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Enabling poor rural people  
to overcome poverty

## **Establishment of the Spanish Food Security Cofinancing Facility Trust Fund**

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**For: Approval**

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## Abbreviations and acronyms

ARRI	Annual Report on Results and Impact of IFAD Operations
DSF	Debt Sustainability Framework
MIC	middle-income country
PBAS	performance-based allocation system
RIDE	Report on IFAD's Development Effectiveness
SPV	special purpose vehicle

## Executive summary

1. As part of its ongoing resource mobilization efforts to increase the total external resources available to its developing Member States, IFAD has entered into financing and cofinancing arrangements with various institutions, including the European Commission (European Union), the Global Agriculture and Food Security Programme, the Netherlands,<sup>1</sup> the OPEC Fund for International Development and the Global Environment Facility. Approximately one third of IFAD's programme of work is financed from replenishment funds and two thirds from various cofinancing and supplementary funds.
2. The Government of Spain has expressed its intention to cofinance projects and programmes for agricultural development and considers IFAD to be a reliable partner for managing Spanish cofinancing funds to be used for such purpose. Management appreciates the confidence placed in the Fund and proposes to set up a financing mechanism in order to receive these funds. The financing mechanism will be one component of a strategic partnership framework to be established between IFAD and the Government of Spain, which will complement the six-year partnership agreement signed in November 2007. Addressing the last session of the Governing Council, Mr Luis Calvo Merino, Permanent Representative of Spain to the United Nations Food and Agriculture Agencies, pointed out that Spain's Master Plan for 2009-2012 explicitly calls for the establishment of strategic agreements with multilateral institutions in different sectors. IFAD is pleased to be associated with the implementation of the Master Plan, which is grounded on principles of alignment, harmonization, predictability, management for development results and mutual accountability.
3. To receive Spanish cofinancing funds, Management proposes that the Board approve the set-up of a trust fund into which the Government of Spain would lend its cofinancing funds. IFAD will manage the trust fund and use it to effectively scale up existing IFAD-funded operations and to expand the outreach of its programme of work.
4. The trust fund will consist of a loan from the Government of Spain in the amount of EUR 285.5 million, payable in a lump sum by December 2010, and a grant of EUR 14.5 million to be committed during the Eighth Replenishment period ending in 2012. The grant portion of this new funding is provided to lower the average interest rate the Government of Spain charges to the Trust Fund and is not for IFAD to provide grants. In addition, the Government of Spain will provide an upfront fee of EUR 200,000 to cover the cost of setting up the trust fund, to be called the "Spanish Food Security Cofinancing Facility Trust Fund".
5. The loan maturity will be 45 years, including a grace period of five years. The interest rate is under negotiation. For financial modelling purposes, a fixed interest rate of 1.1 per cent, the level of the Euro interbank offered rate (Euribor) prevailing during the summer, has been utilized. IFAD will retain 20 basis points of interest rates charged to borrowing countries to cover part of the administrative costs that IFAD will incur in managing the Trust Fund and to provide cofinancing for IFAD-funded projects and programmes.
6. The cofinancing facility proposed by the Government of Spain will not change the country allocations already set under the performance-based allocation system (PBAS) but will make a substantial additional contribution to scaling up IFAD-funded projects, enabling them to have a larger and more meaningful impact.

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<sup>1</sup> In 2009, IFAD signed two cofinancing agreements with the Netherlands, which allocated a total of US\$19 million to boost the food security components of two IFAD-supported programmes in The Sudan.

7. To ensure that the projects it finances are demand- rather than supply-driven, Management assessed realistic demand above the already allocated funding under the PBAS during the Eighth Replenishment period ending in 2012. The additional indicative demand is approximately US\$640 million at July 2010, but more demand still needs quantifying.
8. The excess demand recorded by Management is consistent with the estimated incremental need for investment in the area of agricultural and food security assistance, which the international community is trying to meet by directing additional resources to existing institutions and financing new initiatives. The Spanish loan to the Trust Fund will ensure that additional funds are immediately and predictably available, which will enhance IFAD's ability to reduce rural poverty and create income opportunities for smallholders during the Eighth Replenishment period. The funding will be aligned with the policies and practices of IFAD, which will lend the Spanish cofinancing funds at the same terms and conditions as the regular resources.
9. These additional resources will provide incremental resources for countries in which the PBAS does not fully meet the demand through IFAD investments. They will complement and reinforce IFAD's programme of work, but will not affect the country allocations already established under the PBAS.
10. The basic terms and conditions of the Spanish cofinancing mechanism will be:
 

