

***CREF***  
***Financial Intermediation Mechanism***  
(Final Draft)

CREF Senior Adviser  
and Working Group  
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**List of Abbreviations**

ADB	Asian Development Bank
AEPC	Alternative Energy Promotion Centre
CEO	Chief Executive Officer
CREF	Central Renewable Energy Fund
CRS	Corporate Social Responsibility
Danida	Danish International Development Assistance
DEEU	District Energy and Environmental Unit
DFID	Department for International Development (UK)
ED	Executive Director (of AEPC)
EoD	Embassy of Denmark
ESAP	Energy Sector Assistance Programme
GESI	Gender and Social Inclusion
GIZ	German Agency for International Cooperation
GoN	Government of Nepal
HR	Human Resources
KfW	Kreditanstalt für Wiederaufbau (Reconstruction Credit Institute)
LFI	Local Finance Institution
MoF	Ministry of Finance
MSTE	Ministry of Science, Technology and Environment
NGO	Non-governmental Organisation
NRB	Nepal Rastra Bank
NRREP	National Rural and Renewable Energy Programme
PDF	Power Development Fund
PPB	Prequalified Partner Bank
REF	Rural Energy Fund
RET	Renewable Energy Technology
RSC	Regional Service Centre
SREP	Scaling Up Renewable Energy Programme (World Bank and ADB)
ToR	Terms of Reference
WB	World Bank

## Executive Summary

The Central Renewable Energy Fund (CREF) will be established as the financial intermediation mechanism for the renewable energy sector under the National Rural and Renewable Energy Programme (NRREP).

### Objective and Scope

The objective of CREF is as the core financial mechanism to be responsible for the effective delivery of subsidies and credits to the renewable energy sector.

The indicative budget for CREF for the period 2012-17 is shown in the table below.

CREF Budget Commitment	USD (million)
Danida	11.4
Norway	10.5
DFID	7.6
KfW	2.9
SREP	20.0
Government of Nepal	63.9
<b>Total</b>	<b>116.3</b>

Once established and proven as an effective financing mechanism for the sector, it is expected that further funds will be committed to CREF by the Government and development partners given the importance of renewable energy in protecting the environment and contributing to rural livelihoods and development.

### The Financial Intermediation Mechanism

The CREF Financial Intermediation Mechanism will be implemented through private commercial and development banks selected on a transparent and competitive basis in accordance with well-defined eligibility criteria.

A Handling Bank – the apex financial institution - will be responsible for managing the core functions of CREF i.e. wholesale lending to Prequalified Partner Banks; Subsidy Fund Management; and Investment Management.

A number of Prequalified Partner Banks – the second-tier financial institutions - will be responsible for the retailing of CREF funds to eligible projects in the renewable energy sector. In order to enhance

the outreach, the banks will be required to form strategic alliances with local financial institutions (LFI).

The modality of using Prequalified Partner Banks and LFIs is based on past experience of AEPC (Alternative Energy Promotion Centre) and ESAP (the Energy Sector Assistance Programme) and will significantly upscale this experience and link it to a Handling Bank as the apex financial institution responsible for fund management.

The selected banks will take the credit risks, which will be reflected in the interest spreads, and as such they will also be responsible for loan appraisal and supervision. Cost of fund management and interest margins will be a parameter in the competitive bidding process. CREF will, through the Secretariat, assist the banks with capacity building in order to increase outreach, efficiency, infrastructure and stability of the financial systems for lending to the renewable energy sector.

### The CREF Investment Committee and Secretariat

The NRREP Programme Steering Committee under the chairmanship of the Secretary, Ministry of Science, Technology and Environment (MSTE) decides on the overall priorities of the programme and is overall responsible for the implementation of all components including CREF. Given the specific focus of CREF on financial sector activities, a specialised subcommittee will be established for the strategic management and oversight of the CREF financial intermediation mechanism – the CREF Investment Committee. The membership of the Investment Committee will reflect the nature of CREF and include representation from Ministry of Finance, Nepal Rastra Bank, MSTE, AEPC, the private sector and the development partners.

