ALTERNATIVE PROVISIONS IN THE FINANCIAL PROCEDURES AGREEMENT WITH THE ASIAN DEVELOPMENT BANK ACTING AS MANAGING ENTITY FOR THE GLOBAL PARTNERSHIP FOR EDUCATION FUND

For Decision

1. STRATEGIC PURPOSE

1.1 The purpose of this paper is for the Board to consider approval of alternative provisions to the Financial Procedures Agreement to facilitate the Asian Development Bank (ADB) becoming a GPE Managing Entity (ME) for Education Plan Development Grants for two GPE-eligible Small Island Developing States in the North Pacific.

2. REQUESTED DECISION

2.1 The Board of Directors is asked to consider approval of the following decision:

BOD/2015/12-XX - Financial Procedures Agreement with the Asian Development Bank acting as Managing Entity for the Global Partnership for Education Fund: The Board of Directors, in agreement with the World Bank, as Trustee for the Global Partnership for Education Fund (GPEF), approves the content of the Financial Procedures Agreement between the Asian Development Bank, acting as Managing Entity (Grant Agent), and the World Bank as Trustee for the GPEF as set out in Annex 1 of BOD/2015/12 DOC 20, including alternative provisions to those in the model Financial Procedures Agreement.

3. BACKGROUND

3.1 With the exception of this section 3, the content of this paper is materially the same as BOD/2015/10/DOC 09 that was sent to the Board on 19 October 2015. That paper requested the above decision to be taken via the no-objection process. As one objection was received, the decision could not be approved and therefore the issue will be considered at the Board's face-to-face meeting in December 2015.

Objection - *The Donor 3 constituency objected to the proposed decision. While welcoming the interest of the Asian Development Bank to take on the role of Grant Agent, Donor 3 expressed strong reservations in relation to the removal of references to specific provisions of the Misuse of Funds Policy in the Financial Procedures Agreement considering the recent adoption of minimum standards for Grant Agents by the Board. The Constituency believe that the implications of the proposed decision should be first discussed by the Board in a face to face meeting before any decision is made.*

3.2 Without objecting, Donor 2 supported by Donor 4 provided the following comments

Comments - *We recognize that the two DCPs – The Republic of the Marshall Islands and the Federated States of Micronesia - are entitled to seek an ESPDG grant according to the existing rules and regulations.*

However we do find that approving an exception from the GPE standard FPA, at a time when GPE is in the process of streamlining its operational model, might create an unhelpful precedence.

We furthermore note that the two DCPs are associated with the United States of America under COFA treaties and would like to seek clarification as to how this status should be assessed in terms of the two DCPs ability to finance efforts to strengthen their education systems.

3.3 In relation to the objection and comments raised, the Secretariat agrees that it would be preferable if all organizations accepted the standard requirements. However the Secretariat believes that the minimum standards and requirements expected of a Grant Agent and outlined in the Financial Procedures Agreements are substantively met through the alternative language proposed. In addition, as the Board has mandated a review and revision of the Standard Financial Procedures Agreement by June 2016, the risks in this particular case and in terms of precedence are limited and need to be weighed up against the risk of not being able to conclude an agreement with the Asian Development Bank and the related implications on GPE's ability to support eligible countries in the Pacific.

3.4 In relation to the comments on the two DCPs, the Secretariat notes that it has already received a request for an Education Sector Plan Development Grant from the Federated States of Micronesia (FSM) and a request from Marshall Islands is on hold pending the outcome of this decision. The Secretariat's understanding is that the Compact Agreement is due to expire without renewal in 2023, after which FSM will have to rely on its own means, as well as a self-sustaining sovereign trust fund to be set up using part of the US transfers up to 2023 and increased tax revenue. The planned phasing

out of US transfers under the Amended Compact of Free Association has concentrated attention on the need to develop FSM's human capital and prospects for self-reliance.

