WORLD BANK GROUP

IBRD Framework for Financial Incentives for Projects that address Global Challenges with Cross Border Externalities

ACRONYMS AND ABBREVIATIONS

BSO	Balance Sheet Optimization
CAF	Capital Adequacy Framework
CIF	Climate Investment Fund
CO2e	Carbon Dioxide Emissions
CRDC	Climate Resilient Debt Clause
CSC	Corporate Scorecard
EDs	Executive Directors
E/L	Equity-to-Loans
EMF	Exposure Management Framework
ERC	Emission Reduction Credit
FCV	Fragility, Conflict and Violence
FFI	Framework for Financial Incentives
FIF	Financial Intermediary Fund
FSF	Financial Sustainability Framework
FY	Fiscal Year
GCs	Global Challenges
GC+E	Global Challenges with cross border externalities
GDI	Graduation Discussion Income
GEF	Global Environment Facility
GHG	Greenhouse Gas
GNI	Gross National Income
GPG Fund	IBRD Fund for Innovative Global Public Goods Solutions
GSAP	Global Solutions Accelerator Platform
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
KPI	Key Performance Indicator
LMIC	Lower Middle-Income Countries
LPF	Livable Planet Fund
MDBs	Multilateral Development Banks
MDTF	Multi-Donor Trust Fund
MICs	Middle Income Countries
NDC	Nationally Determined Contributions climate actions under Paris Agreement
PGP	Portfolio Guarantee Platform
PSW	Private Sector Window
SALL	Sustainable Annual Lending Level
SALL-adj	Buffer-adjusted Sustainable Annual Lending Level
SBL	Single Borrower Limit
SCALE	Scaling Climate Action by Lowering Emissions Program
SDGs	Sustainable Development Goals
SDPHC	Shareholder & Development Partner Purchased Hybrid Capital
TF	Trust Fund
UMIC	Upper Middle-Income Countries
UTF	Umbrella Trust Fund Program
WBG	World Bank Group

Framework for Financial Incentives for Global Challenges with Cross-Border Externalities

Contents

A. Background and Context

1. **The new WB vision and mission endorsed at the 2023 Annual Meetings - to create a world free of poverty on a livable planet – provides, for the first time, a formal mandate to both fight poverty and address Global Challenges**. We must now significantly step up the way we work to help ensure that the world achieves the Sustainable Development Goals (SDGs), reaches net zero greenhouse gas emissions, and addresses all other Global Challenges that increasingly affect countries around the world. We need to evolve our ambition, strengthen our solutions, and boost our financing to do so.

2. **Shareholders and Management have agreed to focus on eight Global Challenges in the next few years.** Addressing the following challenges will be key to advancing the World Bank's new vision and mission: (1) Climate change mitigation and adaptation; (2) Enabling Digital; (3) Energy access; (4) Food, Nutrition and Security; (5) Fragility and conflict; (6) Pandemic prevention and preparedness; (7) Protecting Biodiversity and Nature; and (8) Water security and access. The selection of these eight challenges was driven by the need to better support global public goods; address the most pressing needs facing many countries at once (often because of global factors); and the World Bank's comparative advantage to provide support in these areas. These challenges are unique as they affect many countries and addressing them can have positive cross-border implications. At the same time, the costs of addressing them are high and borne by individual countries, while the benefits are often shared, putting them at risk of being under-addressed. While these are not the only challenges affecting many countries, without addressing them, sustained progress on poverty, shared prosperity, and a livable planet will not be possible. The list will be reviewed and evolve over time, as circumstances change.[1]

3. **Implementing this ambitious agenda requires greater financing capacity for IBRD to serve our clients' growing needs.** We have already made significant progress on implementing recommendations from the CAF review and balance sheet optimization (BSO). We introduced a package of measures before the 2023 Spring Meetings that are estimated to increase IBRD's financing capacity by up to $50 billion over 10 years. These included increasing IBRD's leverage ratio (by lowering IBRD's minimum equity-to-loan ratio from 20% to 19%) and increasing the limit for bilateral guarantees. At the 2023 Annual Meeting, two additional BSO measures were introduced: (1) establishing a Portfolio Guarantee Platform (PGP) which, for the first time, will allow us to leverage contingent commitments from shareholders; and (2) introducing a shareholder / development partner hybrid capital (SDPHC) instrument giving shareholders and development partners an opportunity to enter into bilateral agreements to provide perpetual subordinated loans that can be leveraged to increase IBRD's lending. Success on the additional BSO measures endorsed in Marrakesh will need to be enhanced with support from contributing partners to provide (i) voluntary BSO contributions that IBRD can leverage to increase its lending capacity, and/or (ii) grant contributions to the Livable Planet Fund (LPF) that can provide price incentives to IBRD clients as part of a financial incentives package to invest in addressing Global Challenges with cross border externalities.

4. **The proposed Framework for Financial Incentives (FFI) for projects that support Global Challenges with cross-border externalities brings together the need for additional IBRD lending capacity with creating the right incentives for clients to undertake these projects at scale.** When investing in GC projects with externalities (GC+E projects), countries undertaking these projects generate external benefits which the global community should incentivize. Financial incentives are helpful in changing the cost-benefit analysis for investments with cross border externalities, where the domestic cost-benefit

---

[1] See Development Committee report "*Ending Poverty on a Livable Planet: Report to Governor on World Bank Evolution*", September 27, 2023.

ratio of projects is different from the global cost-benefit ratio. The financial incentive package for IBRD clients would include targeted, transparent and visible volume, tenor and other price incentives that stimulate demand for clients to invest in GC+E projects.[2] The mix of volume, tenor and other price incentives would depend on the domestic cost-to-benefit impact for the country compared with the external impact, the client country's financial capacity, and the timeframe over which such benefits will accrue. The proposed LPF would be used to mobilize grant financing for the proposed price incentives, and would be complemented by concessional resources that may also be available through Trust Funds (TFs) and Financial Intermediary Funds (FIFs). The FFI will also establish a mobilization platform (the 'Global Solutions Accelerator Platform' (GSAP)) which PGP and SDPHC BSO contributors may choose to support in order to finance volume incentives. This is intended to facilitate contributors securing domestic political support for additional, voluntary contributions to IBRD because these will be used to provide financing for qualifying GC+E projects while fully aligning with the eight GCs identified by all shareholders.

5. **This paper details the key elements of the FFI and the principles that will be applied in its implementation.** The proposals reflect our experience with IDA, TFs and FIFs, feedback from shareholders through extensive engagement and deliberation, and an approach that aims to balance the need to attract funding for IBRD clients with the power of our country-based model to ensure client demand and ownership, and flexibility to adjust to evolving needs and/or respond to crises. The proposals also reflect our experience with the IBRD Fund for Innovative Global Public Goods Solutions (GPG Fund) and IDA's Private Sector Window (PSW) in terms of the value of project-by-project assessments when determining the optimal level of price incentives. This new approach to providing financial incentives will also benefit from strategic coordination among the World Bank Group (WBG) and with the universe of TF, FIFs, and other sources of concessional finance to avoid duplication, maximize burden sharing, and optimize impact. The proposed FFI is innovative, partly because, to date, systematically available grants for IBRD countries in the Multilateral Development Banks (MDBs) system have been very limited (see Annex 3 for analysis showing global grant resources to Middle Income Countries (MICs) over the past decade). Some technical elements of the proposed FFI framework will need to be further developed as implementation progresses, such as the definition and comparability of externalities across different sectors and the determination of the minimum level of price incentive required. A learning-by-doing approach underpinned by rigorous project-by-project evaluations, keeping in mind the guiding principle of simplicity and efficiency, will be required given the challenges of making these assessments and project selections across different sectors and geographic regions. The proposed approach is designed to generate learnings that will be a knowledge resource for the Bank and other MDBs on how to incentivize greater client investment in GC+E projects to tackle the great Global Challenges of our times.

6. The paper begins with a definition of the eligibility criteria including the approach for assessing and evaluating cross border externalities. It provides a summary of the types of financial incentives available and describes the proposed waterfall approach to allocating incentives aimed at achieving the least financial incentive necessary to enable the project to proceed. We describe the sources of financing for volume and price incentives, including the details of the Global Solutions Accelerator Platform (GSAP) (for volume incentives) and the Livable Planet Umbrella Trust Fund (LPF) (for price incentives). We cover how the proposed FFI will be integrated into existing processes as well as the governance around the FFI, clearly showing how the FFI will be embedded into our existing country led model and project approval processes. We also cover engagement and coordination with other Umbrella Trust Fund Programs (UTFs),

[2] The FFI will support implementation of the World Bank's six Global Challenge Programs (GCPs) by providing financial incentives for GCP projects that also have cross border externalities. While the GCPs will by no means be the only source of potentially eligible GC+E projects, we anticipate important synergies between these efforts.

