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Proposed Amendments to the Basic Legal Texts of IFAD to Facilitate the Fund's Engagement with the Private Sector

Note to the Governors

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Governing Council — Forty-second Session
Rome, 14-15 February 2019

For: Approval

Proposed Amendments to the Basic Legal Texts of IFAD to Facilitate the Fund's Engagement with the Private Sector

Recommendation for approval

In accordance with the recommendation of the Executive Board at its 125th session in December 2018, the Governing Council is invited to adopt the draft resolutions contained in document EB 2018/125/R.13, as attached in annex I.

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Proposed Amendments to the Basic Legal Texts of IFAD to Facilitate the Fund's Engagement with the Private Sector

Note to the Executive Board representatives

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Executive Board — 125th Session
Rome, 12-14 December 2018

For: Approval

Recommendation for approval and transmittal to the Governing Council

This report concerns amendments to the Agreement Establishing IFAD and to the Policies and Criteria for IFAD Financing related to IFAD's ability to provide financing to the private sector. The Executive Board is invited to:

- (a) Consider and approve this report, which includes, as annexes, draft Governing Council resolutions providing for such amendments; and
- (b) Approve the transmittal of this report to the Governing Council, including the recommendation that the Governing Council adopt the draft resolutions at its forty-second session in February 2019.

Proposed Amendments to the Basic Legal Texts of IFAD to Facilitate the Fund's Engagement with the Private Sector

I. Introduction

1. This report concerns amendments to the Agreement Establishing IFAD ("the Agreement") and to the Policies and Criteria for IFAD Financing ("the Policies") granting IFAD the ability to enhance its engagement with the private sector. Upon its consideration and approval by the Executive Board in December 2018, this document is to be transmitted as an Executive Board report to the Governing Council with the recommendation that the Governing Council adopt the draft resolutions (attached as annexes) at its forty-second session in February 2019.
2. IFAD, the Food and Agriculture Organization of the United Nations (FAO) and the World Food Programme (WFP) estimate that an additional US\$265 billion per year is needed to end hunger globally by 2030.¹ Following the adoption of the Addis Ababa Action Agenda, engaging strategically with the private sector to achieve the 2030 Agenda for Sustainable Development is a priority for multilateral development banks to maximize the value of their investments.
3. Using a re-engineered country-based model, IFAD will increase its collaboration with the private sector and facilitate the access of private rural small and medium-sized enterprises (SMEs), producers and their organizations to short- to long-term finance. Currently, 70 per cent of all IFAD projects are focused on developing value chains and the local private sector² is already identified as a partner in over 50 per cent of IFAD's loans and grants.
4. However, IFAD recognizes that there is a large gap between supply and demand for support to rural SMEs and the intermediary businesses that serve poor smallholder farmers and other rural producers (e.g. input suppliers, traders, agroprocessors). IFAD has a comparative advantage in filling this gap through its knowledge of rural areas and its large portfolio of projects and programmes that work with these rural private entities.
5. The public-private-producer partnership (4P) model is a systematic approach to involving the local private sector, together with smallholder farmers and their

¹ FAO, IFAD and WFP, *Achieving Zero Hunger: The critical role of investments in social protection and agriculture* (Rome: FAO, 2015).

² These private entities include commercial banks, microfinance institutions, input suppliers, equipment-leasing firms, private extension and advisers, aggregators, processors, wholesalers, retailers and exporters.

organizations, as equal partners in IFAD-supported projects. The Agri-Business Capital (ABC) Fund, a blended finance fund to be launched in early 2019, will help to meet the growing demand of thousands of small farmers and rural agribusinesses that face structural challenges in attracting the financial services necessary to develop their activities. By adopting more innovative financial mechanisms, IFAD will spur inclusive development by enhancing access to short- to long-term finance that will in turn create markets and services for poor small-scale producers, particularly women and youth.