4. EXECUTIVE SUMMARY

3.1 Two GPE grant-eligible Pacific Small Island Developing States (SIDS) have expressed an interest in accessing the GPE Education Sector Plan Development Grant (ESPDG), with ADB as Managing Entity: Federated States of Micronesia (FSM) and the Republic of the Marshall Islands (RMI).

3.2 Both island states are remote, with a dispersed geography composed of thousands of islands and atolls across a vast ocean zone. The offer of development partner agencies active in education is limited. Only ADB has expressed a willingness to act as ME. ADB has been playing a long-standing role in building capacity for education in both FSM and RMI.

3.3 The countries formally expressed their interest in the ESPDG in an exchange of letters with the Secretariat in October 2014 (FSM) and February 2015 (RMI). FSM's current Education Sector Plan expires this year, so there is a particular urgency in developing its new Plan. In March 2015 the Department of Education of FSM prepared an initial draft application; it is awaiting clarity on the negotiation of the FPA to finalize the application and submit it to the Secretariat. RMI's Education Sector Plan expires in 2016.

3.4 The Secretariat and the Trustee have engaged with ADB over a number of months to negotiate a Financial Procedures Agreement. In April 2015, the Secretariat reported on the status of negotiations to the Governance, Ethics, Risk, and Finance Committee (GERF) for their input, highlighting two key concerns:

1. ADB requested to engage directly with the Trustee on issues of a breach in the agreement rather than adopting the existing language that allows all donors to directly engage with ADB per third party contributor rights. **The GERF found that it would be reasonable to make some accommodation whereby if donors wanted to engage with ADB they would do so through the Secretariat in as far as possible and they should coordinate their response.**

2. ADB did not want to accept any reference to the GPE Policy and Communications Protocol on Misuse of GPE Trust Funds (the "Misuse of Funds Policy") – **The GERF found this unacceptable**

3.5 Since the GERF meeting, The Secretariat and the Trustee have continued to work with ADB to address these concerns and the Secretariat now believes there is sufficient progress for the Board to consider approval of alternative provisions in the FPA. The Secretariat believes that the fiduciary risks involved in this particular situation are extremely low given the reputation of the Asian Development Bank and the expected low value of any future allocation to the two SIDS in question.

3.6 The Trustee is willing to accept such alternative provisions provided the Board agrees to adopt them.

3.7 In the event that the Board adopts at its meeting on October 16, 2015, minimum standards for Supervising and Managing Entities, the review of these standards will take place as soon as possible thereafter but will not impede ADB's ability to perform the role of Managing Entity for these grants.

3.8 Given the total value of any relevant grants would likely not exceed US$1 million, the urgency of resolving this issue to facilitate the national planning cycles of RMI and FSM's, and the desire to maximize the Board's limited face-to-face time on critical strategic matters, the Coordinating Committee agreed for the Secretariat to submit this issue to the Board for a no-objection decision.

4. SUMMARY OF ISSUES FOR DECISION

4.1 The terms under which the Trustee administers GPEF Contributions on behalf of all Contributors are defined in, among other things, the *Standard Provisions Applicable to the Global Partnership for Education Fund* (the Standard Provisions), which is Annex 1 to and forms an integral part of all Contribution Agreements entered into between the Trustee and Contributors to the GPEF.

4.2 **Right of Recourse of Contributors.** The Standard Provisions requires, among other things, that, except as the Trustee and Board may otherwise agree, each Financial Procedures Agreement and Financial Procedures Memorandum "name the Contributors as third party beneficiaries with direct rights on the part of the Contributors to seek recourse under the Financial Procedures Agreement and provide the Trustee with the rights of novation and assignment to enable Contributors to seek direct recourse against a Supervising Entity or Managing Entity" (Standard Provisions, Section 8.4).

4.3 The foregoing has been included in the model Financial Procedures Agreement, and is set out in section 5.5 of the model Financial Procedures Agreement (see **Annex 2**).