FIFs, and other Multilateral Development Banks (MDBs). The final section provides the recommendation to Executive Directors.

B. Eligibility Criteria

a) Sector eligibility

7. Projects that address any of the eight Global Challenges (GCs) and that provide a positive cross-border externality will be eligible for volume and/or price incentives under the FFI. Although it is recognized that other sectors beyond the eight GCs can also produce positive cross-border externalities, the initial focus of the FFI will be limited to these eight. This could be reviewed as part of a future decision if sufficient financing could be mobilized for other purposes.

b) Cross border externalities

8. **A cross-border externality occurs when actions of one country have consequences for at least one other.** Examples of positive cross-border externalities include more efficient water use in countries that share rivers and water tables; reduction in atmospheric pollution; and stronger infectious disease control. Negative externalities arise, for example, from the spillover effects of civil war. For projects to be eligible under the FFI, they will need to provide a credible case that they are expected to produce first order/direct benefits beyond the borders of one country, either by mitigating a negative cross-border externality or producing a positive cross-border externality. In practice, projects will often have externality benefits crossing multiple GCs. For example, a transboundary water project that protects communities from flood or drought, can also address a cause of fragility, or provide climate mitigation (for example mangrove forests are a natural carbon sink as well as a form of flood protection). Table 1 illustrates examples of projects that do and do not have qualifying externalities from each of the eight Global Challenges (GCs). The examples are illustrative only and they are not intended to represent a complete list of eligible project types and omission of a particular sector or project type does not signal lack of eligibility. Through implementation of the FFI, Management will catalogue each project that receives an incentive, building out the database of eligible project types and the basis on which the externality has been evaluated. This will be an output of the learning-by-doing approach that will be shared internally and with other MDBs to amplify the value of the experience we gain.

Table 1: **Illustration of global challenge project examples that do and do not have a qualifying externality component.**

	Project examples with a qualifying externality	**Project examples without a qualifying externality**
Climate change mitigation & adaptation	Expand and protect natural mangroves for flood protection along the border of two countries simultaneously reducing GHG emissions because mangrove forests are effective carbon sinks.	Plan and implement asset-specific resilience measures and improve disaster risk management through master plans of urban and local governments to ease financial constraints on the state government when faced with unexpected shocks.
Enabling Digital	Implement policy reforms supporting international data transmission or regional data centers.	Expand access to digital financial services in rural areas.
Energy access	Develop regional transmission interconnectors that connect the demand and supply across a regional market for renewable energy projects.	Expand the domestic electricity distribution network in a high emissions intensity grid.
Food, Nutrition and Security	Transform agrifood systems through adoption of climate smart agriculture technologies and practices that reduce GHG emissions.	Improve early childhood development through meal programs for school children under the age of five.
Fragility and conflict	Support policy reforms that reduce cost of hosting refugees, thus alleviating the severity of FCV spillovers and cross-border FCV effects.	Improve living conditions and increase the economic self-reliance of targeted *internally* displaced persons.
Pandemic prevention and preparedness	Invest in disease surveillance, laboratories, institutional capacity, and policy harmonization to reduce risk of disease outbreaks becoming regional epidemics or global pandemics.	Improve access to health, nutrition, and public health services at both primary health care level and first level of referral centers or secondary care.
Protecting Biodiversity and Nature	Restore and protect natural habitats and forests to avoid GHG emissions from deforestation and/or protect endangered species.	Reduce dependence of forest-dependent communities on the natural habitat through improved delivery of public services and other efforts aimed at enhancing their economic opportunities.
Water security and access	Implement water pollution prevention measures along a river that flows through multiple countries.	Improve drinking water infrastructure in a city using the local groundwater.

9. **Management will leverage our sector expertise to ensure a consistent approach is used for assessing projects within each sector.** To the extent that methodologies in specific sectors exist (for example in assessing GHG emission reduction), Bank sector experts will apply the existing methodologies to assess the cross-border benefits. In other sectors/GCs, our experts will apply judgement in determining the existence of a qualifying externality. As noted above, our approach will be developed and refined through implementation experience and summaries of the projects reviewed, and the basis for the externality assessment will be compiled as part of the learning outcomes. The reviews of the FFI implementation will explicitly assess the consistency of evaluations of externalities within and across sectors (see Section G(c) below).

10. **Management will make volume and LPF price incentive[3] allocation decisions for batches of projects based on the project-level assessments performed by Bank sector experts.** This will provide a second level of oversight by having visibility of all projects identified across the eight Global Challenges and comparing between project evaluations. In addition, both volume and price incentive allocations will be included in the project documentation provided to the Board. Not only does this retain the Board's final approval authority for the overall project (the financial incentives will not be subject to separate approval on their own), but it also provides a feedback loop on eligibility decisions that would strengthen our approach for identifying eligible projects across different sectors and regions. Finally, as we start to systematically review and assess projects through the lens of Global Challenges with cross-border externalities, we will collect more information from the review process over time which will provide case studies to inform future eligibility decisions.

c) <u>Country eligibility</u>

11. **All IBRD countries will be eligible for volume and price incentives for GC+E projects.** While all IBRD countries will be eligible for price incentives, the scoring system will prioritize lower income and more vulnerable countries all else equal. The LPF umbrella program will be structured in a way to ensure that all IBRD countries are eligible to receive price incentives, with the volume for different income groups depending on grant funding availability. Moreover, allocation of price incentives from the LPF will take into account access to concessional resources through IDA, and TFs and FIFs and prioritize those projects without access to alternative sources of concessional resources.

C. <u>Types of Financial Incentives</u>

12. **Depending on the needs of IBRD projects or programs, financial incentives will be provided through a variety of financial products as outlined below.** These will be deployed in combination as applicable to the country, sector and/or project circumstances. Management may develop additional products (e.g., alternative financing structures that may be deployed to incentivize market offtake/distribution) that can be added as part of the financial incentive toolkit as appropriate.[4] Some of these products would be provided through IBRD, while those that include a grant element would mostly be provided via the LPF (or potentially other TFs/FIFs where such grant financing is available for IBRD countries).

---

3 Price incentive allocations from UTFs and FIF would be done by their respective governing bodies.

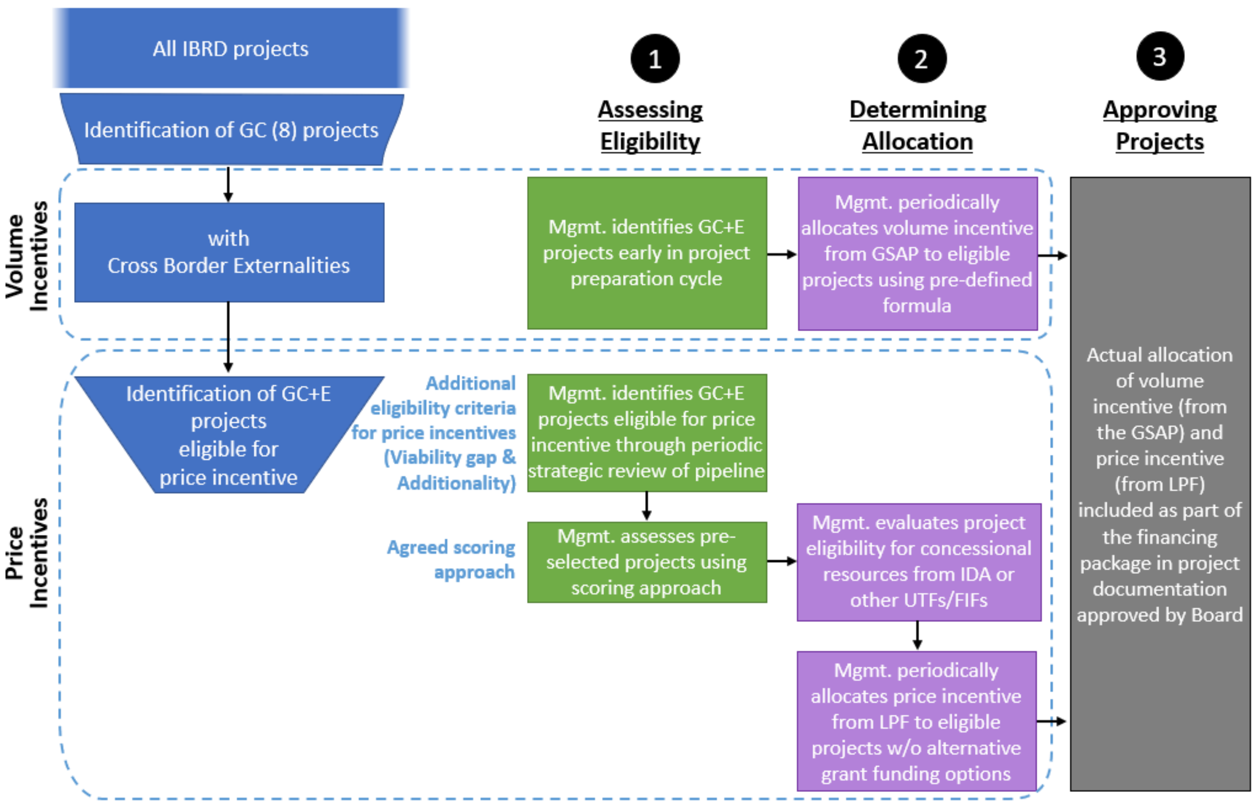
4 For example, Management will explore shareholder support for donor provided grants via the LPF to be used to cover the 5bps fees for the Climate Resilient Debt Clauses (CRDCs) to incentivize eligible countries to use this mechanism as one of the crisis response tools as part of their Climate Adaptation strategy.

