



ADB

Policy Paper

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Establishing the Legal Framework for the Use of Asian Development Fund Resources for Grants

Asian Development Bank

I. INTRODUCTION

1. This paper contains a proposal to revise the Regulations of the Asian Development Fund (ADF Regulations) to enable the use of all resources of the Asian Development Fund (ADF), rather than a specific portion, for grants to be made under the applicable framework for ADF grants.

II. BACKGROUND

2. The use of ADF resources for grants was considered for the first time under the Eighth Replenishment of the ADF (ADF IX). The donors' report for ADF IX stated that "the introduction of grants in ADF IX did not commit future replenishments to continue offering grant assistance".¹ Because of the uncertainty at the conclusion of ADF IX negotiations as to whether the use of ADF grants would be continued, there was no comprehensive amendment of the ADF legal framework to enable the use of all ADF resources for grants. Instead, the ADF Regulations were amended to allow the use of the ADF for grants "in the event and to the extent that the relevant authorizing Resolution of the Board of Governors provides for such financing". Board of Governors' Resolution No. 300 on ADF IX specifically authorized the use of funding provided under ADF IX for grants. As the Board of Governors' resolution on ADF X is expected to be adopted before the amendments proposed in this paper, the draft ADF X resolution also includes a specific authorization for the use of funding provided under ADF X for grants.

3. The ADF IX donors' report recommended a review of the grant allocation framework and its application toward the end of the second year of ADF IX. The framework was discussed extensively at the ADF IX midterm review. The Board of Directors adopted a policy paper² on a revised ADF grant framework in September 2007, which brings the ADF grant allocation system in line with the debt sustainability framework of the International Monetary Fund and the World Bank.

4. The new ADF grant framework assumes ADF resources will continue to be used for grants, depending on the risk of debt distress of the recipient countries. However, as long as there is no general authority to use all ADF resources, in particular reflows from pre-ADF IX resources, for grants, the ADF funding source of every ADF grant needs to be monitored. This requires cumbersome administrative systems. In addition, in the absence of a general authority, specific authority to use future ADF replenishments for grants needs to be sought at every replenishment round. To streamline the replenishment process and the administration of the ADF, it is proposed that the ADF legal framework be amended to allow all ADF resources, regardless of when they were originally committed, to be used for ADF grants in accordance with the ADF grant allocation system. This paper aims to create an enabling legal framework; it does not discuss the issue of compensating the ADF for the funding of grants, which is a matter to be considered in the context of ADF replenishments.

III. PROPOSED CHANGES TO THE ASIAN DEVELOPMENT FUND LEGAL FRAMEWORK

5. The ADF, as a Special Fund of the Asian Development Bank (ADB), is governed by Article 19 of the Agreement Establishing the Asian Development Bank (the Charter). Article 19.3

¹ ADB. 2004. *ADF IX Donors' Report: Development Effectiveness for Poverty Reduction*. Manila.

² ADB. 2007. *Revising the Framework for Asian Development Fund Grants*. Manila.

provides that "Special Funds [...] may be used in any manner and on any terms and conditions not inconsistent with the purpose of the Bank and with the agreement relating to such Funds." With respect to the ADF, the "agreement relating to such Funds" refers to the agreement on the initial contributions and the agreements on the replenishments of the ADF. These agreements are set out in various resolutions of the Board of Governors and the ADF Regulations.

6. Prior to ADF IX, the Board of Governors' resolutions on the ADF did not allow the use of ADF resources for the provision of grants. To enable all ADF resources, including reflows from pre-ADF IX resources, to be used to fund grants, a resolution of the Board of Governors is required authorizing a global amendment of its resolutions on the ADF prior to Resolution No. 300.

7. Section 6.01 of the ADF Regulations provides that "the prior consent in writing of every Contributor shall be required before the coming into effect of any amendment [of the Regulations] modifying (a) the provisions of Section 3.01(a), which specify the manner in which ADB may use the resources of the Fund in its operations".

8. As stated in paragraph 2 above, in connection with ADF IX, the ADF Regulations were amended to allow the use of ADF resources for grants, but with the restriction that such use would only be permitted "in the event and to the extent that the relevant authorizing Resolution of the Board of Governors provides for such financing." Changes need to be made to Sections 3.01, 3.03 and 3.06(b) of the ADF Regulations to delete this restriction and references to specific authorizing resolutions of the Board of Governors. The proposed changes require a modification as specified in Section 6.01 of the ADF Regulations.

9. Written consent from each ADF donor will be sought for the proposed amendment of the ADF Regulations. The ADF Regulations may then be amended by a special resolution of the Board of Directors.

IV. REQUEST FOR BOARD'S GUIDANCE

10. The Board's guidance is sought on the preparation of a draft report to the Board of Governors with a draft resolution as described in paragraph 6 of this paper. Such a draft resolution would be submitted under the special procedure provided under Section 3 of the By-Laws, with a request for a vote by facsimile or e-mail within 30 days of the date of such request.