Upfront fee:	EUR 200,000 to set up the Trust Fund
Principal:	EUR 285.5 million payable to the Trust Fund in a lump sum by December 2010
Maturity:	45 years from 2010, including a five-year grace period
Interest rate:	To be determined. For financial modelling purposes, a fixed interest rate of 1.1 per cent, the level of the Euro interbank offered rate (Euribor) prevailing during the summer, has been utilized (IFAD will retain 20 basis points of interest rates charged to borrowing countries to cover administrative costs).
Repayment:	The total amount of loan repayments collected from Trust Fund borrowers according to the relevant amortization schedules annually
Allocation:	IFAD to commit funds during the Eighth Replenishment period 2011-2012
Grant:	EUR 14.5 million payable to the Trust Fund in three years (this grant money is provided to lower the average interest rate that the Government of Spain charges to the Trust Fund and is not for IFAD to provide grants).  The Government of Spain will provide additional grant money should there be, for example, unexpected events of default or arrears for risk management of the Trust Fund. Similarly, any excess balance of the grant at liquidation of the Trust Fund will be returned to the Government of Spain.
11. A reserve account within the Trust Fund will serve to ensure repayment to the Government of Spain and coverage of any negative annual balance of the Trust Fund.

## Recommendation for approval

The Executive Board is invited to approve the draft resolution on the instrument establishing the Spanish Food Security Cofinancing Facility Trust Fund contained in annex I, and to approve that the Trust Fund enter into a borrowing agreement with Spain.

## Establishment of the Spanish Food Security Cofinancing Facility Trust Fund

### I. Background

1. IFAD has an ambitious programme of work during the Eighth Replenishment period of US\$3.0 billion, which has already been allocated through the performance-based allocation system (PBAS). While the increase in the programme of work is welcomed by the beneficiary countries, the allocation is quite limited in certain countries compared with their needs. This has made IFAD less effective and in some cases, not significant enough to exert the desired impact for the achievement of the Millennium Development Goals.
2. Most of IFAD's operations are designed to benefit poor rural people in low-income countries. During the Eighth Replenishment period, in accordance with its PBAS, IFAD expects to spend 40 to 50 per cent of its resources in sub-Saharan Africa, which is the region where the least progress has been made towards the Millennium Development Goals. However, IFAD's mandate is to mobilize additional resources for agricultural development in all developing Member States, including middle-income countries (MICs)<sup>1</sup> where about one third of all people live in absolute poverty – a majority of them in rural areas. Of course, the primary responsibility for reducing levels of rural poverty in MICs – as in all countries – lies with the governments of these countries themselves, but IFAD continues to play a key role in complementing, reinforcing and helping to expand those national efforts.
3. In Latin America, most of IFAD's lending is to MICs; and with rising incomes in Asia and the Near East and North Africa, the same is likely to be true for these regions within 5 to 10 years. As requested by the Consultation on the Eighth Replenishment of IFAD's Resources, IFAD will present a new strategy for MICs at the end of 2010. This strategy will review IFAD's engagement with MICs, where there is a high demand for IFAD's experience, and will exploit the opportunities of the evolving economic situation of these countries to help them address rural poverty more effectively, even through new financial instruments that leverage national resources. Similarly, low-income countries have resource demands for investment in agriculture and rural development that cannot be adequately met by IFAD's and existing cofinanciers' resources.
4. The demand from IFAD Member States far exceeds the current available funding under the Eighth Replenishment. Within this context, the Spanish Government has offered to make cofinancing funds available and to have IFAD manage these funds through a trust fund. This decision is particularly timely. Spanish cofinancing funds will offer a great opportunity to tailor tools, strategies and approaches to make them more responsive to the very different needs and demands of countries without diverting regular resources from the agreed programme of work. In this regard, appropriate cost recovery assumptions have been embedded in the mechanism to avoid stretching available resources. Moreover, the scaling up of

<sup>1</sup> Article 2, Agreement Establishing the International Fund for Agricultural Development.

projects will entail economies of scale and scope that can benefit IFAD activities at large.

5. Managing a third-party cofinancing facility through a trust fund will also serve to test IFAD's ability to diversify access to financial resources at a time of challenging financial situations around the globe, when traditional sources of financing may be constrained by the need in many countries to keep budget deficits in check. The test – while challenging – does not imply major risks to IFAD since it will be run under the existing financial and operational framework. A prudent approach in the financial management of the additional funds will aim to safeguard the Spanish funds and IFAD's financial position, which will also benefit from the grant component of Spanish funding. Last but not least, the initiative will enlarge the partnership opportunities of IFAD with partners ready to align their contribution to the institution's strategies and practices.