- ***Additional volumes of financing****.* Many GC+E projects are undertaken at regular IBRD pricing as evidenced by the historic borrowing trends of IBRD clients (for example IBRD clients are already prioritizing projects that address climate (just one of the eight GCs) with 42% of IBRD borrowing supporting projects with climate co-benefits in FY2023). In such cases where the project is viable at regular IBRD terms, additional volumes of IBRD financing may suffice as an incentive, by enabling clients to simultaneously finance projects addressing purely domestic priorities at the same time as GC+E objectives.
- ***Loans with extended tenors***. Some GC+E projects or programs may require longer tenors because the returns on the investments are socially diffuse or take a long time to materialize. For such investments, countries could benefit from extending the average maturity of IBRD loans, for example from 20 to 25 years and final maturities from the current maximum 35 years to up to 50 years, charging the same maturity premium as regular long dated loans (50-115bps based on the country group). (See section E(b) for additional information about why this has minimal financial implications for IBRD).
- ***SBL Surcharge removal***: As a complement to provision of financial incentives, removing the SBL surcharge is an income neutral way to increase the lending headroom for SBL clients so that the financial incentives framework can be utilized to encourage them to increase investments in GC+E projects. (See section E(b) for additional information about why this has no income or risk management implications for IBRD)
- ***Project preparation grants****:* Project preparation grants or technical assistance for capacity building (up to a pre-determined maximum size per project, or as a share of program or country envelope) could also be provided by the LPF where clients ability to secure the upfront funding needed is a constraint to undertake GC+E projects.
- ***Upfront grants to blend with IBRD financing****:* this is financially equivalent to charging a lower lending rate for eligible projects (this is the modality being predominantly used by the current GPG Fund).
- ***Buy-down of interest rate upon achievement of predetermined results or KPIs*** (e.g., through sustainability-linked loans). We are piloting this results-based approach in Uruguay. Work is underway to learn from this experience and we will develop a standardized product based on what we learn.
- ***Monetize ERCs***: Incentives could also be provided through engagements that help clients generate and monetize Emission Reduction Credits (ERCs) (e.g., as part of Scaling Climate Action by Lowering Emissions (SCALE) program).

D. Allocation of Financial Incentives Based on Waterfall Approach

13. **An integrated approach will be used for allocating volume and price incentives according to a waterfall approach aimed at providing the least financial incentive required.** Chart 1 illustrates the waterfall approach starting with assessments on a project's eligibility for a volume incentive and then considering the additional eligibility criteria and scoring approach to determine a potential price incentive allocation. This section provides more details on the specific elements of the waterfall approach.

Chart 1: Allocation of financial incentives based on waterfall approach



a) <u>Allocation of volume incentives</u>

14. **Management will identify GC+E projects early in the project preparation process.** The country-driven model underpinning the CPF will continue to guide our engagement with clients. Proactive outreach and communication on the FFI will be undertaken so that both country teams and clients are made aware of the potential for volume and/or price incentives for GC+E projects. Building on their client engagement and dialogue, Management would pre-identify potential projects that could benefit from volume and/or price incentives to either materialize or to foster greater ambition on GC+E. The process would be client-driven, based on appropriate information and dialogue, to understand whether a client wishes to borrow more at regular IBRD terms, if offered, for GC+E activities, and whether the client wants to increase their project's ambition on GC+E to avail themselves of a potential price incentive. This allows for a strategic review based on the lending pipeline, dialogue with clients and Management's sector expertise.

15. **All identified GC+E projects could be eligible for a volume incentive (at regular IBRD terms) in the form of a "top up" above SALL-adj lending headroom.**[5] Building on the externality assessment carried out by World Bank sector experts, the volume incentive allocation approach will be based on a comparatively simple formula aimed at achieving equitable allocations with due consideration to the size

[5] The top-ups will be reflected in the Exposure Management Framework and will take into consideration the economic and fiscal position of the IBRD client. In addition, total exposure, including top up financing via the Global Solutions Accelerator Platform (GSAP), would need to remain below prudential limits (such as the single borrower limit).

of the project, country exposure constraints, and available resources in the Global Solutions Accelerator Platform (GSAP). The range of GC+E being addressed to encompass all eight Global Challenges will also be considered as relevant. This simple formula will be established for the review of the first batch of eligible projects and fine-tuned based on implementation experience. In addition to annual reporting of projects that receive financial incentive allocations, a review of the allocation approach will form part of the evaluation performed after the first year of implementation following the first commitment (see Section G(c) below).

b) Additional eligibility criteria for price incentives

16. **The eligibility criteria for price incentives will need to be more selective than those used for volume incentives provided at regular IBRD terms.** Grant funding to finance price incentives is expected to be significantly more constrained than non-concessional resources provided via the GSAP for volume incentives. From the 'short list' of GC+E projects, Management will identify projects that would be strong candidates for additional price incentives through a periodic review of the pipeline. This assessment will be made with reference to their knowledge of the client's constraints to move forward on the project because of insufficient economic return and where tenor or other price incentives would result in the greatest additionality.

- ***Viability Gap and Additionality***: For projects to be eligible for price incentives, they should produce significant cross-border externalities and their domestic return should be insufficient compared to alternative investments towards the same end (e.g., green technology premiums). In some fiscally constrained environments, a viability gap may also occur even if a project is economically viable but fiscally unviable because taxable benefits largely accrue in the long run. In other words, the price incentives will be used to help compensate a country for an investment that has large global benefits which may not be fully internalized by the country. Additionally, price incentives should only be provided to operations that can demonstrate the incentive induces the country to undertake a GC+E operation or to increase the ambition of the GC+E operation when it would not have done so without such price incentive. How projects can demonstrate this additionality will differ substantially depending on the project, sector, and country context.[6] While evidence of additionality is difficult to demonstrate in some cases, the aim is to select those projects that have the strongest case. While the viability gap and additionality needs to be demonstrated to be eligible for price incentives, applicants for price incentives increase their possibility of being selected if they minimize their asks to achieve a higher additional cross-border benefit per dollar of concessional resources required. As part of the learning-by-doing approach, Management will define viability gaps in more detail and develop methodological guidance for staff to assess cross-border effects.