The CREF Investment Committee will establish a Secretariat as its operational arm. The Secretariat will be responsible for monitoring the performance of the selected banks, promote CREF activities, capacity assessment and development of banks, and for liaison and coordination with AEPC. It will initially be financed out of NRREP funds, will have a professional staff of two and be housed in the Handling Bank in order to facilitate close and efficient interaction on a daily basis.

**Institutional Links with AEPC**

The AEPC is mandated to develop and promote renewable and alternative energy technologies. It has established an outreach structures through Regional Service Centres and District Energy and Environmental Units. Through these structures AEPC are supporting project developers (communities, households, manufacturers, installers, distributors) in preparing bankable projects to be presented to the Prequalified Partner Banks and LFIs. AEPC is, furthermore, the point of entry for subsidy applications and is responsible for the technical verification before submitting to the Handling Bank for financial verification and payment in accordance with the Government's Subsidy Policy and Delivery Mechanism.

A National Project Facilitation Adviser will be recruited by NRREP to assist the Executive Director in supporting technical components and Regional Service Centres in identifying and developing bankable projects with the project developers. The Adviser will be responsible for ensuring a smooth and effective processing of subsidy applications within AEPC. He or she will also be responsible for the coordination and liaison with the CREF Secretariat.

AEPC through its technical components and outreach structures will support demand-side management, while CREF through the Secretariat and the selected financial institutions supports supply-side management for the development and financing of renewable energy technologies.

On the strategic management level the AEPC Executive Director will be a member of the CREF Investment Committee, is Secretary/Ex-officio member of the NRREP Programme Steering Committee and is the NRREP Programme Director.

**Financial Management and Control**

Funds from Government of Nepal and development partners will be channelled to the Handling Bank through Treasury based upon requests approved by the CREF Investment Committee and endorsed by the NRREP Compliance Unit. The Handling Bank and the Prequalified Partner Banks are responsible for the financial management of CREF funds in accordance with approved systems and procedures

including internal and external auditing. The banks will comply with Nepal Rastra Bank (NRB) rules and regulations, and will be subject to regular supervision by NRB. The NRREP financial control mechanisms include systems and compliance audits carried out by the Compliance Unit, annual programme audits and external value for money audits. Furthermore, the CREF Investment Committee will through the Secretariat monitor the performance of the selected banks.

**Long-term Sustainability and Self-financing**

CREF will work as an endowment fund and will as such be allowed to earn revenue and retain surpluses. This will not only make the CREF self-financing, but also enhance long-term sustainability beyond the lifetime of the NRREP programme. This calls for the CREF Investment Committee eventually being institutionalised as a permanent committee.

**Key Risks and Assumptions**

The key risks are associated with the fragile political situation in the country, the possibilities of political interference and a business environment, which may not be attractive for new private sector investments. A risk is also that the Handling Bank goes bankrupt – this risk is, however, considered low given the stringent regulations and supervision by NRB. Furthermore, surplus funds may be invested in other banks through the Handling Bank, thereby spreading the possible risks further.

Key assumptions are that the Government will continue to support renewable energy technologies as well as private sector development. It is also assumed that CREF can operate as an endowment fund and retain earnings.

**Next Steps in the Establishment of CREF**

The CREF Financial Intermediation Mechanism was approved in principle by the AEPC Board chaired by the Minister, MSTE, on 25 February 2013 and by the NRREP Programme Steering Committee on 27 February chaired by the Secretary, MSTE. AEPC will now seek formal approval from MSTE and Ministry of Finance. At the same time development of operational systems and procedures will take place, with the aim of having the CREF mechanism operational from July 2013.

## 1. Introduction

The Central Renewable Energy Fund (CREF) will be established as the financial intermediation mechanism for the renewable energy sector under the National Rural and Renewable Energy Programme (NRREP). The was decided upon in principle by the AEPC (Alternative Energy Promotion Centre Board) Board chaired by the Minister, MSTE (Ministry of Science, Technology and Environment), on 25 February 2013 and by the NRREP Programme Steering Committee on 27 February chaired by the Secretary, MSTE. AEPC will now seek formal approval from MSTE and Ministry of Finance. At the same time development of operational systems and procedures will take place, with the aim of having the CREF mechanism operational from July 2013.

