

## OPERATIONS MANUAL BANK POLICIES (BP)

*These policies were prepared for use by ADB staff and are not necessarily a complete treatment of the subject.*

### PROCESSING SOVEREIGN AND SOVEREIGN-GUARANTEED LOAN PROPOSALS<sup>1</sup>

#### A. The Policy

1. Guided by its country partnership strategies (CPS) for its developing member countries (DMCs), ADB prepares and implements development projects and programs that seek to maximize development impact and optimize ADB's returns on its investments. ADB closely involves the government of the DMC, the borrower (if this is not the government), the executing agency, other stakeholders, and the project beneficiaries at all stages of the project cycle, beginning with project identification. ADB helps its DMCs to formulate and, if necessary, to reformulate projects so that they are viable. ADB ensures that the positive impacts of its investments are maximized and that they do not have any significant negative impacts. All sovereign and sovereign-guaranteed loans, including project loans, sector loans, program loans, credit lines to development finance institutions, technical assistance loans, and multiproject loans follow similar processes.<sup>2</sup>

#### B. Scope of the Policy

##### 1. Scrutiny of Projects during Processing

2. As a matter of policy, ADB examines different aspects of a project at key stages and involves the borrower, project beneficiaries, and other stakeholders. These stages include project identification, design and preparation. Loan negotiations are conducted with the borrower, and the project is considered by the Board for approval.

##### 2. Safeguards

3. ADB has established a set of safeguards related to the environment, resettlement and indigenous people. It ensures that these safeguards are complied with in all its projects. ADB assumes responsibility for conducting due diligence and for reviewing, monitoring, and supervising projects throughout the ADB's project cycle in conformity with the principles and requirements embodied in its safeguard policy statement.<sup>3</sup>

<sup>1</sup> Policies described in this OM section are also applicable to proposals to be financed by Asian Development Fund (ADF) grants and by both a loan and an ADF grant.

<sup>2</sup> Sovereign and sovereign-guaranteed loans are those extended to a government or guaranteed by a government. Emergency assistance loans, subsovereign and nonsovereign loans are processed differently. This OM section does not aim to give a comprehensive description of the operational policy and procedures for a multitranche financing facility. See OM Section D3 (Sector Lending), OM Section D4 (Program Lending), OM Section D5 (Sector Development Programs), OM Section D7 (Disaster and Emergency Assistance), OM Section D10 (Private Sector Operations), OM Section D12 (Technical Assistance), and OM Section D14 (Multitranche Financing Facility).

<sup>3</sup> See ADB. 2009. *Safeguard Policy Statement*. Manila. The safeguard policy statement shall become effective on 20 January 2010.

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### **3. Disclosure of Loan Documents to the Public<sup>4</sup>**

4. It is the policy of ADB to list all loans to be processed on its website (www.adb.org). A project or program information document (PID) is prepared and made publicly available in conformity with the requirements of ADB's public communications policy.<sup>5</sup>

5. The report and recommendation of the President (RRP) is made available to the general public no later than 14 calendar days after approval of the loan by the Board. The borrower is informed of this policy before loan negotiations and, during loan negotiations, it can indicate whether there is information contained in the RRP that it considers confidential. If this information conforms to the public communications policy's exceptions to presumed disclosure, the Board is advised in the circulation memorandum that the RRP has a restricted distribution. Following Board approval, the concerned department then removes the confidential information before disclosing the document, while leaving a reference to the deleted material (with the reason for its removal). Any redaction or the withholding of such documents for public disclosure purposes must be based on the exceptions to presumed disclosure specified in the public communications policy.<sup>6</sup>

### **4. Cost Sharing between ADB and DMC<sup>7</sup>**

6. The country cost-sharing ceiling for loans and Asian Development Fund (ADF) grants is generally set for each DMC in the course of CPS preparation. The ceiling may be revised or confirmed during preparation of the subsequent CPS, or on a stand-alone basis when warranted. Project cost-sharing is based on specific sector, client, and project considerations and sound banking principles. ADB's share in the project cost may exceed or fall below the country cost-sharing ceiling, provided ADB's share in the aggregate cost of the portfolio of projects in a DMC does not exceed the country cost-sharing ceiling over the CPS period.