## **II. Eligibility**

6. The Spanish cofinancing facility will be in the form of a loan from the Government of Spain to a trust fund to be called the "Spanish Food Security Cofinancing Facility Trust Fund" (hereafter: the Trust Fund), which IFAD will manage. The total amount of this loan, EUR 285.5 million, will be disbursed in a lump sum before the end of 2010 and will be committed over the two-year period 2011-2012. The proceeds will be applicable to developing member States of the Fund eligible for loans and will be made available under IFAD's lending terms, as follows:
  - Ordinary terms – 15 to 18 years maturity, including a three-year grace period;
  - Intermediate terms – 20 years maturity, including a five-year grace period; and
  - Highly concessional terms – a service charge of 0.75 per cent, 40 years maturity, including a ten-year grace period.
7. The additional demand as estimated by the Programme Management Department, totals US\$640 million, although this figure includes "red-light countries", that is countries with low debt sustainability that are eligible under the Debt Sustainability Framework (DSF) to receive assistance on 100 per cent grant terms (17 per cent). The allocation to countries eligible for loans on ordinary terms amounts to more than 40 per cent of the total demand; about 10 per cent for loans on intermediate terms; and 30 per cent for loans on highly concessional terms.
8. The matching of the demand calculated by IFAD, excluding DSF red-light countries, with additional cofinancing from Spain, taking into account the geographical priorities of Spanish cooperation, may result in 53 per cent of the resources being on-lent on ordinary terms, 13 per cent on intermediate terms and 34 per cent on highly concessional terms. The country allocation will be provided along with the planned project activities, which Management will regularly present to the Executive Board. The table that follows is an indicative list of potential candidates and loan amounts for this facility, both of which may vary.
9. Criteria for lending through the Trust Fund will be that a country's PBAS allocation has been fully committed and the potential borrowing government is capable of taking on extra funding. The extra funding above the PBAS will be strictly for scaling up of ongoing operations. Once the selection is made, the project in question will go through exactly the same quality enhancement and quality assurance processes as other projects and will be submitted to the Executive Board for final approval.

Table 1  
**Indicative potential lending 2011-2012 from the Spanish Trust Fund**

<i>Country</i>	<i>Selected beneficiaries 2011-2012</i>		
	<i>Additional demand (US\$ million)</i>	<i>Lending terms</i>	<i>PBAS (US\$ million)</i>
Argentina	50	O	7
Bolivia (Plurinational State of)	15	I	17
Brazil	35	O	49
Cambodia	15	HC	40.7
Cuba	15	O	--
Dominican Republic	16	O	14.5
Ecuador	15	O	22.3
Egypt	20	I	86
Ghana	20	HC	45.3
Kenya	18	HC	51.4
Lebanon	10	O	4.6
Madagascar	20	HC	47
Mauritania	10	HC	17.5
Mexico	15	O	19.4
Mozambique	15	HC	39.8
Philippines	15	I	49.9
Tunisia	20	O	20.9
Uganda	16	HC	63.9
Uruguay	15	O	--
Venezuela (Bolivarian Republic of)	15	O	9.4
Viet Nam	15	HC	68.7
<b>Total</b>	<b>385</b>		<b>674.3</b>

O = ordinary terms; I = intermediate terms; HC = highly concessional terms

### **III. Legal set-up: Special purpose vehicle – Trust Fund**

10. To fulfil the objectives and safeguard the interests of Spain and of IFAD, it is proposed that a special purpose vehicle (SPV) be established in the form of a trust fund. The Trust Fund will be a legal entity that will borrow funds from the Government of Spain and invest the proceeds in accordance with the terms of the legal instrument governing the SPV (the Trust Fund).
11. The assets and liabilities of the Trust Fund will be ring-fenced and kept separate from the accounts of IFAD and used only for the purposes of the Trust Fund. The property and assets held in IFAD's other accounts will not be used to discharge liabilities or to meet losses arising out of the administration of the Trust Fund. Equally, the resources of the Trust Fund will not be used to discharge liabilities or to meet losses arising out of the administration of the other accounts of IFAD. IFAD will report on the resources and operations of the Trust Fund in the annual report of the Executive Board to the Governing Council.