The CREF design process has been very consultative and robust. It has been driven by the CREF Interim Task Force established jointly by the Government and development partners with representation from Ministry of Finance, MSTE and AEPC as well as development partners committing funds to CREF. A CREF Working Group was established by the CREF Interim Task Force to undertake more detailed analytical work and develop proposals for the establishment of CREF<sup>1</sup>.

In reaching the decision to establish CREF as a financial intermediation mechanism a number of different options have been considered by the Government and Development Partners, including the options of establishing a development board, a public limited company or a financial institution. The options were assessed against the seven criteria - guiding design principles - established by the CREF Working Group and endorsed by AEPC and development partners. The guiding design principles are presented in Section 3.

The seven criteria suggest that the overall guiding principle is that subsidies for promotion of renewable energy technologies (RET) should gradually be phased out and replaced by credit facilities and that the management of such credit facilities should be the responsibility of the private sector.

Furthermore, the CREF Working Group was requested to examine and analyse the concept of a financial intermediation mechanism for CREF in more detail. In this connection a Concept was developed and circulated in December 2012. The development of the Concept Note was based on:

- Review of the Three Year Plan Approach Paper (2010/11 – 2012/13);
- Review of “Banks and Financial Institutions Act” Nepal Rastra Bank (2006);
- Review of ADB’s Financial Intermediation Lending Policy;
- Interviews of CEOs and management teams from five commercial banks<sup>2</sup> to solicit their views and comments on the financial intermediation mechanism;
- Review of similar financial intermediation mechanisms in Nepal and elsewhere; and
- A peer-review by an experienced development banker.

This paper documents the agreed CREF Financial Intermediation Mechanism based upon the Concept Note and incorporates findings and recommendations made by the Government and development partners. It will serve as the basis for formalising and establishing CREF accordingly.

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<sup>1</sup> The CREF Working Group consists of Torben Lang, Team Leader and Senior CREF Adviser, Anand R. Maskey, REF

<sup>2</sup> Everest Bank, Himalaya Bank, Nabil Bank, Standard Chartered Bank and Clean Energy Development Bank.

## 2. CREF Objective and Scope

The NRREP programme documentation states that the objective of CREF is as the core financial mechanism to be responsible for the effective delivery of subsidies and credits to the renewable energy sector. As such CREF will be established to cater for:

- The issuing of subsidies to qualified renewable energy technology installers and other authorised recipients of subsidy funds; and
- Facilitating the provision of credit facilities to households and communities that wish to acquire renewable energy technologies.

The funds committed to CREF are shown in the table below. The CREF Component Description envisages a 50/50 split of the budget between subsidies and credits. As mentioned below a guiding design principle for CREF is that subsidies should gradually be phased out and replaced by credit facilities.

CREF Budget Commitment	Currency	Amount (million)	Exchange Rate <sup>3</sup>	NPR (million)	USD (million)
Danida	DKK	65.0	15.03	977.0	11.4
Norway	NOK	60.0	15.02	903.0	10.5
DFID	UK £	5.0	129.71	650.0	7.6
KfW	EUR	2.2	112.09	247.0	2.9
SREP	USD	20.0	85.71	1,714.0	20.0
GoN	NPR	5,474.0		5,474.0	63.9
<b>Total</b>				<b>9,965.0</b>	<b>116.3</b>

Note: Figures may not add up due to rounding

## 3. Guiding Design Principles

Development partners and AEPC subscribe to a number of guiding design principles, which have been applied in order to determine the optimal institutional and legal framework for CREF.