### **5. Board Consideration**

7. All projects and programs financed by sovereign and sovereign-guaranteed loans are approved by the Board on the recommendation of the President. Some projects undergo full Board discussion before approval, others follow the summary procedure process for approval.<sup>8</sup> Under the summary procedure process, although full loan documentation is submitted to the Board, financial assistance (a loan<sup>9</sup> or ADF grant) is not normally discussed by the Board unless any Board member shall so request. To be eligible for Board consideration under summary

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<sup>4</sup> See OM Section L3 (Public Communications).

<sup>5</sup> The initial PID for a sovereign or sovereign-guaranteed loan and/or ADF grant project that is made publicly available no later than 30 calendar days following approval of a project concept paper will include key project information from the concept paper.

<sup>6</sup> See ADB. 2005. *The Public Communications Policy of the Asian Development Bank: Disclosure and Exchange of Information*, Manila; and OM Section L3 (Public Communications).

<sup>7</sup> See OM Section H3 (Cost Sharing and Eligibility of Expenditures for ADB Financing).

<sup>8</sup> See ADB. 2005. *Revision of the Summary Procedure*. Manila.

<sup>9</sup> Including a technical assistance loan. Emergency projects that meet the above criteria may also be considered under summary procedure.

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procedure, the financial assistance must be consistent with the relevant CPS and must meet all the following conditions.

- (i) The amount of ADB financial assistance should not exceed \$200 million for sovereign and sovereign-guaranteed operations.
- (ii) The project should not involve any exception to an existing ADB policy.
- (iii) The financial assistance should not be for a program, a sector development program,<sup>10</sup> or a project with a major policy reform component.
- (iv) The project should not involve an important new approach for ADB in the developing member country concerned.
- (v) The project should not have the potential for significant adverse environmental, economic and/or social impact, particularly on vulnerable groups that may be unable to absorb such impact
- (vi) The project should not involve use of a complementary financing scheme or a novel financing arrangement.

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<sup>10</sup> See OM Section H5 (Supplementary Financing) on the use of summary procedure for supplementary financing of an investment component of a sector development program.

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**Basis:** This OM section is based on:

ADB. 2009. *Better and Faster Loan Delivery: Report of the Loan Delivery Working Group*. Manila (November).

ADB. 2006. *Further Enhancing Country Strategy and Program and Business Processes*. Manila (August).

ADB. 2005. *Cost Sharing and Eligibility of Expenditures for Asian Development Bank Financing: A New Approach*. Manila (August).

ADB. 2005. *The Public Communications Policy of the Asian Development Bank: Disclosure and Exchange of Information*. Manila (March).

ADB. 2005. *Revision of the Summary Procedure*. Manila (September).

ADB. 2004. *Review of the Asian Development Bank's Policy on the Performance-Based Allocation of ADF Resources*. Manila (December).

ADB. 2004. *Review of the Asian Development Bank's Poverty Reduction Strategy*. Manila (June).

ADB. 2001. *Streamlining the Approval Process of the Board of Directors through More Efficient Use of the Summary Procedure for Loan Proposals*. Manila (July).

ADB. 1992. *Streamlining of Board Documents on Project-Loan and Technical Assistance*. Manila (December).

ADB. 1988. *Streamlining of Technical Assistance Loan Proposals*. Manila (November).

ADB. 1984. *Streamlining of Loan and Technical Assistance Operations* Manila (September).

This OM section is to be read with OM Section D11/OP.

**Compliance:** This OM section is subject to compliance review.

**For inquiries:** Questions may be directed to the Director of the Strategy, Policy, and Interagency Relations Division, Strategy and Policy Department.