6. Moving forward, as part of its commitment for the Eleventh Replenishment of IFAD's Resources (IFAD11), the Fund will strive to strengthen its engagement with the private sector through a revised Private-Sector Strategy (PSS). The PSS will streamline and articulate both private sector funding to IFAD and private sector financing by IFAD to achieve this goal. Regarding the latter, IFAD will focus on investments in rural areas that reduce risk and create an enabling environment. IFAD will act as an assembler of finance and a broker to crowd in private investments in rural areas, helping small-scale producers, "agripreneurs" and their organizations to become competitive business partners; and in doing so, better serve IFAD's target group of poor smallholder farmers. In order to ensure that IFAD fulfils its mandate – for both ongoing and future initiatives – this report proposes amendments to the Agreement and the Policies, granting IFAD the ability to engage more effectively with the private sector.
7. Currently the Agreement limits IFAD financing to developing States that are Members of the Fund or to intergovernmental organizations in which Members participate. In proposing this new framework, IFAD is endeavouring to diversify its lending portfolio by broadening the scope of lending to include private sector counterparties and invest in equity funds and other financing methods targeting rural SMEs and smallholder cooperatives. This will allow IFAD to fund a wider range of projects that promote small-scale farming, climate-smart solutions, post-harvest technologies that reduce food losses, and sustainable agricultural output.
8. Procedures including ceilings and risk-mitigation measures will be approved subsequently by the Executive Board.
9. All financing of private sector activities shall follow existing review and approval procedures, including approval by the Executive Board.

II. Proposed amendments to the Agreement Establishing IFAD

10. The following amendments are proposed to deepen IFAD's engagement with the private sector in order to meet growing demand from Member States to broaden the Fund's positive impact by including financing for private sector organizations and enterprises. This will allow IFAD to extend loans directly to smallholder cooperatives and SMEs, or indirectly invest capital in equity funds or other financing facilities that offer financial and advisory services to these target groups.
11. Article 7, sections 1(b), 2(a) and 2(f) of the Agreement are to be amended to read as follows (added text is underlined and deleted text is shown in strikethrough):

Article 7, section 1(b):

Financing by the Fund shall be provided only ~~to~~ for the benefit of developing States that are Members of the Fund~~, or~~ Such financing may be provided directly to developing Member States or through ~~to~~ intergovernmental organizations in which such Members participate ~~or to, or through,~~ private sector organizations and enterprises. In the case of a loan to an intergovernmental organization, the Fund may require suitable governmental or other guarantees.

Article 7, section 2(a):

Financing by the Fund ~~shall~~ may take the form of loans, grants, ~~and~~ a debt sustainability mechanism, equity or other means, which shall be provided on such terms as the Fund deems appropriate, having regard for to the economic situation and prospects of the Member and ~~to~~ the nature and requirements of the activity concerned. The Fund may also provide additional financing for the design and implementation of projects and programmes, financed by the Fund through loans, grants, ~~and~~ debt sustainability mechanisms, equity or other means, as the Executive Board shall decide.

Article 7, section 2(f):

The loan agreement, or other agreements, as may be relevant, shall be concluded in each case by the Fund and the recipient which shall be responsible for the execution of the project or programme concerned.

12. It is recommended that the proposed amendment be adopted by the Governing Council in accordance with article 12 of the Agreement.

III. Procedures for amending the Agreement Establishing IFAD

13. Article 12 of the Agreement vests the Governing Council with the authority to adopt any amendment to the Agreement. An amendment may originate either from a Member State of the Fund or may be proposed by the Executive Board. In the event that it proposes an amendment, the Executive Board is required to submit its recommendation to the Governing Council and communicate it to the President of IFAD, who then notifies all Member States. The adoption by the Governing Council of a proposed amendment requires a majority of four fifths of the total number of votes. With the exception of four stated cases, the amendment process does not require acceptance by Member States and takes effect when provided for by the resolution.
14. Article 12 of the Agreement reads:
 - "(a) Except in respect of Schedule II:
 - (i) Any proposal to amend this Agreement made by a Member or by the Executive Board shall be communicated to the President who shall notify all Members. The President shall refer proposals to amend this Agreement made by a Member to the Executive Board, which shall submit its recommendations thereon to the Governing Council.
 - (ii) Amendments shall be adopted by the Governing Council by a four-fifths majority of the total number of votes. Amendments shall enter into force three months after their adoption unless otherwise specified by the Governing Council, except that any amendment modifying:
 - (A) the right to withdraw from the Fund;
 - (B) the voting majority requirements provided for in this Agreement;
 - (C) the limitation on liability provided for in Section 3 of Article 3;
 - (D) the procedure for amending this Agreement;
 shall not come into force until written acceptance of such amendment by all Members is received by the President.
 - (b) In respect of the several parts of Schedule II, amendments shall be proposed and adopted as provided in such parts.
 - (c) The President shall immediately notify all Members and the Depositary of any amendments that are adopted and of the date of entry into force of any such amendments."

