

## **Addendum Paper to Special Study PE08-434S**

### **1. BACKGROUND**

Evaluation Department ('EvD') issued a Special Study concerning the EBRD Trade Facilitation Programme on 6 July 2010 (the 'Study'), which was presented at Audit Committee on 12 July 2010. Due to the time needed to provide a considered response to the Study, Management proposed not to submit full Management Comments at that time, but to return to Audit Committee at a later date with a full response to EvD recommendations. It was also agreed at the Audit Committee meeting that EvD would be able to provide its view on the Management Comments.

The purpose of this Addendum is to present EvD responses to the final Management Comments, that have now been submitted. EvD notes that there are substantial areas of agreement in the Management Comments, particularly on many of the key recommendations. Further comment has only been provided by EvD where considered necessary.

### **2. EvD RESPONSES**

#### **Recommendation 3: TFP must develop an agreed framework for measuring success that reflects the new strategy.**

EvD agrees with Management that the right time to consider performance measurement criteria is in conjunction with the Programme review. It will only be possible to determine the appropriate measurement parameters after operational and transition impact objectives have been restated and refinements to the TFP product agreed. Average transaction size and number of intra regional transactions describe an aspect of TFP activities but it will only be possible to assess the usefulness of these criteria as indicators of achievement of objectives, or their usefulness as indicators of impact or outcome, as part of the Programme review.

#### **Recommendation 5: For certain countries where transparency is lacking, TFP must ensure its activities are aligned to EBRD's country strategy.**

In countries where issues of financial transparency and disclosure in the corporate sector are acute, TFP must be satisfied that Issuing Banks have adequate mechanisms in place to minimise the passing on of inappropriate transactions to TFP, such as those at undervalue. This is particularly applicable to guarantee transactions where EBRD is party to the transaction paper trail.

#### **Recommendation 8: Clear demarcation lines need to be established between TFP products and other overlapping products of the Bank.**

EvD agrees that meeting eligibility criteria for utilising credit line products is a key feature. On reflection, EvD also agrees that it is overly harsh to conclude that providing the opportunity for Participating Banks to select between EBRD products on the basis of the lowest level of conditionality tarnishes the reputation of the Bank. However, it is to be stressed that banks reported that they find product overlap confusing and will actively choose the product with the lowest level of conditionality. To the extent that overlaps can be reduced to a minimum, it will only enhance the effectiveness of both TFP and credit line products.

**Recommendation 12: TFP must cooperate with ESD to rectify deficiencies in environmental execution.**

EvD emphasises the recommendation that all transaction files should be clear on the environmental rating or express the reason for exemption from rating. TFP should be prepared to question transactions that have not been rated or may not be considered as consistent with a rating of low risk. Transaction files should be clear where clarification has been sought, including the reasoning behind accepting a transaction that has been questioned. EvD notes Management's willingness to track cases that have been referred to the Environment and Sustainability Department.

**Recommendation 15: The current TFP approach to AML and similar issues requires a comprehensive overhaul.**

EvD notes Management's position that AML processes are now sufficiently robust. EvD notes that new procedures or requirements have been prepared and implemented with respect to i) transactions where neither party is in an EBRD country of operation and ii) establishing documentary paper trails relating to cross border trade. In addition EvD is aware that a higher level of declaration is now required under each transaction disbursement request such that the Participating Bank represents and warrants that the transaction is 'fully compliant with all commercial laws, tax regulations and central bank regulations in [country of applicant / sub borrower]'.<sup>1</sup>

EvD does not concur that this corresponds to new procedures enabling TFP or Participating Banks to 'assess whether there are indicators of tax evasion, money laundering or terrorists financing schemes, or inconsistent terms of trade.'<sup>2</sup> Therefore EvD appreciates Management's willingness to liaise further with OCCO. EvD emphasises the additional sensitivity of inappropriate transactions under the guarantee product, where EBRD is party to the transaction paper trail.

EvD notes the wording in the MCs that 'these steps have been agreed with Internal Audit'. EvD is aware that new TFP approaches have been implemented in consultation with IA but is not aware of any formal agreement. EvD has confirmed with Internal Audit ('IA') that Management remains solely accountable for the implementation of any IA recommendations.

**Recommendation 17: Banking must introduce a process of monitoring for TFP in line with other frameworks.**

The Programme review (Recommendation 1, agreed by Management) provides an opportunity for Management to reconsider the most appropriate monitoring process for TFP once future programme objectives and measurement parameters have been determined.

**Recommendation 19: FI should consider whether it is appropriate to offer financing specifically for working capital purposes (which is how TFP cash advances have been used predominantly by participating banks) and make explicit product proposals to the Board as necessary.**

For the reasons described in the Study, the collection of contracts and invoices will not provide a trade linkage, only guidance that the sub-borrower has in some way handled goods that have passed borders as some part of their business at a time, or times, around that of the TFP cash advance. TFP participating banks have been implementing TFP cash advances as working capital or loans for general corporate purposes. The opportunity may exist to engage with participating banks on

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<sup>1</sup> TFP standard format documents.

<sup>2</sup> Management Comments.

increasing the sophistication of their working capital product or enhancing skills in transactionally secured trade finance.

**Recommendation 20: New implementation procedures must be prepared and implemented for post LC financing to ensure use of proceeds for trade purposes.**

EvD notes that sub loan agreements will now be provided in connection with post LC financing. EvD emphasises again the potential for post LC financing to be implemented as bank to bank credit, under EBRD guarantee (at nil capital weighting to confirming banks benefiting from the EBRD guarantee) and therefore highlights the value of checking for sub-loan agreements. Sub loan spot checks, as referred to in Management Comments, are well advised to confirm that drawings under the sub-loan agreement have taken place of equivalent tenor and amount to the post LC financing.