17. **Project selection and sizing of the allocation will be determined by Management through a competitive process awarding price incentives to those operations that score best under the proposed selection criteria**. This competitive process is necessary because, in practice, it is unlikely that the World Bank will have sufficient resources to compensate all projects which meet the viability gap and

[6] For instance, in the Uruguay Debt-Buy Down supported by the GPG Fund, additionality was demonstrated by setting the targeted GHG emission reductions in excess of the sector's unconditional NDCs. In this case, the government only receives the interest buy down if it exceeds the targets that it committed to achieving using domestic resources. In other cases, projects may demonstrate additionality by showing that project targets or scope exceed what was planned for by the government.

additionality criteria. There is no exact formula to assess the price elasticity of demand for GC+E borrowing and our approach will be developed through learning-by-doing. Management will leverage prior experience with the existing GPG Fund and other Trust Funds and FIFs windows to evaluate specific projects and build experience through case studies. In order to evaluate projects in different sectors and country context, a scoring approach will be developed and used by World Bank sector experts to grade qualified projects (i.e., GC+E projects in countries eligible for price incentive that demonstrate a viability gap and GC+E additionality) with the objectives to: (i) incentivize projects producing the most additional externality benefits on a relative basis, *or* incentivize innovative GC+E operations with the greatest potential for replicability at scale, (ii) ensure that the country is committed to ambitious actions to address relevant Global Challenges, and (iii) support countries that have greater needs for incentives, including lower income and small economies. Each sector would refine bespoke evaluation methods for these criteria utilizing the common scoring approach. The following elements of the scoring approach are proposed, and Annex 1 provides an illustration of how this could be applied:

- **Scale of the cross-border externality benefit**: The operations should produce externality benefits at a significant scale (e.g., SCALE Trust Fund requires at least 1 million tons of CO2e reduction). Compared to other operations in the same thematic area, priority will be given to projects that have a high return of additional externality benefits on each dollar of grant resources provided. In situations in which it is difficult to quantify the additional externality benefit with sufficient certainty, a needs-based approach may be taken to evaluate operations. [8]

- **Innovation with replicability at scale:** Alternatively, the operation should pioneer an innovation that, if demonstrated successfully, can be replicated at scale. Operations that focus on replicability at scale should show strong evidence that overcoming well-identified and significant barriers could lead to replication that no longer requires as much concessional support, if any. They should also present a plan for how this replication at scale will be achieved (e.g., a learning agenda and dissemination plan).

- **Country ambition and action:** In allocating grant resources to GC+E projects, it is important to reward countries for their ambition and actions taken in addressing Global Challenges, including the impact of policy reforms. Allocating concessional resources to free riders would reward behavior that undermines the world's collective ability to address Global Challenges and, if done systematically, could even create moral hazard (i.e., an incentive to free ride).

- **IBRD income group:** While it is important to incentivize GC+E projects that demonstrate additionality and a viability gap in all IBRD countries, LMICs and small states would receive a higher allocation than UMICs, all else equal.

---

[8] Methodologies for estimating cross-border externalities are better established in some thematic areas than in others. For instance, for climate change mitigation operations, the metric would be the CO2e tons of additional emission reductions per dollar of grant-equivalent concessional resources. In other instances, a needs-based approach could be employed where appropriate. For instance, funding for pandemic prevention could be allocated to operations in countries that have some of the greatest risk of originating a pandemic. Similarly, price incentives for refugee operations could be allocated to those IBRD countries that face the worst spillover effects of FCV situations.

c) Allocation of price incentives

18. **Price Incentive allocation decisions would be undertaken by Management.** Management will allocate price incentives based on scoring done for each qualified project by the relevant sector experts according to a standardized scoring approach such as the approach illustrated in Annex 1. Allocations would be made following the least price incentive principle and would consider project needs for specific type of incentives as articulated by the clients though the country teams.[9] Additionally, consideration will be given to alternative sources of concessional funding through IDA (for blend countries) or other TFs/FIFs so that LPF resources will be used only where no or insufficient alternative concessional funding can be secured. Consequently, the size of the price incentive will vary according to the specific needs and circumstances of the operation. Where applicable (for example for an infrastructure project that takes a long time to generate economic returns), extended tenors would be used first. Other price incentives like project preparation grants, results-based grants, or interest buy-downs would be considered based on the nature of the project. As noted previously, there is no existing methodology or approach for comparing externalities across sectors and regions. Our approach will be developed and refined as part of implementation through a learning-by-doing approach which will benefit from a rigorous project-by-project evaluation to accumulate knowledge and experience to improve and refine the process.

19. **To help project teams with planning, eligible projects would be identified and reviewed at a sufficiently early stage in the project lifecycle**. Selected projects will receive an indicative allocation early in the planning phase. For selected beneficiary projects, volume and price incentive allocations would then be discussed and re-confirmed at decision review prior to submitting the project for Board approval as part of regular ADM arrangements for each lending instrument.

20. **The proposed approach builds on previous experience and Management's regional and sector specific expertise**. Management will build on existing practices under the GPG Fund while also heightening the importance of evidence of a viability gap and GC+E additionality in the project selection process for price incentives. The allocation approach will leverage the information that regions have about countries, our technical expertise within the sectors in comparing applications, and centralized allocation decisions. Similar to volume incentives as described above, price incentive allocations from the LPF will be included in the project documentation provided to the Board for the overall project approval (the financial incentives will not be subject to separate approval on their own).

E. Sources of Finance

21. The funding source for financial incentives under the FFI will depend on whether this relates to volume, tenor, or other price incentives. Volume incentives (at IBRD lending terms) can be financed with non-concessional resources like partner contributions through portfolio guarantees (PGP) or shareholder and development partner purchased hybrid capital (SDPHC) BSO measures directed to a mobilization platform specifically aligned with GC+E projects (the Global Solutions Accelerator Platform (GSAP)). Price incentives (except for tenor extension and SBL removal) require grant financing that can be provided via grant contributions to the Livable Planet Fund (LPF) Umbrella Program or associated trust funds, or other UTFs/FIFs. Securing sufficient grant contributions to finance price incentives would be critical to achieving the targeted objective of clients investing in GC+E projects.

`

Table 2: Summary of funding source by instrument

<table>
<tr><th>Form of contribution</th><th>Funding mechanism</th><th>Uses of resources</th></tr>
<tr><td>Shareholder/Development Partner Purchased Hybrid Capital (SDPHC)</td><td rowspan="2">Global Solutions Accelerator Platform (GSAP)</td><td rowspan="2">Volume incentives at regular IBRD lending terms</td></tr>
<tr><td>Portfolio Guarantee Platform (PGP)</td></tr>
<tr><td rowspan="2">IBRD</td><td>IBRD lending term modifications with no material impact on IBRD net income/SALL</td><td>Extending tenor, SBL surcharge removal</td></tr>
<tr><td>Transfers from IBRD surplus to GPG Fund (an Associated Trust Fund under the LPF Umbrella Program) as decided by the Governors</td><td rowspan="2">Price incentives (interest buy-downs, results-based grants, project preparation grants).</td></tr>
<tr><td>Donor grant contributions</td><td>LPF Umbrella Program (an Anchor Multi Donor Trust Fund (MDTF) that will channel donor resources for eligible IBRD projects when no or insufficient alternative concessional resources through IDA (for blend countries) or other TFs/FIFs are available..</td></tr>
</table>

a) Volume incentives financed through the Global Solutions Accelerator Platform (GSAP)

22. **IBRD shareholders are exploring options to increase IBRD's lending capacity to support the expanded mission including to address Global Challenges**. IBRD needs to increase its lending capacity beyond what has already been achieved through the CAF review and implementation of BSO measures to meet the financing needs of IBRD clients to achieve the expanded mission of reducing poverty and inequality on a livable planet.[10] Shareholders are working on further BSO measures aimed at attracting additional voluntary contributions through PGP and SDPHC. Efforts to mobilize such contributions to support IBRD lending to clients would be facilitated if the contributors could agree on the types of projects that would be financed with their contributions. This could be achieved by the World Bank Board establishing the GSAP directly aligned with the Bank's strategic objectives and providing BSO contributors the opportunity to direct their contributions plus the additional lending capacity generated by such contributions to finance volume incentives under the FFI.

23. **Funding for volume incentives could be mobilized through the Global Solutions Accelerator Platform (GSAP) suggested above whose eligibility criteria would be exactly aligned to the criteria under the FFI** (described in Section B). Contributing partners would have the opportunity to support IBRD clients

[10] IBRD sets its sustainable annual lending level (SALL-adj) based on the maximum lending it can sustain over 10 years without breaching the policy minimum E/L ratio. SALL-adj is currently $36bn per annum in real FY24 terms, which includes the impact of the BSO measures adopted at the 2023 Spring Meetings to increase lending capacity by up to $50bn over 10 years.

undertaking GC+E projects by directing up to 100%[11] of their BSO contributions plus the additional lending capacity generated over 7 years to the GSAP which would be used to finance the volume incentives under the FFI. Due to IBRD's ability to leverage BSO contributions, each $1 of portfolio guarantee or hybrid capital could add up to $5 or $6.5 respectively of lending capacity to the GSAP when committed evenly over 7 years. The target annual commitment rate would be 14.3% per annum but with the ability to front load up to 20% per annum with commensurate cuts in the following years and modifications to the overall Platform size.[13]

24. **While the Global Solutions Accelerator Platform (GSAP) may be used as a permanent tool to facilitate fund raising for IBRD to support its clients GC+E ambitions, there would be a sunset clause for how long the lending capacity generated from a BSO contribution would remain as part of the Platform**. The following sunset provisions would apply:

- Subsequent reflows from projects financed with lending capacity from the Platform will form part of IBRD's core lending capacity and included in SALL-adj.