15. Rule 34.3 of the Rules of Procedure of the Governing Council further specifies that:
- "The adoption of amendments to the Agreement shall require at least four-fifths of the total number of votes in the Governing Council, except that in respect of the several parts of Schedule II to the Agreement amendments shall be adopted as provided in the respective paragraphs thereof."
16. The amendment contained in the draft resolution, for adoption in accordance with the procedures set forth in article 12 of the Agreement, does not fall within the exceptions specified in article 12(a)(ii)(A),(B),(C) and (D) of the Agreement, and thus does not require acceptance by Member States.
17. Pursuant to Article 12(a)(ii), amendments enter into force three months after the Governing Council adopts the draft resolution unless the Governing Council specifies another date. In the case of the proposed amendment, the last paragraph of the draft resolution specifies that the amendment will enter into force on the date of the adoption of the PSS by the Executive Board.

IV. Proposed amendments to the Policies and Criteria for IFAD Financing

18. In addition to the proposed amendments to the Agreement, which will give IFAD the flexibility to engage with the private sector, it is also necessary to make amendments to the Policies in order to introduce new products that will allow IFAD to lend to private sector organizations and enterprises, including investment funds. This is consistent with Article 7, section 1(e) of the Agreement, which states that financing by IFAD "shall be governed by broad policies, criteria and regulations laid down, from time to time, by the Governing Council...". The establishment of new financing instruments, as proposed in the draft revised Policies, namely "loans to the private sector" and "equity or other means", shall be reflected in a policy approved by the Governing Council. As provided in paragraph 4 of the Policies, while the Governing Council retains "authority to establish the broad policies, criteria and regulations that govern financing by the Fund, the Council acknowledges that the Executive Board has the primary responsibility to set out the detailed policies governing such financing...". In this respect, IFAD's engagement with the private sector will be framed under a revised PSS, which will be presented to the Executive Board in April 2019. The new PSS will build on the existing PSS, which was approved in December 2011. It will reflect the many changes that have occurred since 2011, including: the development of IFAD's 4P approach; the establishment of the ABC Fund; IFAD's formal global-level partnerships with multinational companies; and other cofinancing and public-private partnership arrangements aimed at facilitating private investment in rural areas and delivering greater results in a decentralized environment. The new PSS will also provide a forward-looking roadmap and the basic principles and parameters for investment in the private sector.
19. The sections of the Policies that are proposed for modification are as follows (added text is underlined and deleted text is shown in strikethrough):
3. The Lending Policies and Criteria were amended by the Governing Council several times between 1994 and 1998, but the document was not updated or reviewed thereafter. In 2010, the Governing Council instructed the Executive Board to "submit to the thirty-fourth session of the Governing Council in 2011 revised Lending Policies and Criteria that shall take into account all developments since the last revision of the Lending Policies and Criteria in 1998 and express concisely and clearly the broad policies and criteria applicable to financing by the Fund." As a result, the Policies and Criteria for IFAD Financing were adopted by the Governing Council in February 2013. In 2018 and in 2019, the Policies and Criteria for IFAD Financing were amended to reflect changes

required to give effect to the Transition Framework and the engagement with the private sector."

(...)

11. Project and programme Country criteria. Projects and programmes submitted for financing by the Fund shall be based as much as possible on results-based country strategic opportunity programmes or on other strategies that provide a framework for making strategic choices about the Fund's operations in a Member State, identifying opportunities for Fund financing and facilitating management for results.

(...)

13. Implementation of projects and programmes. The implementation of projects and programmes financed by the Fund must be consistent with the regulations on the procurement of goods and services to be financed from resources of the Fund adopted by the Executive Board, and in conformity with the policies on corruption, audit and supervision adopted from time to time by the Executive Board. Financing agreements with Member States shall be subject to the General Conditions for Agricultural Development Financing established by the Executive Board. Financing agreements with private sector organizations and enterprises shall be subject to the Private-Sector Strategy adopted by the Executive Board. Projects and programmes are supervised by the Fund in accordance with the Policy on Supervision and Implementation Support established by the Executive Board.