12. The cofinancing facility default risk will be mitigated through a reserve account to be set up within the Trust Fund. Moreover, accessibility to the resources of the Trust Fund will be subject to the rules, regulations and policies governing loan arrears of IFAD.
13. The establishment of such a trust fund would be consistent with the Governing Council provision encouraging the Executive Board and the President "to examine opportunities to supplement the resources of the Fund by using the Fund's power to perform financial and technical services, including the administration of resources and acting as trustee, that are consistent with the objectives and functions of the Fund."<sup>2</sup> The body of the Fund that has the authority to decide on the proposed scheme is the Executive Board by virtue of Governing Council resolution 77/2, as amended by resolution 86/XVIII, under which the Executive Board is authorized to exercise all the powers of the Governing Council, with the exception of the powers that cannot be delegated as determined by article 6, section 2(c) of the Agreement Establishing IFAD and certain other powers reserved in the said resolution. Moreover, Governing Council resolution 134/XXVII delegates the authority to decide on the establishment of a multi-donor trust fund.
14. Annex I contains the draft resolution on the instrument establishing the Trust Fund, which the Executive Board is invited to approve.
15. The governance structure of the Trust Fund should be part of the governance of IFAD, as follows:
  - Submission of projects by the President to the Executive Board;
  - Approval of projects by the Executive Board; and
  - Implementation of projects by the relevant regional division of IFAD.

#### **IV. Financial implications**

16. IFAD will manage the proceeds of the cofinancing facility in such a way as to cover the cost of project implementation and supervision and to maintain a sufficient reserve to cover any potential risk. Financial scenarios have been built on these assumptions. It has been estimated that a fixed intermediation spread of 20 basis points (0.20 per cent) of the interest rates applied by IFAD to recipient countries, together with the investment income accruing from liquidity, will cover IFAD's administrative expenses. The reserve account will allow IFAD to manage risks. Furthermore, should there be unexpected defaults or arrears that deplete the reserve account, the Government of Spain will provide additional grants as necessary to ensure that the Trust Fund's net present value is never negative.
17. The Spanish cofinancing facility will be paid in lump sum before the end of 2010 and repaid in line with reimbursements the Trust Fund will receive from borrowing countries, with the final maturity being 2055. The funds will be committed over two years starting in 2011 with the bulk of the loans to be approved in 2011 (a possible breakdown is 60 per cent in 2011 and 40 per cent in 2012). The liquidity available in the Trust Fund will be invested according to an investment policy that will ensure the security of the principal and provide the required liquidity for operational disbursement needs, while generating adequate risk-adjusted return. Principal repayments and interest payments (net of the 20 basis points retained by IFAD) will accrue in the Trust Fund until due. Over the period, the resources held in the reserve account will be invested and net earnings will also accrue to guarantee for default risks and arrears. At the end of this initiative, any unutilized balance of the grant will be returned to the Government of Spain.

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<sup>2</sup> Resolution 154/XXXII on the Eighth Replenishment of IFAD's resources, paragraph 6 (GC 32/Resolution-154-XXXII/Rev.1).



18. The currency of the cofinancing between the Government of Spain and the Trust Fund will be denominated in euros. The Trust Fund can use the proceeds of this cofinancing facility to lend in euros or any currency linked to special drawing rights.
19. Management, in conjunction with the Spanish counterparts, assessed the financial viability of the lending programme through financial models. The outcome of these exercises indicates that under the proposed terms and conditions, the Trust Fund will be able to manage risks to repay the cofinancing loan. For the purposes of the model, assumptions have been made very conservatively whereby IFAD will generate 1.5 per cent of investment income on loans undisbursed to cover administrative costs and accumulate in the reserve account, and the Government of Spain will receive interest of 1.1 per cent. The model shows that the total cash balance of the Trust Fund at the end of the period is about EUR 14 million, if no default or arrears materialize.
20. The summary of the results of the financial model is provided in annex II.

## **V. Can IFAD expand its operations while delivering quality?**

21. Both the 2009 Report on IFAD's Development Effectiveness (RIDE) and the 2009 Annual Report on Results and Impact of IFAD Operations (ARRI) show that there has been a significant improvement in development effectiveness and in the impact of IFAD operations. Principal highlights include:
  - The performance of the projects measured in terms of relevance, effectiveness and efficiency has improved significantly and is reported at 82 per cent by both the RIDE and the ARRI.
  - Sustainability – the continuation of benefits after projects close – has improved steadily over the past few years and is reported at 75 per cent by the RIDE and 73 per cent by the ARRI.
  - Promotion of pro-poor innovations is moderately satisfactory or better in 100 per cent of the projects according to the ARRI, and in 71 per cent according to the RIDE.
  - Impact on rural poverty has also markedly improved: 91 per cent of the projects evaluated were found to be moderately satisfactory or better by the ARRI, and 83 per cent by the RIDE.
22. Both reports suggest that the twin drivers of direct project supervision and enhanced field presence are beginning to yield significant results. They have allowed IFAD to support the implementation of the projects it finances more closely.
23. Management has launched a number of key initiatives under its change and reform agenda to enable the Fund to build on the achievements made under the Seventh Replenishment while ensuring that it has the required management and organization capacity to deploy its human and financial resources efficiently in support of full implementation of the Eighth Replenishment programme of work. Major progress has been made, particularly with regard to reconfiguring and streamlining management and reporting relations and launching the medium-term plan, including work on zero-based budgeting and the strategic workforce plan. In addition, a number of human resources reforms are being implemented and are expected to be completed by end-2010. Full implementation of the change and reform agenda will undoubtedly strengthen IFAD, enabling it to implement the Eighth Replenishment programme of work successfully. In this regard, it is crucial that IFAD meet not only its quantitative goals but also its qualitative objectives. Management is confident that the strategic alignment of IFAD's resources – both human and financial – with its key deliverables and strategic priorities through the

medium-term plan, along with the human resources reforms under way, will ensure success in this regard.<sup>3</sup>