- In case the contributor elects to redeem its SDPHC or cancel its PGP in exchange for the paid-in portion of a future capital increase, the remaining lending capacity associated with that BSO would be released from the Platform and added as part of core lending capacity to be managed in accordance with the capital increase policy package (i.e., the policy commitments agreed in the capital increase would overtake the eligibility criteria of the Platform).

- Uncommitted lending capacity from a BSO would be released from the Platform after 8 years (i.e., one year after the end of the target commitment period) and added as part of core lending capacity. This would follow regular feedback to contributors on utilization of volume incentives for GC+E projects to assess the implementation experience, contributing partner interest and feedback, and client demand. In case the additional lending capacity from the GSAP was consistently underutilized, Management would discuss with contributing partners options to increase utilization such as re-calibrating the eligibility criteria to broaden the potential projects that could be eligible as well as the feasibility of adding more grant resources via the LPF to finance additional price incentives, if that was the binding constraint.

25. **Management would report on the Platform's utilization at the individual project level and in aggregate**. Volume incentive allocations from the Platform will be included in the project documentation provided to the Board for overall project approval (the financial incentives will not be subject to separate approval on their own). In addition, as part of the annual reporting described in section G(c) below, information about the projects that receive financing from the GSAP would be reported including the proportion of the project financed (i.e., the size of the volume incentive relative to the total project) and

---

[11] For example, a BSO contributor might elect to direct 50% of its contribution to core lending capacity and 50% of its contribution to the GSAP. For the portion directed to the GSAP, all associated lending capacity generated over 7 years from that contribution would be attributed to the GSAP.

[13] The leverage potential of 5x for PGP and 6.5x for hybrid capital over 7 years assumes annual commitments would be made at 14.3% per annum. If actual annual commitments would be faster, say at 20% per annum, this would translate to a 5-year target commitment horizon which has a leverage potential of 4.5x for PGP and 6x for hybrid capital. When setting the annual lending capacity for the Platform, this would be provided as a range of 14.3% assuming 7-year total Platform size or 20% assuming 5-year total Platform size. Annex 2 illustrates the leverage potential of the Platform under different commitment speed assumptions.

information on the expected results (leveraging the new Corporate Scorecard) identifying the global challenge sectors.

b) Financial incentives that can be provided directly via IBRD

26. **Some price incentives can be provided directly through IBRD consistent with the 2018 capital increase measures agreed.** As part of the 2018 capital increase, shareholders agreed on IBRD's pricing structure, a graduated formula for making its annual net income transfers to IDA and a fund to provide financial support for GPG projects. IBRD Shareholders remain committed to demonstrating the World Bank Group solidarity to the poorest through the IBRD-IDA transfers, while paying due regard to the financial sustainability of both institutions. Therefore, price incentives requiring grant funding would need to be provided through the LPF or other UTF/FIFs (discussed in the next section) to protect IBRD's net income and the IDA transfer. However, continuing the current GPG funds transfers, extending tenor, and removing the SBL surcharge could be done directly through IBRD without materially affecting IBRD net income as follows:

- ***Net income transfer to LPF***. Through the 2018 Capital Increase Package agreement, shareholders agreed to transfer up to $45 million per year from IBRD's surplus to provide direct support to GPG projects through the current IBRD Fund for Innovative Global Public Goods Solutions (GPG Fund). Since the financing of the GPG Fund comes from surplus resources - after the IDA-transfer amount from net income has been determined - this allocation does not impact the IBRD's transfer to IDA. As described in the next section, the GPG fund would be associated with the LPF Umbrella and would continue receiving annual transfers from IBRD's surplus, subject to approval by the Governors as part of the annual decision on net income allocation.

- ***Extending Tenor***. For qualifying GC+E projects, the average maturity of IBRD loans could be increased from 20 to 25 years and final maturities increased from the current maximum 35 years to up to 50 years, without charging additional maturity premium. There would be no impact on IBRD net income as it would continue to charge the existing 50-115bps maturity premium (based on the country group) on extended tenor loans. Extended tenors will be available for a limited number of eligible GC+E projects where such long maturities make sense. As such, any potential impact on SALL/SALL-adj due to slower pace of IBRD reflows from such loans will be limited.

- ***Removing the SBL surcharge***. The SBL surcharge is proposed to be removed as an income neutral way to increase the effective lending headroom of large clients so that they can be incentivized under the FFI to undertake more GC+E projects. This can be easily implemented since there is no SBL country above the surcharge threshold. This would have no impact on IBRD net income because, in practice, SBL clients manage their lending program in a manner designed to remain below the SBL surcharge threshold ($2.5 billion below the applicable SBL) to avoid paying the additional 50bps surcharge.[14] Additionally, this change will not present any risk management impacts based on IBRD's SBL framework.

[14] Only one borrower has paid the surcharge for a short duration since the introduction of the surcharge.

c) <u>Concessional resources to finance price incentives</u>

27. **Donor-funded resources will be required to complement existing funds and provide IBRD countries with price incentives to reduce the all-in cost of IBRD financing for GC+E projects** (including project preparation grants, up front grants to blend with IBRD financing, and interest buy-downs for results. Such resources would be channeled through three main mechanisms as outlined below with fundraising coordinated through the Strategic External Fundraising Framework (SEFF) process. Direct public sector co-financing could provide additional concessional resources. Project teams could use all available options, including pooling resources from multiple sources where applicable.

- ***Livable Planet Umbrella Trust Fund (LPF)*****:** The LPF will be launched as a new umbrella program by establishing an Anchor MDTF that will serve as the primary funding source to channel donor resources for countries above or below GDI. The GPG fund will be associated with the LPF Umbrella and would continue receiving annual transfers from IBRD's surplus. Additional Associated Trust Funds may be established in cases where a donor is unable to pool its contributions in the Anchor MDTF. The LPF, together with other UTFs or FIFs, will provide grant financing for price incentives for qualifying GC+E projects undertaken by IBRD clients. A project could be eligible for a volume incentive from the Global Solutions Accelerator Platform (GSAP) and a price incentive from the LPF. The same eligibility criteria for the price incentives would apply to all accounts under the LPF, including the current GPG Fund. The LPF will be an addition to the existing concessional vehicles (e.g., TFs/FIFs) and not substitute for them. It aims to fill a documented void in financial incentives to IBRD countries.

- ***Existing UTFs and other TFs****:* In addition to the LPF, projects may be able to use other relevant UTFs for price incentives to the extent that these UTFs were designed to provide resources to IBRD countries for project financing activities. These could be used as soon as the framework is agreed, and while fundraising for the LPF is ongoing. UTF Managers and donors are encouraged to make funding available. Additionally, the flexibility and adaptability of these funds allows for rapid response to evolving country needs and priorities, ensuring that resources can be channeled efficiently where they are most needed.

- ***Relevant FIFs (e.g., CIFs, GEF, Pandemic Fund, etc.)***. IBRD teams using FIF resources for co-financing or blending to address Global Challenges would continue to adhere to the FIF criteria. Independent FIF governing bodies are responsible for setting the strategic directions of FIFs, determining country eligibility and approving funding allocations. The Bank does not play a role in FIF decision-making. Instead, Management will engage with counterparts in FIF Secretariats and key members of the governing bodies to adopt practices that make FIFs easier for MDBs to work with as sources for co-financing and blending. This includes, for example, more systematic use of programmatic approaches and reducing the transaction costs for project / program proposal development.

F. <u>Integration of the Platform into Existing Processes</u>

28. **Lending approved for projects eligible for volume incentives from the Global Solutions Accelerator Platform (GSAP) will conform to existing policies and procedures**. The following section examines how this lending will be incorporated into existing financial risk management policies, and loan agreements.

a) Financial risk management

29. **Hybrid capital and portfolio guarantee BSO instruments are integral to IBRD irrespective of whether the lending capacity they generate is used to notionally set the size of the Global Solutions Accelerator Platform (GSAP)**.