(...)

IV. Financing terms

15. With due regard to the long-term viability of the Fund and the need for continuity in its operations, the Fund provides financing through loans, grants, and a debt sustainability mechanism, equity or other means. The Fund's financing of private sector organizations and enterprises shall be for the purpose of assisting the Fund in fulfilling its objectives under the Agreement and shall not, at any time, exceed the prudential limits at individual or portfolio levels as determined by the Fund's risk framework and policies.

A. Loans³

- (a) Loans to the public sector

(...)

- (b) Loans to the private sector

The Fund shall provide loans to private sector entities in accordance with the Private Sector Strategy established by the Executive Board or pursuant to other approvals granted by the Executive Board.

(...)

- (e) Equity or other means

The Fund shall provide financing through equity or other means in accordance with the Private Sector Strategy established by the

³ It is proposed that paragraph 15(a) on loans be split into: (a) loans to the public sector; and (b) loans to the private sector. The section on loans to the public sector will not require any changes since it will continue to apply to financing through loans provided by IFAD to its borrowing Member States.

Executive Board or pursuant to other approvals granted by the Executive Board.

V. Implementation of the amendments to the Policies

20. As already mentioned, paragraph 4 of the Policies provides that the Governing Council "while retaining its authority to establish the broad policies, criteria and regulations that govern financing by the Fund, acknowledges that the Executive Board has the primary responsibility to set out the detailed policies governing such financing". Paragraph 18 further provides that: "The Executive Board shall establish from time to time other policies for financing that may be required or may be appropriate in order to fulfil the objective of the Fund." Based on this authority, and in view of the need to maximize IFAD's flexibility in its engagement with the private sector, a new Private Sector Strategy will be brought to the Executive Board for approval in April 2019.

VI . Conclusion

21. In light of the above, it is proposed that the Executive Board present the two attached resolutions for adoption by the Governing Council at its forty-second session in February 2019.

Draft resolution ____/XLII

Amendment to the Agreement Establishing IFAD

The Governing Council of IFAD,

Having considered the Executive Board's report EB 2018/125/[R.X], Proposed Amendments to the Basic Legal Texts of IFAD to Facilitate the Fund's Engagement with the Private Sector;

Having noted the proposal, made pursuant to article 12 of the Agreement Establishing IFAD, for amendment of the Agreement Establishing IFAD;

Noting the Executive Board's report and recommendation to the Governing Council submitted in accordance with article 12 of the Agreement Establishing IFAD;

Acting in accordance with article 12 of the Agreement Establishing IFAD;

Adopts the Agreement Establishing IFAD, as revised below, which shall take effect from the date of the approval by the Executive Board of the revised IFAD Private Sector Strategy:

Hereby decides:

1. Article 7, section 1(b) is hereby amended to read as follows (added text is underlined and deleted text is shown in strikethrough):

Financing by the Fund shall be provided only ~~to for the benefit of~~ developing States that are Members of the Fund, ~~or~~, ~~Such financing may be provided directly to developing Member States or through~~ to intergovernmental organizations in which such Members participate ~~or to, or through, private sector organizations and enterprises~~. In the case of a loan to an intergovernmental organization, the Fund may require suitable governmental or other guarantees.

2. Article 7, section 2(a) is hereby amended to read as follows (added text is underlined and deleted text is shown in strikethrough):

Financing by the Fund ~~shall may~~ take the form of loans, grants, ~~and~~ a debt sustainability mechanism, equity or other means, which shall be provided on such terms as the Fund deems appropriate, having regard ~~for~~ to the economic situation and prospects of the Member and ~~to~~ the nature and requirements of the activity concerned. The Fund may also provide additional financing for the design and implementation of projects and programmes, financed by the Fund through loans, grants, ~~and~~ debt sustainability mechanisms, equity or other means, as the Executive Board shall decide.

3. Article 7, section 2(f) is hereby amended to read as follows (added text is underlined):

The loan agreement, or other agreements, as may be relevant, shall be concluded in each case by the Fund and the recipient which shall be responsible for the execution of the project or programme concerned.