## **VI. Concluding remarks**

24. This cofinancing mechanism is true to the spirit of the Governing Council directive that IFAD mobilize additional resources to supplement its programme of work during the Eighth Replenishment. It will allow IFAD to scale up existing projects and have a larger and more meaningful impact in supporting agricultural development in the rural areas of its developing countries.
25. Forming this type of partnership with the Government of Spain is an important initiative that will further strengthen the relationship between IFAD and its Member States. Management is encouraged by the confidence given by the Government of Spain in the implementation of this initiative.

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<sup>3</sup> See document EB 2010/99/R.31/Rev.1, Change and reform: Implementation. Progress report on IFAD's operations, Medium-term Plan, zero-based budget, strategic workforce plan and human resources reforms.

## **Instrument establishing the Spanish Food Security Cofinancing Facility Trust Fund<sup>1</sup>**

Whereas the G8 Summit (L'Aquila 8-10 July 2009) determined in the Joint Statement on Global Food Security that there is an urgent need for decisive action to free humankind from hunger and poverty. Food security, nutrition and sustainable agriculture must remain a priority issue on the political agenda, to be addressed through a cross-cutting and inclusive approach, involving all relevant stakeholders, at global, regional and national level;

Whereas the International Fund for Agricultural Development (the "Fund") is the United Nations specialized agency, which was established to finance agricultural development projects and programmes in the developing countries;

Whereas, the Agreement Establishing the International Fund for Agricultural Development provides that its objective shall be to mobilize additional resources to be made available for agricultural development in the developing Member States; and,

Whereas the Kingdom of Spain ("Spain"), which endorsed the Joint Statement on Global Food Security, has expressed its interest to allocate resources committed at L'Aquila for financing Projects and Programmes focused on food security and agriculture and considered IFAD as a reliable partner to implement such Projects and Programmes.

Whereas, the Executive Board of the Fund, at its 100th Session<sup>2</sup>, having regard to Governing Council Resolution 154/XXXII on the Eighth Replenishment of IFAD's Resources which provides in its Article II 6. that "*During the Replenishment Period, the Executive Board and the President are encouraged to examine opportunities to supplement the resources of the Fund by using the Fund's power to perform financial and technical services, including the administration of resources and acting as trustee, that are consistent with the objective and functions of the Fund. Operations involved in the performance of such financial services shall not be on the account of the Fund*"; approved and adopted this Instrument Establishing the Spanish Food Security Co-financing Facility Trust Fund for immediate application;

Now, therefore, be it known that:

### **Introductory Article**

To help fulfil its objective, the Fund has adopted this Instrument establishing the Spanish food Security Co-Financing Facility Trust Fund (hereinafter called the "Trust"), which shall be administered by the Fund as Trustee (hereinafter called the "Trustee"). The Trust shall be governed by and administered in accordance with the provisions of this Instrument, of the Borrowing Agreement and those established in the relevant agreements to be entered between the Trust and Spain.

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<sup>1</sup> In the event of any discrepancy between the English version of this document and the versions in the other official languages of the Fund, the English version shall prevail.

<sup>2</sup> i.e. September 2010

## **Article I. General Provisions**

### **Section 1. Purposes**

The Trust shall mobilize resources that otherwise would not be available to the Fund under Article 4 of the Agreement Establishing IFAD and provide loans on concessional terms to developing Member States that qualify for assistance under this Instrument. For this purpose, the Trustee is authorized to enter into financing arrangements and agree to their terms and conditions, with borrowers of the Trust.

### **Section 2. Accounts of the Trust**

(a) The operations and transactions of the Trust shall be conducted through a Loan Account, a Reserve Account, and an Administration Account. The resources of the Trust shall be held separately in each Account.

(b) The Trustee shall establish sub-accounts in the Loan Account to receive and disburse resources dedicated to specified regions.

### **Section 3. Unit of Account and media of payment**

(1) The Euro shall be the unit of account for commitments, loans, and all other operations and transactions of the Trust.

(2) Media of payment:

(a) Resources loaned or donated to the Trust shall be in the Euro.