1. Subsidies should in the long-term be phased out and replaced by credit facilities and the management of credit facilities will be the responsibility of the private sector;
2. As the core financial mechanism for the RET sector, CREF should be autonomous with its own mandate and well-defined management structures. As such CREF should be independent from AEPC, however working in close relationship and at the same institutional level as AEPC - a guiding principle is to have a clear demarcation and independency between the technical development and assessment of RET projects, and the financial management of subsidies and credit schemes;
3. In order to gradually achieve self-financing and long-term sustainability CREF should be allowed to place surplus funds in secure/low risk investments and thereby generate a source of income - applying the principles of an endowment fund;
4. Retained earnings/surpluses should be fully re-invested within CREF in order to allow it to expand and consolidate its financial position;
5. The legal and institutional foundation should be acceptable to the Government of Nepal as well as to all development partners for CREF managing grants as well as loan schemes e.g. from World Bank and ADB;
6. The autonomy of CREF should allow it sufficient freedom in its operations with the objective of widely promoting access to financial services for the RET sector, e.g. open and transparent selection of partner financial institutions for the retailing of REF credit schemes; and

<sup>3</sup> Nepal Rastra Bank 28 February 2013. NOK exchange rate according to rate applied by Royal Norwegian Embassy

7. The success of CREF will to a great extent hinge on the quality and competence of the management structure put in place for CREF as well as the management team and the staff. Hence, it is of critical importance to have established a specialised CREF Investment Committee with government and private sector representation, which will in a highly professional manner contribute to the advancement of CREF. Similarly the CREF should have a staff recruitment and remuneration policy that will attract highly qualified and committed personnel in competition with private sector financial institutions.

## 4. CREF Financial Intermediation Mechanism

### 4.1 Conceptual Framework

The concept of the proposed mechanism is based on the principle that the core functions of CREF – Subsidy Fund Management, Investment Management and Wholesale Lending – will be managed by a well-established and functioning private sector commercial bank (Class A<sup>4</sup> bank). The bank will be selected on a transparent and competitive basis as the Handling Bank for CREF. The Handling Bank will work under the oversight and strategic directions of a CREF Investment Committee, which will be reporting to the NRREP Programme Steering Committee. The Handling Bank will work in close collaboration with AEPC and its technical departments as well as AEPC’s representation in districts. Projects suitable for funding under the CREF scheme will be identified on a demand-basis by the end users with the technical support of AEPC. The project developers<sup>5</sup> will, as appropriate, apply to AEPC for subsidies and to a prequalified financial institution<sup>6</sup> for credit/loan facilities for the project supported by technical analysis and endorsement from AEPC. The prequalified financial institutions will appraise the loan request against its internal procedures and if approved approach the Handling Bank for re-financing of the loan on a case-by-case basis or using a replenishment system.

Subsidy funds will initially be applied to create awareness about renewable energy solutions and to stimulate demand. They will be managed in accordance with the Government’s Subsidy Policy and Delivery Mechanism. Subsidies will gradually be replaced by credit facilities for financing renewable energy projects. The Government and development partners will inject seed capital into the CREF wholesale lending mechanism for on lending through retail banks – the prequalified partner banks. The Handling Bank and the Prequalified Partner Banks will leverage the CREF funding with own funds and thereby expand the lending to the sector. Recycling of loans and revenue from investments of surplus funds should ultimately make the CREF funding mechanism sustainable and the long-term management should be the responsibility of the private sector. The CREF Investment Committee will continue to oversee the management of the funds, however, the membership composition may change once the Government and development partners have provided sufficient seed capital to create a critical mass of funding. The Nepal Rastra Bank will play a critical role in regulating and supervising the performance of all the participating financial institutions in accordance with established bank regulations and rules.

Like any other element of NRREP the Handling Bank and the participating banks will be subject to random system and compliance audits by the NRREP Compliance Unit.