- ***Equity and Liquidity management****:* All proceeds received from issuing hybrid capital will be pooled with IBRD's existing capital (and held in IBRD's liquidity pending disbursement) and used without restriction in IBRD's operations.

- ***Capital Adequacy Framework***: Hybrid capital and portfolio guarantee BSO instruments' risk absorption coverage is unrestricted and applies to the entire balance sheet. This is essential to realize the risk-absorbing benefits of these instruments to enable the proposed leverage effect.

- ***Exposure Management Framework (EMF)*****:** The EMF is flexible and has been used effectively to support shifts in commitments toward priority areas, such as the 2018 capital increase package. Lending capacity from a Platform can be incorporated into the existing mechanism to make sure that there are sufficient exposure limits for countries that receive additional commitment allocations, subject to overall prudential limits such as SBL.

- ***Prudential Exposure Limits***: BSO contributions through hybrid capital and portfolio guarantees will increase prudential limits based on IBRD equity, like the single borrower limit, even though they will not increase prudential limits defined as a percentage of GNI. All prudential limits will continue to apply to aggregate disbursed and outstanding exposures from both core and Platform lending capacity.

- ***Financial Sustainability Framework*****:** The FSF is used to determine the Sustainable Annual Lending Level (SALL), which is the maximum annual commitment level sustainable over a 10-year planning horizon, and the adjusted SALL (SALL-adj), which incorporates a set-aside to preserve capacity to respond in a crisis. The additional annual lending capacity available from the GSAP will be reported as part of the FSF paper. SALL-adj (i.e., IBRD's core lending capacity) and total annual lending capacity from the Platform will be reported as separate limits that will be calibrated to ensure that IBRD aggregate lending remains sustainable.

b) Loan agreements

30. From the clients' perspective there would be no legal distinction between financing provided from SALL-adj or the Global Solutions Accelerator Platform (GSAP) providing volume incentives at regular IBRD terms; it would all be a loan from IBRD to the client covered under the same legal documentation and having the same pricing as any other IBRD loan to the specific country (notwithstanding potential simultaneous eligibility for a price incentive including longer tenor or concessional funding through the LPF where the price incentive could be structured through a separate document or embedded in the same loan agreement).

G. Governance

a) Implementation of the FFI

31. Once the FFI is approved by the Board, Management will implement the FFI including (i) selection of projects in accordance with eligibility criteria defined within the FFI; and (ii) allocation of financial incentives under the FFI to eligible activities that are in line with the country's development priorities and embedded in a country-based development model. There will be budget implications to implement the FFI as it introduces additional processes and reporting requirements, the need for staff and client outreach and support, and it will require the ability to track individual projects receiving financial incentives (i.e., which would require system enhancements). At the same time, the scope of the FFI depends critically on the financial resources provided by contributing partners and donors to fund the financial incentives; the implementation will be delivered in a manner that is proportionate considering the program size.

b) Process for approving individual operations

32. All World Bank projects will remain subject to the same Accountability and Decision Making (ADM) and Board approval process irrespective of whether financed from core or Platform lending capacity. While BSO contributors may direct that their contribution and portion of the lending capacity generated is added to the GSAP, they will not be involved in approval of specific projects. Volume and price incentive allocations by Management will be included in the project documentation provided to the Board as part of the regular ADM arrangements for project approval.

c) Implementation review

33. **Management would report on financial incentives allocated under the FFI including volume, tenor, and other price incentives**. The following information would be incorporated into the annual report:

- ***Additional volume***: Details of new BSO contributions directed to the Global Solutions Accelerator Platform (GSAP) in the current year as well as cumulative amounts previously directed to the Platform. Details of the additionality the GSAP allows through top-up financing to individual projects, and the aggregate amount of commitments from the Platform in the current year as well as prior utilization and the projected remaining balance.

- ***Extended tenor***: Details of the individual projects that take advantage of extended tenor for IBRD loans including average and final maturity.

- ***Price incentives***: Details of new grant contributions to the LPF umbrella and associated trust funds in the current year as well as cumulative amounts previously contributed. Details of individual projects that receive price incentives (for example in the form of project preparation grants, up front grants to blend with IBRD financing, and interest buy-downs for results), and the aggregate amount of grants provided via the LPF and associated trust funds in the current year as well as prior utilizations and the remaining balance.

34. **An initial review of the FFI implementation experience will be undertaken after the first year of implementation following the first commitment or when sufficient case studies to review exist** (which will be a function of the resources available for financial incentives) which will include reviewing the consistency of evaluations of externalities within and across sectors, the consistency and approach for volume and price allocation decisions, feedback on the implementation experience for TTLs and clients,

success at mobilizing additional BSO contributions, grant contributions to the LPF, and contributing partner feedback, and feedback from other entities that adopt the same or equivalent frameworks. This implementation review will be over and above on-going monitoring of the implementation experience by Management considering feedback from the Board during project approval as well as comparing requests for financial incentives under the FFI among batches of projects and with retrospective comparison to prior requests.

H. <u>Engagement with External Counterparts</u>

a) <u>Coordination with UTFs and FIFs</u>

35. **Grant resources are scarce and several UTFs and FIFs address priorities which overlap with the Global Challenges.** FIFs excel in mobilizing diverse funding sources and offering concessional financial instruments like grants and low-interest loans. Their targeted investment in key areas, including climate change mitigation and biodiversity conservation, supports innovative and pilot projects related to many of the eight GCs.

36. **Providing financial incentives through the FFI will benefit from strategic coordination with the universe of UTFs, FIFs, and other sources of concessional finance to avoid duplication, maximize burden sharing, and optimize impact**.

- ***UTF engagement***: Once the Framework for Financial Incentives is approved by the Board, Management will work with selected Partnership Councils to aim for agreement on the application of consistent frameworks for the use of financial incentives to the extent relevant in Umbrella Trust Funds Programs (UTFs).

- ***FIF engagement***: As the Bank plays no role in FIF decision-making and must remain a neutral, honest broker vis-à-vis other Implementing Entities in its roles as trustee and host, as applicable, the Bank will need to engage with FIF stakeholders opportunistically to strengthen complementarity between FIFs and the Global Challenges. For example, in its Implementing Entity role, the Bank can propose and attempt to build consensus for proposals that include a more programmatic approach. To make programmatic approaches more systematic, however, may require amendments to the governance and operations frameworks that would need to be agreed by FIF governing bodies. Given that FIFs have their own governance, support from WB shareholders that are also donors and clients of the relevant FIFs also would be needed to encourage their counterparts in FIF governing bodies to adopt balanced practices that make FIFs easier for MDBs to work with, while recognizing that the partnership inherent in FIF structures means FIFs also need to be responsive to other Implementing Entities and end-beneficiaries. Any efforts to encourage expanded country eligibility in FIFs would need to be part of a broader resource mobilization strategy to ensure that expanding the focus on IBRD-eligible countries would not reduce resources intended for IDA countries.

37. **In addition to high level coordination efforts on approaches, we also need to support staff in operations navigate the complex aid architecture landscape.** There are a number of existing tools and resources aimed at helping TTLs identify concessional resources (See Box 1). However, it is complex for TTLs to navigate with too many touch points and the landscape of resources very specific to each Global Challenge. In addition, each UTF/FIF has its own governance structure and allocation rules and there is a lack of predictability because allocation decisions are made by independent governing bodies mostly through calls for proposals.

38. **A "help desk" comprised of a network of existing Management focal points will support TTLs in determining their client's concessional funding needs and connect them with the appropriate sources of concessional funding**. A comprehensive communication and outreach strategy will be developed to create awareness among staff in operations and clients on the availability of tools and resources that can help identify appropriate grant funding sources. In addition, the existing tools and resources will be upgraded to better understand funding opportunities available in FIFs.

Box 1: Current tools & resources that can help TTLs identify concessional resources

<u>**Strategic External Funding Framework (SEFF)**</u>
Ensures WB senior Management's oversight of fundraising plans and TF portfolio architecture. It can help identify TFs & FIFs that will support Global Challenges and plan to provide concessional resources for projects or programs in IBRD countries.

<u>**Umbrella Funding Availability System and Tool (UFAST)**</u>
Helps TTLs to identify Umbrellas and programmatic Standalone TFs that have available funding for projects or programs that tackle Global Challenges in IBRD countries. Also provides information on how to access these funds.

