing is genuinely additional, with no crowding out or substituting of other preexisting sources taking place?
Process of agreement	<ul style="list-style-type: none"> • Is the process of reaching agreement on incremental cost with counterparts and authorities described? • Does the description suggest adequate stakeholder consultation with counterparts and/or authorities?
Overall coherence and fit	<ul style="list-style-type: none"> • Does the incremental cost assessment complement the project document? • Is the incremental cost assessment consistent with the project document? • Is the incremental cost assessment logical and easy to follow? • Does the incremental cost assessment communicate GEF and incremental cost concepts? • Does the incremental cost assessment provide a strong justification/rationale for the project in terms of global benefits?
4. Specific focal area incremental cost technical quality aspects	
Biodiversity	<ul style="list-style-type: none"> • Is the country's commitment to biodiversity conservation and support for the project via national strategies, policies, and plans clearly described? • Are threats to globally significant biodiversity adequately described? • Does the alternative clearly address threats to globally significant biodiversity? • Is there a clear understanding of the distinction between global biodiversity benefits and domestic benefits? • Does the alternative describe complementary and substitutional activities? • Are the complementary and substitutional activities justified in terms of global environmental objectives? • To what extent do the GEF-funded activities complement existing baseline activities (complementary funding)? • Do what extent is GEF funding targeted to securing global biodiversity benefits? • To what extent do the GEF-funded activities substitute for existing baseline activities (substitutional funding)?
Climate change	<ul style="list-style-type: none"> • Are climate change issues adequately described? • Does the alternative clearly focus on efforts to reduce climate change? • Is there a clear delineation of local versus global benefits? • Does the alternative describe complementary and substitutional activities? • Are the complementary and substitutional activities justified in terms of global environmental objectives? • To what extent do the GEF-funded activities complement existing baseline activities (complementary funding)? • To what extent is GEF funding targeted to securing direct global benefits? • To what extent is GEF funding targeted to securing indirect global benefits? • To what extent do the GEF-funded activities substitute for existing baseline activities (substitutional funding)?

International waters

- Have transboundary (global) issues/benefits been clearly distinguished from local ones?
- Is this project creating or supported by a solid evidence base that examines issues, causality, and legal and institutional issues at scales relevant to global benefits?
- Is the cost for creating this evidence base (where relevant) divided between baseline and incremental costs in proportion to local and global benefits?
- To what extent are the global benefits of the project independent of processes at higher scales (socially and geographically)?
- Does the baseline reflect efforts to address existing commitments to enhancing or protecting transboundary waters (or explain why this is not happening)?
- Are the costs of institutional arrangements/reforms adequately described in the baseline and alternative?
- Is support for institutional arrangements and investments through other projects or associated activities adequately described in the baseline and alternative?
- Does the project explore more than one alternative from the baseline in order to justify the one selected?
- Are the uncertainties and assumptions described in the analysis?
- Did the GEF Secretariat review critically appraise the incremental cost statement?
- Did the Scientific and Technical Advisory Panel review critically appraise the incremental cost statement?

Land degradation

- Are land degradation objectives adequately described and justified?
- Does the alternative clearly focus on efforts to reverse land degradation?
- Is there a clear delineation of local versus global benefits?
- Does the alternative describe complementary and substitutional activities?
- Are the complementary and substitutional activities justified in terms of global environmental objectives?
- To what extent do the GEF-funded activities complement existing baseline activities (complementary funding)?
- To what extent is GEF funding targeted to securing direct global benefits?
- To what extent is GEF funding targeted to securing indirect global benefits?
- To what extent do the GEF-funded activities substitute for existing baseline activities (substitutional funding)?