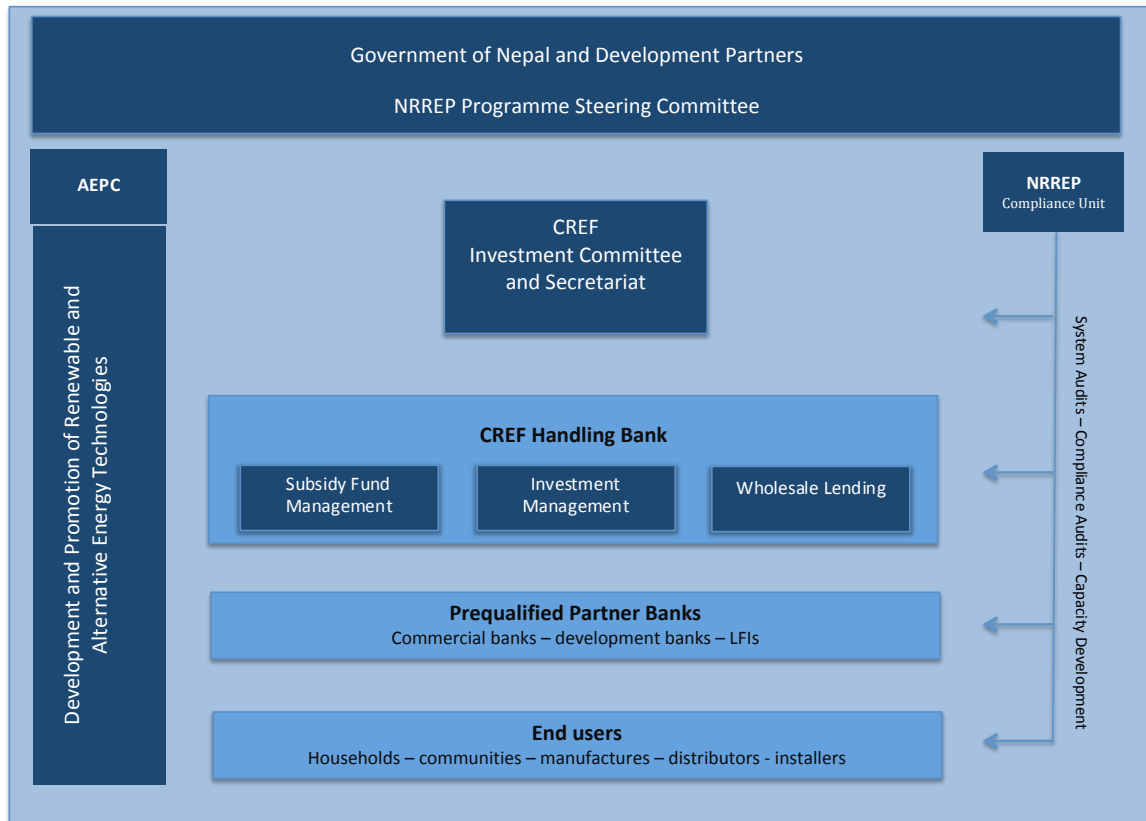
The role and functions of the different institutions engaged in the mechanism are briefly outlined in Section 5 and an overview of the mechanism is presented in the figure below.

<sup>4</sup> The option of also including Class “B” banks in the tender will be further explored with NRB

<sup>5</sup> Project developers may include households, communities, manufactures, distributors and installers

<sup>6</sup> Development bank, commercial bank, MFI/LFI, SACCO





## 4.2 Compliance with Government Policies and Regulations

The Government has stated in its Three Year Plan Approach Paper (2010/11 – 2012/13)<sup>7</sup> that it has the objective to increase the involvement of the private sector as a development partner of the government in the areas of investment, production, distribution, social development and employment generation. The Three-Year Plan is also emphasising the need to expand accessibility of banking services in all sectors of the economy as well as in rural areas. The CREF Financial Intermediation mechanism will support the Government in reaching its objectives in this respect as well as in the general promotion of renewable energy financing. CREF will engage private commercial banks for the advancement of financing for renewable energy technologies, especially in rural areas, and actively capacitate the banks to develop relevant products and services as well as expand their outreach.

The CREF Financial Intermediation mechanism furthermore complies with the “Banks and Financial Institutions Act, 2063 (2006)”. The Act states that Class “A” and “B” banks may “supply funds received from the Government of Nepal or other native or foreign agencies as credits for the promotion of projects, or managing such credits”. This clause allows the participating financial institutions to undertake wholesale and retail lending as envisaged in the NRREP Programme Document. Furthermore, the Act stipulates that the Class “A” banks may “act as an agent of the Rastra Bank on the conditions prescribed by the Rastra Bank, and carrying on governmental and other transactions on behalf of the Government of Nepal”. This clause allows the Handling Bank to undertake the subsidy fund management as well as the investment management on behalf of CREF.

<sup>7</sup> The Three-Year Plan is currently being revised. However, it is assumed that the main thrust of the policies and strategies will be maintained.