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*These procedures were prepared for use by ADB staff and are not necessarily a complete treatment of the subject.*

### PROCESSING SOVEREIGN AND SOVEREIGN-GUARANTEED LOAN PROPOSALS

#### A. Introduction

1. The processes and instruments applicable to ADB sovereign and sovereign-guaranteed loans are set forth below.<sup>1</sup>

#### B. Business Processes

##### 1. Project Concept Clearance

2. A project loan is normally processed when it has been included in the indicative rolling country operations business plan (COBP) and its concept has been approved by the operations vice president.<sup>2</sup> A loan proposal that has not been included in the COBP can be processed if the operations vice president's approval is obtained based on a government request or its agreement to the proposal. For all loan proposals, a concept paper is subject to internal review and approval by the operations vice president. Concept paper clearance requires that sufficient information be provided to enable the operations vice president to make a prima facie judgment on the processing of the project and risk category assignment that will determine the quality assurance approach to be followed.

3. The concept paper includes the rationale, indicative impact, outcome, and outputs, financing plan and implementation arrangements. It also includes the required due diligence with details about the requirements for staff, staff consultants, or project preparation technical assistance (PPTA). Terms of reference,<sup>3</sup> consultancy requirements, and the implementation arrangements of any PPTA should be attached to the project concept paper. The relevant reference documents should be stored in the electronic knowledge repository to be established for the project.<sup>4</sup>

4. The project team leader and project team of the responsible operations department prepare the draft concept paper, where appropriate in consultation with the resident missions concerned. A departmental meeting is held to consider the draft concept paper. The meeting determines the merits of the proposed project and, if it is supported, decides on the risk

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<sup>1</sup> Procedures described in this OM section are also applicable to proposals to be financed by Asian Development Fund (ADF) grants and by both a loan and an ADF grant. All references to "projects" in this OM section also refer to programs. Sovereign and sovereign-guaranteed loans are those extended to the government or guaranteed by the government.

<sup>2</sup> Policies described in this OM section are also applicable to loan proposals included in an annual indicative rolling regional operations business plan.

<sup>3</sup> The scope of any PPTA may include pre-implementation works and this should be reflected in the terms of reference of consultants.

<sup>4</sup> For further information on the proposed electronic knowledge repository, see ADB. 2009. *Country Partnership Strategy: Responding to the New Aid Architecture—Report by the Country Partnership Strategy Working Group*. Manila.

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categorization to recommend to the operations vice president, based on the degree of project complexity, risks, and readiness. After the meeting, a reconnaissance mission would normally be undertaken to further develop and agree with the government the project concept and due diligence requirements, including arrangements for PPTA or other project preparatory support.

5. The concept paper is peer reviewed and necessary revisions are made (see para. 20). The final concept paper, including the key issues and the proposed project risk category, are submitted by the regional director general to the operations vice president for consideration and approval.<sup>5</sup> The operations department may subsequently recommend to the operations vice president a change in the project risk category based on new information gathered during project processing.

6. **Risk categorization and quality assurance process.** At the concept clearance stage, projects are allocated to one of the two categories depending on the level of complexity, risk, and processing readiness. Categorization as a "low risk" project means that it has all of the following features: (i) a loan amount not exceeding \$200 million for projects (or not exceeding \$50 million for programs); (ii) a sound record of ADB's previous experience in the sector in the concerned country; (iii) reasonable executing agency capacity in terms of externally financed project administration; and (iv) safeguard categorization other than A. Unless the project is designated as "low risk" on this basis, it will be considered and classified as "complex" and will require closer scrutiny and a more intensive quality assurance process, including more in-depth due diligence and management and peer review than that required for a "low risk" project.

7. **Project classification.** Loan projects<sup>6</sup> are classified by: type of financial product; financial modality (in order to highlight partnerships); sector and subsector(s); location impact; themes; and targeting. The classification may be tentative at the project identification/concept stage and may be changed during processing. The primary responsibility for the classification of a project rests with the initiating department.

8. **Design and monitoring framework.**<sup>7</sup> The design and monitoring framework is a design tool that logically links the impact or rationale of a project, its outcome, expected outputs, inputs and activities, key indicators (targets, timeframe, and baseline), key risks and assumptions, the analysis that needs to be undertaken, the manner in which data are collected, the expected beneficiaries, and the stakeholders. Conceptualization of the framework starts at the project concept clearance stage and is refined as project processing proceeds. An initial draft of the framework for the lending operation should be attached to the concept paper.<sup>8</sup> Its final version enables project implementation to be monitored, and indicates where and when any remedial interventions need to be carried out.