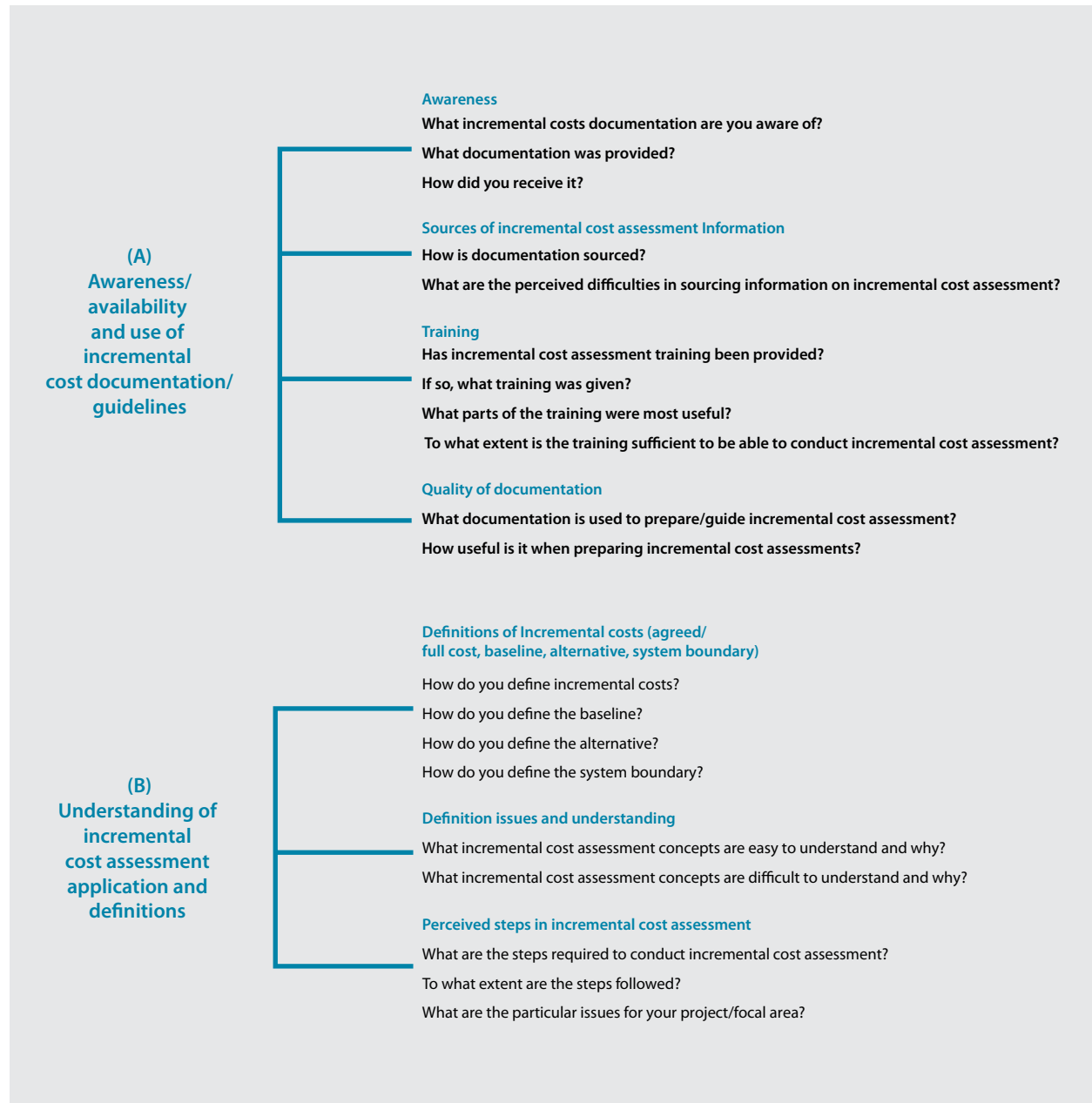
Multifocal

- Are multifocal objectives adequately described and justified?
- Does the alternative clearly focus on efforts to achieve the multifocal objectives?
- Is there a clear delineation of local versus global benefits?
- Does the alternative describe complementary and substitutional activities?
- Are the complementary and substitutional activities justified in terms of global environmental objectives?
- To what extent do the GEF-funded activities complement existing baseline activities (complementary funding)?
- To what extent is GEF funding targeted to securing direct global benefits?
- To what extent is GEF funding targeted to securing indirect global benefits?
- To what extent do the GEF-funded activities substitute for existing baseline activities (substitutional funding)?

5. Best practices and key shortcomings

- What elements of good practice are contained within the incremental cost assessment?
- What are the key shortcomings of the incremental cost assessment?

Instrument 3: Semi-Structured Interview





**(F)
Ensuring
GEF additionality**

Incremental cost assessment and cofinancing

What is the relationship between incremental cost assessment and cofinancing?
How do project financing negotiations affect incremental cost assessment?
Is incremental cost assessment considered at the same stage as negotiating GEF funding and cofinancing?

Perceptions of baseline versus incremental funding

What is considered for baseline funding?
What is considered for incremental funding?
What (if any) are the overlaps?
How are overlaps addressed in funding/ incremental cost assessment?

**(G)
Stakeholder
involvement
and negotiation**

Stakeholder involvement in incremental cost assessment

What stakeholders are involved in incremental cost assessment and why?
When is stakeholder involvement initiated?
How is the level of stakeholder involvement determined (by whom?)?
What factors influence the level of stakeholder involvement in incremental cost assessment?

Knowledge of incremental cost assessment

What stakeholders have knowledge of incremental cost assessment?
What level (depth) of knowledge is required for involvement in incremental cost assessment?

Stakeholder involvement methods

What methods are used to gain stakeholder involvement in incremental cost assessment?
What affect does stakeholder involvement have on the quality of incremental cost assessment?