4.4 **Misuse of Funds Policy and Cooperation with Law Enforcement Authorities.** In 2013, the Board of Directors determined that the model Financial Procedures Agreement shall

include: (a) the undertaking by the Supervising Entity and/or Managing Entity to observe the provisions of the Misuse of Funds Policy; and (b) the undertaking by the Supervising Entity and/or Managing Entity to cooperate, in accordance with its policies and procedures, with all investigations by law enforcement authorities into possible fraud (see Section 5.4 of model Financial Procedures Agreement).

Alternative Provisions Proposed by ADB and Secretariat Opinion

4.5 With respect to the undertaking to name the Contributors as third party beneficiaries with direct rights to seek recourse, the Asian Development Bank (ADB) has proposed that: (a) ADB be afforded the opportunity to take remedial action within a period of thirty (30) calendar days to address instances of misuse of funds; and (b) only after the exhaustion of this remedial procedure, the Contributors shall have the right to seek recourse against ADB with respect to any unmet or breached obligations.

4.6 Secretariat Opinion - This appears to be a common sense pragmatic approach consistent with the GERF position from April 2015 that indicated it would be unreasonable for so many individual donors to immediately seek recourse against ADB for a breach without first allowing the Secretariat to work with ADB to address the issues. The proposed alternative provisions are more reflective of actual practice.

4.7 With respect to the undertakings to observe the provisions of the Misuse of Funds Policy and to cooperate with law enforcement authorities investigating possible fraud, ADB has proposed that the application of its Integrity Principles and Guidelines satisfies the purpose of these undertakings, and has proposed that, in lieu of these undertakings:

(a) "The ADB, in accordance with its **Integrity Principles and Guidelines**, will inform the Secretariat of credible allegations of misuse of funds. Any information provided by ADB will be considered strictly confidential and will only be disseminated within the organization on a strict 'need to know' basis. The information shared may not be: (A) relied upon as a basis to initiate any administrative, civil or criminal action; or (B) attributed to ADB. However, nothing in [the Financial Procedures] Agreement will prevent the Secretariat from using the information provided to develop independently its own evidence for use in support of sanctions or other coercive or remedial action. To support the confidentiality of any possible investigation by ADB, the GPE will not issue any public statement on the allegation without obtaining the prior consent of ADB's Office of Anticorruption and Integrity (OAI)."; and

(b) "If ADB establishes, in accordance with its policies and procedure, that project funds have been misused and has decided to impose sanctions, ADB will inform the Secretariat of ADB's decision. Any communication to be made by the Board of Directors in relation to the ADB decision shall be agreed with ADB's OAI."

4.8 Secretariat Opinion - The Secretariat has reviewed ADB's Integrity Principles and Guidelines and can confirm that in substance it would meet the requirements of the Misuse of Funds Policy and that the proposed additional provisions in the Financial Procedures Agreement proposed with respect to communication on credible allegations of misuse also comply with the policy.

4.9 The Trustee is willing to accept ADB's proposed alternative provisions if the Board of Directors approves of such alternative provisions. ADB's proposal does not materially change the Trustee's obligations and responsibilities under the Contribution Agreements and/or the Financial Procedures Agreement.

5. IMPLICATIONS FOR SECRETARIAT RESOURCES

5.1 There are no implications for Secretariat resources at this time.

6. PLEASE CONTACT Padraig Power at ppower@globalpartnership.org for further information

7. ANNEXES AND FURTHER INFORMATION

7.1 This paper contains the following annexes:

Annex 1: Proposed Financial Procedures Agreement

Annex 2: Model Financial Procedures Agreement

7.2 For further information on the Asian Development Bank's Integrity Principles and Guidelines, please refer to the following link http://www.adb.org/documents/integrity-principles-and-guidelines

7.3 For further information on the GPE Policy and Communications Protocol on Misuse of GPE Trust Funds (the "Misuse of Funds Policy"), please refer to the following link: http://www.globalpartnership.org/content/policy-and-communications-protocol-misuse-gpe-trust-funds