(b) Payments by the Trust to Spain shall be made in the Euro

(c) Payments to borrowers of the Trust shall be in the currency or currencies agreed with such borrowers.

(3) The conversion of the currencies of loan repayments, interests and other charges into the Euro shall be at the exchange rate of the date of payment.

## **Article II. Financing by the Trust**

### **Section 1. Eligibility and Conditions for Financing**

(1) The loan shall be provided to developing member States of the Fund eligible for loans.

(2) Before approving a financing arrangement under the present Instrument, the Trustee shall be satisfied that the Member State is making an effort to strengthen substantially and in a sustainable manner its national food production.

(3) The Trustee shall not approve a request for an arrangement under this Instrument whenever the Member State has an overdue financial obligation to the Trust, the Fund or to Spain.

(4) The Trustee shall not complete a review under an arrangement under this Instrument unless and until all other conditions for the disbursement of the corresponding loan have been met or waived.

(5) The General Conditions for Agricultural Development Financing adopted by the Executive Board and as they may be amended from time to time by it, shall apply *mutatis mutandis* to financing under the present Instrument.

## **Section 2. Amount of Financing**

(a) An initial maximum limit on access to resources under the Instrument shall be established by the Trustee for each eligible Member State. These access limits shall be subject to review from time to time by the Trustee in the light of actual utilization of resources available to the Loan Account. The Trust shall keep Spain informed of the reviews and the eventual modifications of the access limits.

(b) To the extent that a Member State has notified the Trustee that it does not intend to make use of the resources available from the Trust, the Member State shall not be included in the calculations of the access limits on Trust loans.

(c) The access for each Member State that qualifies for assistance from the Trust shall be determined on the basis of an assessment by the Trustee of the food production need of the member, the strength of its programme, the amount of the member's outstanding use of credit extended by the Fund, and its record in using Fund credit in the past.

(d) Any commitment shall be subject to the availability of resources to the Trust.

## **Section 3. Disbursements**

(a) Any disbursement shall be subject to the availability of the resources to the Trust.

(b) Except in what is expressly provided for in this Instrument and other relevant agreements concerning the Trust, the Fund's rules, policies and procedures shall apply *mutatis mutandis* to any disbursement under the present Instrument.

(c) No disbursement under any commitment to a Member State shall be made after the full repayment of the amount borrowed from Spain.

## **Section 4. Terms of loans**

(a) Trust loans shall be approved by the Trustee in accordance with the provisions of the Lending Policies and Criteria adopted by the Fund's Governing Council and with the modalities set forth in the Trust Loans concluded between the Trust and the borrowing Member State.

(b) Trust loans shall be disbursed in a freely usable currency as decided by the Trustee. They shall be repaid, and interest paid in a freely usable currency as decided by the Trustee. The Trustee shall administer the Trust in accordance with the highest standards of efficiency and economy;

(c) The Trustee shall deduct a fixed rate of 20 basis points (0.20%) from the interest rate of the Trust loans to cover the administrative costs for managing the Trust.

(d) The Trustee may not reschedule the repayment of loans from the Trust.

(e) The Trustee shall ensure at all times that the corresponding foreign exchange operations are arranged to minimise the currency risk of the Trust.

(f) The Trust shall lend resources from the Loan Account on such terms that would permit the reimbursement of the loans obtained for the Trust.

## **Section 5. Modifications**

Any modification of these provisions will affect only loans made after the effective date of the modification, provided that modification of the interest rate shall apply to interest accruing after the effective date of the modification.

## **Section 6. Information**

Following the Fund's internal procedures, Spain shall be kept informed of the Trust loans operations that are being reviewed by the Trust and on the Trust loans that are finally committed.

# **Article III. Loan Account**

## **Section 1. Resources**

The resources held in the Loan Account shall consist of:

- (a) the proceeds of loans made to the Trust for that Account
- (b) the proceeds of donations made to the Trust for that Account; and
- (c) the resources needed to cover the administrative cost of the establishment of the Trust.

## **Section 2. Borrowing authority**

- (a) The Trust may obtain resources for the Loan Account from Spain on such terms and conditions as may be agreed between the Trustee and Spain subject to the provisions of this Instrument. For this purpose the Trust is authorized to enter into the Borrowing Agreement and agree to their terms and conditions with Spain.
- (b) The Trust may not obtain resources for the Loan Account on such terms that would not permit concessional financing.

## **Section 3. Use of resources**

The resources held in the Loan Account shall be used by the Trust to provide loans to borrowing Member States and to make payments to the Reserve and to the Administration Account.