Benefits and challenges

What are the benefits of stakeholder involvement in incremental cost assessment?
What are the key challenges of and to stakeholder involvement in incremental cost assessment?

Perceptions of negotiation

Who is involved in the incremental cost assessment negotiations and when?
How is incremental cost assessment negotiated?
How does negotiation influence other GEF principles? (such as country drivenness, stakeholder involvement)

Instrument 4: Online Survey

1. To what extent do you understand the following concepts.					
Concept	Completely understand - 4 -	Understand - 3 -	Poorly understand - 2 -	Don't understand - 1 -	
Incremental cost					
Global environmental benefits					
National/domestic benefits					
Baseline					
Alternative					
Additionality					
Cofinancing					
System boundary					
2. To what extent do you agree or disagree with the following statements about incremental cost approach.					
Statement	Strongly agree - 4 -	Agree - 3 -	Disagree - 2 -	Strongly disagree - 1 -	Don't know
ICA strengthens project design					
ICA assists in mobilizing cofinancing					
ICA clarifies GEF mandate					
ICA is clear and transparent					
Baseline is difficult to estimate					
ICA is arbitrary					
Incremental cost is not negotiated					
ICA helps in distinguishing between local and global benefits					
ICA weakens the country ownership of a project					
ICA is intimidating					
ICA is completed as an one-off exercise during project proposal design					
3. How useful are the following types of documents or information sources for conducting incremental cost assessment in GEF projects?					
Document/information source	Very useful - 4 -	Useful - 3 -	Marginally useful - 2 -	Not useful - 1 -	Don't know
Council documents					
GEF Secretariat guidelines					
PRINCE documents					
Implementing Agency's guidelines					
Approved GEF project examples					

4. How frequently are the following tasks included in incremental cost assessment?

Document/information source	Always - 4 -	Most times - 3 -	Few times - 2 -	Never - 1 -	I am not aware of this step
Analysis of national development goals					
Baseline formulation					
Definition of global environmental objectives					
Alternative formulation					
Specification of scope of analysis/ system boundary					
Description of the negotiation process					
Incremental cost matrix					

5. At which stage is the incremental cost assessment carried out (if applicable, tick multiple options)?

- Project concept
- Project proposal design
- Throughout project preparation
- At the end of project preparation
- After GEF Secretariat review
- After GEF Council review
- After GEF Council approval
- Don't know (please specify)

6. How long does it take to carry out an incremental cost assessment for the project proposal?

- A day or less than a day
- Several days
- Several weeks
- Several months
- Don't know
- Other (please specify)

7. Does the incremental cost assessment increase the overall time required for project preparation?

- Yes
- No
- Don't know
- Other (please specify)

8. If yes, then by how much does the incremental cost assessment increase the overall time required for project preparation?

- A day or less
- A few days to a week
- A few weeks to a month
- A few months to a year
- More than an year
- Not applicable
- Don't know

9. How much does it cost to carry out an incremental cost assessment for a full-size GEF project?

- No additional cost
- Hundreds of dollars
- Thousands of dollars
- Tens of thousands of dollars
- Varies from project to project
- Don't know

10. Which of the following statements most closely approximates the relationship between incremental cost assessment and project design?

- Incremental cost approach and project design are usually fully integrated
- Incremental cost approach is conducted once the project has already been designed so it does not influence project design
- The incremental cost approach does not have any relationship with project design
- Other (please specify)

11. In your experience with the GEF projects, how often are following GEF project stakeholders involved in negotiating the incremental cost?

Stakeholder	Always - 4 -	Most times - 3 -	Few times - 2 -	Never - 1 -	Don't know
GEF Secretariat					
GEF Implementing/Executing Agencies					
Government partners					
Cofinancers					
NGOs					
Local communities					
Please explain, what does cofinancing pay for in the GEF projects?					

12. Incremental cost assessment should primarily be seen as:

- Quantitative, numerical calculation
- Qualitative, descriptive analysis
- A form of logic or reasoning
- Don't know
- Other (please specify)

13. Have you used the concept of incrementality or additionality in any other project or with any other donor, other than those supported by the GEF? If yes, then explain.

14. Do you have anything to add, including recommendations for this evaluation?

15. Which organization do you belong to and in what role are you associated with the GEF?

16. If you have been involved in the GEF projects, which aspects have you been involved in (could be more than one)?

- Project design
- Project Implementation
- Evaluation
- Review
- Other (please specify)

17. What are your GEF areas of expertise (could be more than one)?

- Biodiversity
- Climate change
- International waters
- Land degradation
- Persistent pollutants
- Ozone-depleting substances
- Other (please specify)

18. Have you received any training on the incremental cost approach? If yes, the how useful was the training?

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