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<sup>5</sup> Concurrently, the operations vice president approves the PPTA (if required) within his/her approval authority. In the course of circulation of the project concept paper, the director general provisionally approves a small-scale PPTA (if required) within his/her approval authority pending project concept clearance by the operations vice president.

<sup>6</sup> In this context, "loan projects" include project loans, program loans, sector loans, and technical assistance loans.

<sup>7</sup> See also OM Section J1 (Project Performance Management System).

<sup>8</sup> The director signs the design and monitoring framework for circulation. A problem analysis should accompany the DMF.

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### 2. Safeguard Requirements

9. ADB adheres to environmental and social safeguards.<sup>9</sup> ADB carries out project screening and safeguard categorization at the earliest stage of project preparation when sufficient information is available for this purpose. Screening and categorization is undertaken to (i) reflect the significance of potential impacts or risks that a project might present; (ii) identify the level of assessment and institutional resources required for the safeguard measures; and (iii) determine disclosure requirements.

### 3. Project Design

10. **Project preparation and due diligence.** Project design is an evolving process from the time of conceptualization through the design stage to Board approval. The design process involves the project team, the borrower, beneficiaries, consultants, development partners, NGOs, and other stakeholders. The design process usually involves several steps, including project preparatory support, project fact-finding, management review meeting (MRM) or staff review meeting (SRM) depending on risk categorization, loan negotiations, and Board consideration. The project team examines the project design in terms of its technical, financial, macro- and microeconomic, institutional, sectoral policy, legal, and safeguard contexts, in conjunction with the country partnership strategy (CPS), operational experience, and lessons from evaluations of previous projects (available in the evaluation information system database of the Independent Evaluation Department [IED]). Attention is also paid to institutional capacity, cost estimates and financing plans, implementation arrangements (project readiness, procurement, consulting services, project management, disbursements, accounting, and auditing), and possible conditions or covenants. ADB coordinates with other funding agencies.

11. **Fact-finding.** A loan fact-finding mission is conducted by the project team to confirm the viability of the project<sup>10</sup> after sufficient feasibility work has been undertaken either by the government or through ADB's project preparatory support. This would normally be following completion of surveys, initial design work, costing, safeguards, and due diligence to establish the viability of the project. When ADB PPTA is provided, there should be close cooperation between all concerned—consultants, government, and the fact-finding mission.<sup>11</sup> Fact-finding in the course of PPTA implementation ensures the project team remains fully involved and plays an integral role in guiding project preparation; consultants have closer supervision and direction; and the government is more closely involved in the project design. The fact-finding mission would prepare a memorandum of understanding or aide memoire that outlines the agreement with the government on the rationale, impact, outcome, and outputs of the project and on the project administration manual (PAM)<sup>12</sup> that details the project implementation arrangements.

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<sup>9</sup> See ADB. 2009. *Safeguard Policy Statement*. Manila. The safeguard policy statement shall become effective on 20 January 2010, and its operational procedures are laid out in OM Section F1 (Safeguard Policy Statement).

<sup>10</sup> More than one mission may be fielded for this purpose. See Footnote 19.

<sup>11</sup> Care should be taken to ensure that the functions and activities of the loan fact-finding mission staffed by ADB and of the PPTA consultants are not co-mingled. This is because PPTAs are funded from special funds resources, while loan processing by ADB staff is funded from internal administrative expenses, which are part of ordinary capital resources, and each has to be separated from the other.

<sup>12</sup> All references to "project administration manual" or "PAM" in this OM section should be read "facility administration manual" in the case of the multitranches financing facility.

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Subsequent to the fact-finding mission, PPTA consultants would normally further refine the project design to augment and improve project documentation and undertake pre-implementation works.

12. **Project administration manual.** The PAM includes all the information and schedules describing project implementation.<sup>13</sup> The PAM should be agreed with the government at fact-finding.<sup>14</sup> The PAM should also include project readiness filters covering major pre-project implementation actions (e.g., government approvals, procurement, and resettlement) to ensure a rapid start-up and enable early disbursement.