<u>**Trust Fund Focal Points**</u>
Dedicated **TF Focal Points** in each GP & Region (i) support TTLs in ensuring that fundraising for TFs is strategically aligned & coordinated and provide guidance on all other TF matters, (ii) provide guidance to TTLs on existing tools & resources to identify funding opportunities for financing Global Challenges in IBRD countries.
Teams representing Bank as IEs for various FIFs support TTLs access FIF resources.

<u>**DFi Support Team**</u>
Dedicated team of TF experts in DFi that supports staff across the different GPs & Regions on all aspects of the TF lifecycle. This team works with TF teams to improve existing fund allocation mechanisms to support concessionality.

b) <u>Coordination with MDBs</u>

39. The World Bank is already collaborating with other MDBs to discuss the challenges of allocating scarce concessional resources, share specific experience from across the institutions, and create a forum for on-going dialogue. We will share our experience implementing IBRD's FFI with other MDBs to be adapted to their individual situations. The World Bank FFI is specifically focused on providing the right incentive structure for IBRD clients to undertake GC+E projects. Among the MDBs, our client bases differ, our areas of focus may differ, and our access to concessional resources may differ. Adoption of any financial incentives framework will need to consider such differences. Nonetheless, we see strong value in collaboration to learn from each other's experience and to ensure that our approaches are at least complementary if not harmonized and allow for MDBs to work as a system.

I. Other Risks and Mitigation Measures

40. While management of the financial risks related to the FFI are addressed in section F(a) above, this section considers other risks and mitigation measures associated with the FFI including:

- ***Operational risk:*** There is a risk that the FFI may add complexity which would be at odds with the objective of operational streamlining and simplification. We expect that operational issues will surface during implementation. Management will proactively monitor and manage operational risk considerations during implementation and seek to balance rigor and simplification adequately.

J. Conclusion and Recommendations

41. **There is an urgency for IBRD to secure additional financing capacity to support client country efforts to achieve the expanded mission of fighting poverty and inequality on a livable planet**. Significant progress has already been achieved through implementation of the Capital Adequacy Framework (CAF) recommendations and balance sheet optimization (BSO) which added up to $50bn of additional IBRD lending capacity over 10-years. However, adoption of the mobilization platform structure incorporated into the FFI is required to attract strong contributor interest to participate voluntarily in the additional measures that have been approved under the Portfolio Guarantee Platform (PGP) and Shareholder and Development Partner Purchased Hybrid Capital (SDPHC). Additionally, the establishment of the LPF with allocations made in line with the FFI is intended to attract donor contributions to finance the price incentives proposed.

42. **The FFI lays out the principles and approach that will be used to incentivize GC+E projects in IBRD countries including a learning by doing approach for some key elements of the proposal**. We lack clear definitions and formulae for some technical elements of the FFI such as defining, assessing and comparing externalities across different sectors and determining the minimum level of price incentive required for the use of financial incentives for MICs. Hence, a 'learning by doing approach', underpinned by rigorous project-by-project evaluations, will be required given the challenges of making these assessments and determinations across different sectors and geographic regions.

43. **The proposed approach embeds systematic opportunities to review the implementation experience, adjust and enhance the approach and share the learning outcomes across the MDB community.** Volume and price incentive allocations will both be included in the project documentation provided to the Board as part of regular ADM arrangements for project approval providing an opportunity for a feedback loop on eligibility decisions that will strengthen our approach for identifying eligible projects across different sectors and clients. Furthermore, the learning by doing approach will include summarizing details about eligible projects so that the accumulated body of examples will facilitate comparisons across sectors and regions that will in turn provide opportunities for reviewing and enhancing the approach through experience. This will also be shared among the MDB community to amplify the learning experience and create a forum for joint discussions on the topic. In additional to an annual report, there will also be a review of the FFI after the first year of implementation following the first commitment or when sufficient case studies to review exist.

44. **Management recommends that the Board approves**:

(i) The following to facilitate the implementation of the Framework for Financial Incentives:

- Remove the SBL surcharge in IBRD pricing;
- Allow tenors of up to 25 years average maturity and 50 years final maturity for qualifying GC+E projects subject to the same additional maturity premium as IBRD loans in the longest tenor bucket;
- Associate the existing GPG Fund with the LPF umbrella once the Anchor MDTF is established with IBRD surplus transfers continuing subject to approval by the Governors; and
- Establish the Global Solutions Accelerator Platform (GSAP) to which PGP and SDPHC BSO contributors can direct up to 100% of their contributions plus the additional lending capacity generated over 7 years.

(ii) The Framework for Financial Incentives, including the principles set forth in sections B through G of this paper and the respective divisions of responsibility between Management and the Board.

Annex 1: Illustrative Scoring Approach for Price Incentives

1. **Management will develop a scoring approach to facilitate comparison of projects across sectors and regions.** The design of the scoring approach will be developed over time using actual project examples to test and calibrate the components, their weights, and the approaches for scoring projects. This annex provides an illustration of how this approach could work comparing a large-scale transboundary water project in a UMIC country (IBRD group C) to an innovative forest restoration project in a LMIC country (IBRD group A). The illustrative weight of each component represents the importance of the component in the total score and the priority that we are trying to incentivize. Given the focus on the cross-border benefits and/or replicable innovative projects, these are proposed to have higher weight than the other two components. The categories and their weights presented are illustrative, and subject to change. The weighting will be calibrated before implementation of the scoring system and will be adjusted and refined as needed and based on implementation experience.

Selection Criteria	Illustrative Weight	Illustrative Categories	Example 1: Large-scale Transboundary Water project in IBRD C country	Example 2: Innovative Forest Restoration project in IBRD A country
Cross-border externality benefits	0.4	High: 3 Medium: 2 Low: 1	High = 3	Low = 1
Replicability	0.4		Low = 1	High = 3
Country Ambition & Action	0.1		Medium = 2	Medium = 2
IBRD group adjustment	0.1	Group A: 3 Group B: 2 Group C: 1 Group D: 0	Group C = 1	Group A = 3
Sum	1	Maximum total score: 3	1.9 (0.4*3 + 0.4*1 + 0.1*2 +0.1*1)	2.1 (0.4*1 + 0.4*3 + 0.1*2 +0.1*3)

2. **Weights for cross-border externality and Replicability:** Assigning similar weights to cross-border externality benefits and innovative projects with replicability is to allow the support of highly cost-effective projects at scale and highly innovative projects that have the potential for replicability at scale but are not as cost-effective yet. Addressing GC+E requires innovation. Price incentives are a tool for enabling countries to adopt innovations and pilot them. How the case for replicability is made will differ among projects. For instance, a project may make the case that the innovation the concessionality enables would be scaled across a wide variety of countries after the certain enabling conditions are in place (e.g., prices come down, the project demonstrates the success of the innovation, or the regulatory environments adapt to the innovation). The scoring of the Replicability and Externality Benefit will implicitly reflect the trade-off between the two, as sector experts will score both based on their assessment of the trade-off.

3. **Country Ambition and Action:** Country Ambition and Action will be scored on a case-by-case basis and differently for different sectors. This will depend on the type of GC+E project and may need to take in account sector specific considerations. Once the scoring formula is agreed, the specifics on how to assess each dimension will be defined in collaboration with the relevant sector experts, as needed. While Country Ambition and Action may be difficult to demonstrate in some sectors, the aim is to select those projects that have the strongest case.

4. **IBRD Group Adjustment:** Determining the technically optimal size of the IBRD group adjustment rate coefficient requires carefully weighing tradeoffs and an understanding of how scoring will work in practice. On the one hand, lower-income countries have a greater need for concessional resources. On the other hand, for pure global public goods such as GHG emission reduction, all countries, including lower-income countries, benefit from a system that awards concessional resources to the most cost-effective and additional operation. In navigating this tradeoff and determining appropriate size of the IBRD group adjustment rate, it is important to understand that even a relatively small coefficient is expected to have a significant impact on biasing the selection of the applications towards lower-income IBRD countries. This is the case for two reasons. First, the promising applications for price incentives are likely to score highly (irrespective of their country origin), near to the upper bound of the scoring system. Then, the inclusion of the IBRD income group adjustment term – even if small – will lead to projects from lower-income IBRD countries being prioritized. Put differently, even a relatively small coefficient has the consequence that lower-income countries are systematically awarded more concessionality assuming their applications have similar ratings as those of richer countries. Second, poorer IBRD countries are expected to score higher in other criteria as well because (i) a small price incentive is more likely to lead to additionality in a more resource-constraint environment and (ii) the Country Ambition and Action criterion is expected to also benefit lower-income IBRD countries. This is the case because existing methodologies for rating Country Ambition and Action structurally tend to rate relatively richer countries more strictly. While a relatively small coefficient should already shift allocation decisions significantly on the margins, the risk of a relatively large coefficient is that leads to economically suboptimal allocations – which make everybody including lower income IBRD countries (besides the recipient) worse off.