Draft resolution .../XLII

Revision of the Policies and Criteria for IFAD Financing

The Governing Council of IFAD,

Recalling resolution 178/XXXVI, in which it decided upon the proposal of the Executive Board to approve the Policies and Criteria for IFAD Financing;

Having reviewed the proposed revisions to the Policies and Criteria for IFAD Financing submitted by the Executive Board as contained in document GC 42/L.X;

Adopts the Policies and Criteria for IFAD Financing, as revised below, which shall take effect from the adoption of the revised Private Sector Strategy by the Executive Board;

Tasks the President with maintaining a consolidated text of the policies and guidelines adopted by the Executive Board pursuant to the Policies and Criteria for IFAD Financing hereby adopted;

Hereby decides:

1. Section 1, paragraph 3 of the Policies is hereby amended to read as follows (added text is underlined):
 3. The Lending Policies and Criteria were amended by the Governing Council several times between 1994 and 1998, but the document was not updated or reviewed thereafter. In 2010, the Governing Council instructed the Executive Board to "submit to the thirty-fourth session of the Governing Council in 2011 revised Lending Policies and Criteria that shall take into account all developments since the last revision of the Lending Policies and Criteria in 1998 and express concisely and clearly the broad policies and criteria applicable to financing by the Fund." As a result, the Policies and Criteria for IFAD Financing were adopted by the Governing Council in February 2013. In 2018 and in 2019, the Policies and Criteria for IFAD Financing were amended to reflect changes required to give effect to the Transition Framework and the engagement with the private sector.
2. Section III, paragraph 11 of the Policies is hereby amended to read as follows (added text is underlined and deleted text is shown in strikethrough):
 11. Project and programme Country criteria. Projects and programmes submitted for financing by the Fund shall be based as much as possible on results-based country strategic opportunity programmes or on other strategies that provide a framework for making strategic choices about the Fund's operations in a Member State, identifying opportunities for Fund financing and facilitating management for results.
3. Section III, paragraph 13 of the Policies is hereby amended to read as follows (added text is underlined):
 13. Implementation of projects and programmes. The implementation of projects and programmes financed by the Fund must be consistent with the regulations on the procurement of goods and services to be financed from resources of the Fund adopted by the Executive Board, and in conformity with the policies on corruption, audit and supervision adopted from time to time by the Executive Board. Financing agreements with Member States shall be

subject to the General Conditions for Agricultural Development Financing established by the Executive Board. Financing agreements with private sector organizations and enterprises shall be subject to the Private Sector Strategy adopted by the Executive Board. Projects and programmes are supervised by the Fund in accordance with the Policy on Supervision and Implementation Support established by the Executive Board.

Financing terms, section IV

4. Paragraph 15 of the Policies is hereby amended to reflect the change introduced in article 7, section 2(a) of the Agreement Establishing IFAD (added text is underlined and deleted text is shown in strikethrough):
 15. With due regard to the long-term viability of the Fund and the need for continuity in its operations, the Fund provides financing through loans, grants, and a debt sustainability mechanism, equity or other means. The Fund's financing of private sector organizations and enterprises shall be for the purpose of assisting the Fund in fulfilling its objectives under the Agreement and shall not, at any time, exceed the prudential limits at individual or portfolio levels as determined by the Fund's risk framework and policies.
5. Paragraph 15(a) on loans is split into: (a) loans to the public sector and (b) loans to the private sector. Paragraphs 15(b) on grants, and 15(c) on debt sustainability mechanism will become paragraphs 15(c) and 15(d) respectively. Paragraph 15 section IV of the Policies is therefore hereby amended to read as follows (added text is underlined):

A. Loans

(a) Loans to the public sector

(...)

(b) Loans to the private sector

The Fund shall provide loans to private sector entities in accordance with the Private Sector Strategy established by the Executive Board or pursuant to other approvals granted by the Executive Board.

6. A new paragraph 15(e) is added to reflect the change introduced in article 7, section 2(a) of the Agreement Establishing IFAD (added text is underlined):

(e) Equity or other means

The Fund shall provide financing through equity or other means in accordance with the Private Sector Strategy established by the Executive Board or pursuant to other approvals granted by the Executive Board.