13. **Report and recommendation of the President (RRP).** The RRP presents the project proposal in sufficient detail for Board consideration. Sector assessments, detailed implementation arrangements in the form of the PAM, and other supporting documents should be presented as stand-alone linked documents.

### **4. Quality Assurance Meetings**

14. The draft RRP is reviewed by peer reviewers (see para. 20) before it is submitted to the MRM or SRM.<sup>15</sup> For "complex" projects, an MRM is chaired by the operations vice president with the director general, sector director, and project team in attendance. Other relevant parties may be invited to join the meeting by the regional department or attend at their discretion. The MRM will take decisions on further project processing. For "low-risk" projects, an SRM is chaired by the director general, with the project team in attendance. Other relevant parties may be invited to join the meeting by the regional department or attend at their discretion. The SRM will take decisions on further project processing.

15. The draft RRP presented to the MRM or SRM explains how eligible expenditures are to be financed,<sup>16</sup> and provides an assessment and justification for the financing of expanded eligible expenditures.<sup>17</sup> The MRM or SRM considers the project's viability, the readiness of the project design and analysis, advance contracting under the loan,<sup>18</sup> retroactive financing in principle, risks and the control mechanisms associated with the proposed financing option, and the due diligence that has been carried out. The MRM or SRM will decide whether to give the

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<sup>13</sup> In the case of a program loan, the development policy letter and policy matrix presented as part of the RRP should specify required actions in the form of reform implementation and the PAM would be optional.

<sup>14</sup> Thereafter, PAM should be reviewed by the Management review meeting (MRM) or the staff review meeting (SRM), during loan negotiations, and by loan inception, midterm, and other review missions.

<sup>15</sup> An invitation, with an attached issues note and comment matrix, to attend MRM or SRM is issued by the regional director general (usually, two days prior to the meeting). It should be copied to all peer reviewers.

<sup>16</sup> ADB financing may be provided in a variety of ways, including three options presented in OM Section J6 (Disbursement). When ADB proposes to finance up to 100% of eligible expenditures of every claim up to a point where the balance of grant or loan amounts are fully disbursed, the RRP should indicate the associated risks and the proposed control mechanism for Management's guidance.

<sup>17</sup> See OM Section H3 (Cost Sharing and Eligibility of Expenditures for ADB Financing).

<sup>18</sup> To ensure that the executing agency has the capacity to carry out the actions needed for advance contracting, the project team normally conducts procurement capacity assessment before the MRM or SRM during loan processing.

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project team clearance to proceed with loan negotiations.<sup>19</sup> MRM or SRM will also consider whether to endorse a proposal for recourse to the Board summary procedure.<sup>20</sup> The MRM and SRM minutes should in all cases be signed off by the director general, and should be copied to the operations vice president.

### **5. Loan Negotiations**

16. Before loan negotiations, as part of the usual process of inviting the borrower's representatives to loan negotiations, or at the specific request of the DMC through ADB's official channel of communication in the DMC, the draft loan documents, including the RRP and the PAM both reflecting peer reviewers' comments, will be provided to the borrower. The borrower is advised that the documents do not commit ADB to finance the project or program, and may be revised. The invitation to loan negotiations requires the borrower's negotiating team to indicate any information or data in the loan documents that are to be treated as confidential. The borrower submits a procurement plan for approval by ADB before loan negotiations. The operations department reviews the procurement plan in consultation with Central Operations Services Office (COSO) to obtain its concurrence. The project team leader leads the negotiations, and, when these have been completed, the project counsel prepares minutes for signature by both parties.