Annex 2: BSO Instrument Leverage Potential at Different Target Commitment Horizons

5. **IBRD shareholders have approved Portfolio Guarantees (PGP) and Shareholder / Development Partner Hybrid Capital (SDPHC) instruments as two new balance-sheet optimization (BSO) measures that IBRD can leverage to expand lending capacity**. A $1bn portfolio guarantee and hybrid capital instrument are expected to support $4bn and $5.3bn in additional IBRD exposure respectively. However, since IBRD loans take a number of years to fully disburse and then begin to amortize after an initial grace period, the amount of additional lending commitments that can be supported over 10 years is $6bn for portfolio guarantees and $8bn for hybrid capital.

6. **The methodology used to estimate the additional lending commitments over 10 years can be used to show the equivalent amount of lending commitments that can be supported over a 5-year and 7-year period** as illustrated below. As the target commitment horizon is shortened, the amount of reflows that begin after the typical 5-year grace period is less and thus a lower total amount of lending is supported within that time horizon while remaining consistent with the maximum additional exposure described above. The amount of lending commitments that can be supported over a given time horizon are derived based on model assumptions about the average speed of disbursement, loan repayment, prevailing interest rates, and net spread (after admin expense recovery) on lending in addition to the target annual commitment rate. Changes in these assumptions will also change the sustainable leverage amount.

Table A: Leverage Potential of BSO contributions at different target commitment horizons

c

		Total cumulative commitments generated per $1 (Leverage Factor)	
Target commitment horizon	**Annual target commitment as percentage of total**	**SDPHC** (Remaining below $5.3 exposure at any point)	**PGP** (Remaining below $4.0 exposure at any point)
10-year	10% pa	8x	6x
7-year	14.3% pa	6.5x	5x
5-year	20% pa	6x	4.5x

7. **The annual lending capacity for the Platform would be provided as a range with the lower bound based on a 7-year commitment horizon and the upper bound-based on a 5-year commitment horizon**. This would define the sustainable lending level over the target commitment period of 7 years, while allowing for front-loading up to the equivalent of a 5-year target commitment horizon if there would be very strong client demand for GC+E financing. For example, the annual lending capacity from $1bn hybrid capital plus $1bn portfolio guarantee directed to the Global Solutions Accelerator Platform (GSAP) would be provided as a range of $1.6bn - $2.1bn per annum. Table B illustrates the calculation.

Table B: Illustration of determining annual lending capacity based on target commitment horizon

BSO contribution type	Contribution amount	Leverage factor	Total added to GSAP	Target commitment horizon	Annual lending capacity
Hybrid Capital	1,000	6.5x	6,500	7 years	929
Portfolio Guarantee	1,000	5x	5,000	7 years	714
					1,643
Hybrid Capital	1,000	6x	6,000	5 years	1,200
Portfolio Guarantee	1,000	4.5x	4,500	5 years	900
					2,100

8. **The financial sustainability of the Platform will be reassessed annually as part of the Financial Sustainability Framework analysis.** The assumed leverage potential of BSO commitments directed to the Platform (i.e., the leverage factors shown in Table A which are used to set the total size of the Platform) will be reassessed annually and updated where the impact of changes in assumptions is material. Additionally, the annual lending capacity from the Platform will be updated each year to reflect actual usage to date. While the annual lending from the Platform and SALL-adj lending capacity (i.e., IBRD's core lending capacity) will reported as separate limits, they will be calibrated to ensure that IBRD's aggregate lending remains sustainable.

Annex 3: Flows of Global Grant Resources to Middle Income Countries

Methodology

1. The analysis presented in this annex reviews grant financing provided to Middle Income Countries. The analysis is based on OECD CRS data (for ODA flows) and covers 56 IBRD-only countries that are classified as middle-income countries. According to the Bank's FY24 country classification, out of 69 IBRD-only countries, 11 are high-income countries, and 58 are middle-income countries. Of the 58 IBRD-only MICs (except for Bulgaria and Russia), 56 countries are ODA eligible and are therefore tracked in the CRS database. Of these 56 IBRD-only countries, 40 are classified as UMICs in the CRS database, 15 as LMICs, and one as LDC (Angola).

Findings

2. MDBs only provided $1 billion (990 million) in grant financing to UMICs and $0.5 billion to LMICs in 2012-21 (Table C). This contrasts sharply with the grant financing of $167 billion provided by bilateral donors, EU institutions, FIFs, and the UN system to UMICs and $98 billion to LMICs in 2012-21 (in orange and blue color in Table C). Bilateral donors are the largest providers of grant financing to IBRD-only countries, followed by UN institutions and FIFs.

Table C. Global grants financing to IBRD-only countries in 2012-21 (in $ millions)

Donor Category	FlowName	Income group	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Grand Total	Share (%)
Bilateral Donors	ODA Grants	LDCs	132	124	111	87	139	107	92	88	135	129	1,146	1%
		LMICs	6,392	11,316	7,245	7,110	5,357	6,741	6,336	6,625	6,689	12,348	76,159	38%
		UMICs	9,605	9,894	10,359	10,500	13,658	13,218	14,048	13,861	15,233	12,545	122,920	61%
	ODA Grants Total		**16,130**	**21,335**	**17,715**	**17,697**	**19,155**	**20,066**	**20,476**	**20,574**	**22,057**	**25,022**	**200,225**	100%
EU Institutions	ODA Grants	LDCs	46	120	0	0	35	83	28	28	30	0	369	1%
		LMICs	1,321	1,462	1,208	1,074	1,391	1,131	1,077	1,312	1,582	778	12,336	28%
		UMICs	3,365	3,597	2,467	3,055	3,074	3,315	2,990	3,993	3,016	2,466	31,337	71%
	ODA Grants Total		**4,732**	**5,179**	**3,675**	**4,129**	**4,499**	**4,528**	**4,095**	**5,334**	**4,628**	**3,244**	**44,042**	100%
FIFs	ODA Grants	LDCs	61	33	24	12	78	37		35	27	82	390	3%
		LMICs	609	887	519	1,481	610	363	498	543	887	907	7,305	49%
		UMICs	682	994	396	370	1,056	639	360	1,217	820	708	7,241	48%
	ODA Grants Total		**1,352**	**1,914**	**939**	**1,863**	**1,745**	**1,039**	**858**	**1,795**	**1,734**	**1,697**	**14,936**	100%
MDBs	ODA Grants	LDCs			0	1				1	1	0	3	0%
		LMICs	20	46	40	64	78	56	77	62	56	42	541	35%
		UMICs	78	116	105	96	107	111	87	92	121	78	990	65%
	ODA Grants Total		**98**	**162**	**145**	**161**	**185**	**167**	**164**	**155**	**178**	**120**	**1,534**	100%
Other IFIs (e.g. Donor Funds and TFs)	ODA Grants	LDCs						12	2	7	4	5	30	3%
		LMICs	11	23	14	9	16	18	48	24	28	15	206	21%
		UMICs	56	59	78	73	53	74	89	72	102	85	740	76%
	ODA Grants Total		**67**	**82**	**91**	**81**	**70**	**105**	**138**	**103**	**134**	**105**	**976**	100%
UN System	ODA Grants	LDCs	16	16	18	21	22	15	18	21	18	20	183	2%
		LMICs	197	220	239	209	213	193	190	286	236	276	2,257	28%
		UMICs	486	419	462	536	542	667	533	662	611	631	5,550	69%
	ODA Grants Total		**698**	**655**	**720**	**766**	**777**	**875**	**741**	**969**	**864**	**927**	**7,991**	100%
Grand Total			**23,077**	**29,327**	**23,285**	**24,696**	**26,430**	**26,780**	**26,471**	**28,930**	**29,594**	**31,114**	**269,705**	

Of which:	
Commitments made by Bilateral donors, EU, FIFs, and UN system to UMICs	167,049
Commitments made by Bilateral donors, EU, FIFs, and UN system to LMICs	98,057

Note: Some FIFs (like GPE) do not report directly to OECD DAC; their financing is included under bilateral donors.