## **Article IV. Reserve Account**

### **Section 1. Resources**

(1) The resources held in the Reserve Account shall consist of:

- (a) transfers by the Fund from its resources in accordance with decisions of the Governing Council of IFAD;
- (b) net earnings from investment of resources held in the Reserve Account;
- (c) net earnings from investment of any resources held in the Loan Account pending the use of these resources in operations;
- (d) payments of interest under Trust loans minus a fixed rate of 20 basis points (0.20%) per annum or semi-annually, as specified in Article II, Section 4 (c);
- (e) payments of overdue principal or interest or interest thereon under Trust loans;
- (f) payments of the principal under Trust loans; and
- (g) donations made to the Trust for that Account.

(2) The Trustee shall hold balance in the Reserve Account of at least the 3% of the outstanding Trust Loans.

### **Section 2. Use of resources**

The resources held in the Reserve Account shall be used by the Trustee to make payments to Spain of principal and interest on its borrowing.

### **Section 3. Review of resources**

If resources in the Reserve Account are, or are determined by the Trustee likely to become, insufficient to meet the obligations of the Trust that may be discharged from the Reserve Account as they become due and payable, the Trustee shall review the situation in a timely manner. The Trustee shall consult with Spain for that purpose.

### **Section 4. Terminology**

The term "interest" is deemed to include any fee charged on Trust loans.

## **Article V. Administration of the Trust**

### **Section 1. Trustee**

(a) The Trust shall be administered by the Fund as Trustee. Decisions and other actions taken by the Fund as Trustee shall be identified as taken in that capacity.

(b) Subject to the provisions of this Instrument, the Fund in administering the Trust shall apply the same rules as, in accordance with the Agreement Establishing IFAD, apply to the operation of the resources of the Fund.

(c) The Trustee, acting through its President, is authorized:

(i) to make all arrangements, including establishment of accounts in the name of the Fund as Trustee, with such depositories of the Fund as the Trustee deems necessary; and

(ii) to take all other administrative measures that the Trustee deems necessary to implement the provisions of this Instrument.

## **Section 2. Administration Account**

(a) The resources referred to in Article II, Section 4(c) shall be held in the Administration Account. They shall be used exclusively to cover the costs of the administration of the Trusts.

(b) Should the resources in (a) above be insufficient to meet the administrative expenditures, the difference shall be met from the income earned from the investments.

(c) Upon liquidation of the Trust, all amounts remaining in the Administration Account shall be transferred to the Reserve Account.

## **Section 3. Separation of assets and accounts, audit and reports**

(a) The Resources of the Trust shall be kept separate from the property and assets of all other accounts of the Fund, including other Fund Trusts, and shall be used only for the purposes of the Trust in accordance with this Instrument.

(b) The property and assets held in the other accounts of the Fund shall not be used to discharge liabilities or to meet losses arising out of the administration of the Trust. The resources of the Trust shall not be used to discharge liabilities or to meet losses arising out of the administration of the other accounts of the Fund.

(c) The Fund shall maintain separate financial records and prepare separate financial statements for the Trust.

(d) The external auditor selected under Financial Regulation XII shall audit the financial transactions and records of the Trust. The audit shall relate to the financial year of the Fund.

(e) The Fund shall report on the resources and operations of the Trust in the annual report of the Executive Board to the Governing Council referred to in Financial Regulation XII.

## **Section 4. Investment of resources**

(a) Any balances held by the Trust and not immediately needed in operations shall be invested as established in this section.

(b) Investments will be carried out through treasury securities, *inter alia*: (i) sovereign bonds; ii) corporate fixed income with investment grade; iii) treasury inflation-protected securities/notes.

(c) Following the Fund's internal procedures, Spain shall be kept informed periodically of the investment operations.



(d) The income derived from the investments shall be paid into the Reserve Account after deducting the resources needed to cover the administrative expenses.

## **Article VI. Period of Operation and Liquidation**

### **Section 1. Period of operation**

The Trust established by this Instrument shall remain in effect until forty-five years after its approval. The Fund may extend this period of operation, for as long as is necessary, in the judgement of the Fund, to conduct and to wind up the business of the Trust.

### **Section 2. Liquidation of the Trust**

(a) Upon liquidation of the Trust, all amounts remaining in the Reserve Account after (i) discharge of liabilities authorized to be discharged by the Reserve Account and (ii) the repayment to Spain up to an amount equivalent to the donations granted by Spain to the Trust, shall be used to discharge any liabilities of the Trust.

(b) Any remaining resources shall be transferred to the Fund, unless Spain and the Fund otherwise agree.

## **Article VII. Miscellaneous Provisions**

### **Section 1. Limitation of liability**

The Fund shall not be liable for acts or obligations of the Trust, solely by reason of its capacity of Trustee.