17. For loans from ordinary capital resources, the borrower may request brief presentations on the LIBOR-based loan product and associated debt management features from the Treasury Department during loan negotiations.<sup>21</sup> For loans from Asian Development Fund (ADF) resources, the borrower determines the repayment currency out of the special drawing rights currencies during loan negotiations. The borrower can change the repayment currency, provided it gives sufficient advance notice to ADB.<sup>22</sup>

### **6. Board Consideration**

18. When loan negotiations have been completed, the RRP is edited by the Office of the Secretary (OSEC). If major changes to the RRP are not expected as a result of loan negotiations, the RRP may be edited before loan negotiations start. When it has been edited, the RRP is returned by OSEC to the project team leader for finalization. The loan agreement is cleared by the Office of the General Counsel (OGC) and the final RRP is cleared first by OGC (for clearance to circulate to the Board) and then by OSEC (for clearance for printing). The project team leader prepares a memo to the President,<sup>23</sup> with the RRP attached, requesting approval to circulate the RRP to the Board. Usually, unless approved by the Management, at least 21 calendar days are needed between circulation of the loan documents to the Board and

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<sup>19</sup> It is envisaged that a follow-up missions and/or a second SRM would be optional and undertaken if specifically required by either the MRM or the first SRM. If a further mission is called for, loan negotiations should be completed as part of the mission where possible.

<sup>20</sup> ADB. 2005. *Revision of the Summary Procedure*. Manila.

<sup>21</sup> See ADB. 2006. *Enhancements for the Asian Development Bank's Loan and Debt Management Products*. Manila.

<sup>22</sup> See ADB. 2005. *Asian Development Fund Currency Management Proposal*. Manila.

<sup>23</sup> The memo should be coursed from the regional director general through the operations vice president. The recommendation for the President's final decision on the summary procedure should be stated in the memo,

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Board consideration. After Board approval of the loan documents, the operations department<sup>24</sup> is responsible for arranging the prompt signing of the loan agreement by the borrower's representative, and for ensuring that any loan conditions have been met by the borrower. OGC is responsible for declaring the acceptance of a legal opinion and that other documents that may be required by the loan agreement are satisfactory to ADB.<sup>25</sup>

### **7. Disclosure of Loan Documents**

19. Sovereign and sovereign-guaranteed loan and/or ADF grant agreements, related project agreements, pertinent RRP, and project information documents shall be made publicly available in accordance with the requirements of the public communications policy.<sup>26</sup>

### **C. Peer Review in the Course of Loan Processing**

20. A two-fold peer review process during processing of loans comprises: (i) a specific cross-departmental review; and (ii) a sector-focused review. The cross-departmental review takes place on specific technical aspects of the project design and implementation arrangements. The Economics and Research Department (on economic analysis), Controller's Department (on investment and financing plans, and disbursement), COSO (on procurement, and DMF), IED (independent feedback on operations), Office of Cofinancing Operations (in cases where cofinancing is proposed), Office of Regional Economic Integration (in cases of interventions addressing regional cooperation and integration), the Regional and Sustainable Development Department (on safeguards by the Environment and Safeguards Division), and the Office of the General Counsel (on legal matters) should be engaged in this process.<sup>27</sup> The sector-focused review concentrates on technical advice on the sector concerned, whereby the full RRP is sent to the head of the community of practice (CoP) to coordinate a comprehensive sector-focused review of the proposal. Peer reviews' comments should focus on their areas of direct expertise. Sector-focused peer reviewers are acknowledged in the RRP.

### **D. Retrospective Stocktaking of Approved Loans**

21. ADB may undertake assessment of quality-at-entry of approved loans as part of a biennial retrospective review of projects prepared and approved over a respective review period to examine their quality, assess the areas for improvement and those where improvements are needed.

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<sup>24</sup> The regional director general has the authority for loan and grant signing, and the authority to delegate this function. See ADB. 2009. *Better and Faster Loan Delivery: Report of the Loan Delivery Working Group*. Manila.

<sup>25</sup> See OM Section J5 (Effectiveness of the Loan Agreement).

<sup>26</sup> See ADB. 2005. *The Public Communications Policy of the Asian Development Bank: Disclosure and Exchange of Information*. Manila; and OM Section L3 (Public Communications).

<sup>27</sup> Operations departments should copy draft RRP or sections of RRP for review and may consult with other departments or offices, as well as the concerned resident mission, that may provide inputs specifically on technical matters in the areas of their direct expertise.

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**Basis:** This OM section is based on OM Section D11/BP and the documents cited therein.

**Compliance:** This OM section is subject to compliance review.

**For inquiries:** Questions may be directed to the Director of the Strategy, Policy, and Interagency Relations Division, Strategy and Policy Department.