### **Section 2. Modifications**

Any modifications to the terms and conditions established in this Instrument shall be made in consultation with Spain.

## Results of the financial model

### 1. Payment of the Spanish cofinancing facility to the Trust Fund:

A total of EUR 300 million will be received as follows:

	Year 2010	Year 2011	Year 2012
Principal	285.5	0.0	0.0
Grant portion	4.5	5.0	5.0
<b>Total</b>	<b>290.0</b>	<b>5.0</b>	<b>5.0</b>

2. **Repayment of the Spanish cofinancing facility:** Repayment of principal will be based on the same amortization schedules that the Trust Fund will have with the borrowers. A grace period of five years will apply. Repayment of interest is assumed at a constant rate of the current Euro interbank offered rate (Euribor) flat rate of 1.1 per cent on the outstanding loan amount.
3. **Programme of work:** The programme of work for the Spanish cofinancing facility is assumed at the total amount of EUR 300 million. Yearly approvals, materializing during IFAD's Eighth Replenishment period, are assumed as follows:

Year 2010	Year 2011	Year 2012
0.0	185.0	115.0

4. **Lending terms and loan portfolio composition:** Projections of the loan flows are derived on the basis of the following lending term parameters and loan portfolio composition:

	Maturity (years)	Grace period (years)	Interest rate (percentage)	Allocation (percentage)
Highly concessional	40	10	0.75	37
Intermediate	20	5	0.65	13
Ordinary	18	3	1.30	50

Note: For modelling purposes, the interest rate for intermediate and ordinary loans is assumed constant at Euribor of 1.1 per cent plus a fixed spread of 20 basis points.

5. **Disbursements:** Disbursements are projected based on disbursement profiles by the three lending terms, with disbursements periods ranging from 10 to 11 years. Loans to Trust Fund borrowers are assumed to disburse 100 per cent of the approved amount.
6. **Lending reflows:** Projections of future loan principal and interest reflows are based on the lending terms and loan portfolio composition (see table in point 4 above).
7. **Arrears:** Based on historical levels of loan arrears, it is assumed that 3 per cent of principal and interest payments could fall into arrear status. The corresponding amount is assumed to be transferred into the reserve account, in order to provide the necessary funding to materialization of arrears.

8. **Administrative costs:** IFAD will retain 20 basis points on the interest/service charge levied to borrowers in order to cover administrative costs.
9. **Investment income:** The unused balance in both the Trust Fund and the reserve account are assumed to return 1.5 per cent per year.
10. **Ending balances:** As shown in the following table, under the above assumptions, the estimated ending balance at the end of the loan (45 years) is estimated at a total of EUR 14.2 million, as shown below.

**Ten-year summary results derived from the financial model**

(in Euro)

	<i>Years 2010-2019</i>	<i>Years 2020-2029</i>	<i>Years 2030-2039</i>	<i>Years 2040-2049</i>	<i>Years 2050-2055</i>	<i>Total</i>
Spanish support	300 000 000	-	-	-	-	300 000 000
Loan disbursements	(263 892 431)	(35 907 569)	-	-	-	(299 800 000)
Interest on loans	7 507 757	15 707 299	4 887 795	2 062 127	90 051	30 255 029
Principal repayment on loans	53 361 489	155 045 704	46 571 844	36 475 667	8 345 296	299 800 000
Front fee IFAD	(200 000)	-	-	-	-	(200 000)
IFAD Management fee	(1 524 733)	(3 421 658)	(1 299 755)	(549 900)	(24 014)	(6 820 060)
Financial income	26 381 521	2 467 938	1 010 920	795 265	415 441	31 071 085
Interest on Spanish loan	(27 105 762)	(18 027 628)	(6 685 707)	(2 784 667)	(103 921)	(54 707 685)
Spanish loan reimbursements	(50 816 228)	(147 650 261)	(44 350 439)	(34 735 833)	(7 947 239)	(285 500 000)
Trust Fund balance	43 735 866	12 026 501	12 187 254	13 467 717	14 248 016	14 248 016
<b>Contingency fund balance</b>	<b>1 850 331</b>	<b>7 049 732</b>	<b>8 619 885</b>	<b>9 793 554</b>	<b>10 051 298</b>	<b>10 051 298</b>
<b>Total general reserve balance</b>	<b>41 885 535</b>	<b>4 976 769</b>	<b>3 567 639</b>	<b>3 674 163</b>	<b>4 196 718</b>	<b>4 196 718</b>
<b>Trust Fund balance</b>	<b>43 735 866</b>	<b>12 026 501</b>	<b>12 187 254</b>	<b>13 467 717</b>	<b>14 248 016</b>	<b>14 248 016</b>