There is experience in Nepal with the establishment of financial intermediation mechanisms. An example is the establishment of the Power Development Fund (PDF) with the support of the World Bank and International Finance Corporation. The PDF was established to finance private sector hydropower development projects through a similar mechanism of financial intermediation. However, the PDF was not successful in attracting project proposals mainly due to high administrative costs and charges. An important lesson learned, which should not be replicated in the CREF mechanism.

Furthermore, the design builds on lessons learned from past experience with lending to the renewable energy sector through a similar mechanism with pre-qualified partner banks and LFIs e.g. the AEPC and ESAP supported Hydro-debt Fund, the Credit Financing of Solar-Home System and the Biogas Credit Scheme. The case studies for these three financing mechanisms are attached hereto as Annex V.

### **4.3 Compliance with Development Partners' Policies and Strategies**

The CREF Financial Intermediation mechanism has been assessed against policies and strategies of development partners and in particular against ADB's Financial Intermediation Lending Policy. Development partners are aligning and harmonising their development assistance in Nepal with policies and objectives of the Government. This is also the case in terms of support to the renewable energy sector, the private sector and the financial sector and as such the CREF mechanism is also complying with policies and strategies of the development partners. Furthermore, it is assumed that if the CREF mechanism complies with ADB's Financial Intermediation Lending Policy then the concept of using a financial intermediation mechanism would also be acceptable to other multilateral and bilateral development partners. This assumption was confirmed in the meeting on 10 January 2013 with the development partners committing funds to CREF.

ADB's Financial Intermediation loans aim to finance projects whose individual financing requirements are not large enough to warrant the direct supervision of ADB. Lending is provided through an Apex Financial Institution (handling bank) to second-tier financial institutions (partner financial institutions), who in turn on-lend such loan proceeds to the sub-borrowers (project developers). The Apex institution takes the risk on the second-tier intermediaries. Financial intermediation loans seek to help achieve a number of objectives: (i) furthering policy reforms in the financial and real sectors; (ii) financing real sector investments through market-based allocation mechanisms; (iii) strengthening the capacity, governance, and sustainability of participating financial intermediaries; and (iv) helping increase the outreach, efficiency, infrastructure, and stability of the financial system.

The ADB's Financial Intermediation Lending policy further suggests a number of eligibility criteria, which may also form part of the selection criteria for CREF financial institutions:

- Financial soundness as evidenced by adequate capital, asset quality, liquidity, and profitability;
- Adequate credit and risk management policies, operating systems, and procedures;
- Compliance with prudential regulations, including exposure limits;
- Acceptable corporate and financial governance and management practices including, among other things, transparent financial disclosure policies and practices;
- Sound business objectives and strategy and/or plan;
- Autonomy in lending and pricing decisions; and

- Adequate policies, systems, and procedures to assess and monitor the economic, social, and environmental impact of subprojects in accordance with parameters established by ADB for this purpose.

#### 4.4 Assessment of Key Features

The CREF Financial Intermediation mechanism offers the following key features, which were also discussed and agreed upon at the meeting between development partners and AEPC 10 January 2013:

1. The mechanism complies with policies, objectives and strategies of the Government as well as of the Development Partners;
2. It complies with the seven guiding design principles outlined in the section above;
3. It will be *efficient* in terms of utilisation of resources; *effective* in terms of achieving results; *lean* in terms of manpower and other resources; and it will be *flexible* in terms of new services, products and partners as it will buy into the existing structures of a well-functioning and established private sector commercial/development bank;
4. It offers significant prospects for long-term sustainability of the CREF funds as they will be leveraged by the Handling Bank and the Prequalified Partner Banks, loan recoveries will be recycled into new loans and surplus funds will be invested for revenue generation;
5. Fiduciary risk management will benefit from the internal control systems of the participating financial institutions notably the Handling Bank as well as the rigorous regulation and supervision of the banks conducted by Nepal Rastra Bank;
6. It will be fairly simple to establish and operationalize – basically it requires that the NRREP Programme Steering Committee establishes the CREF Investment Committee and Secretariat, which will tender out the services as Handling Bank and prequalifying Partner Banks;
7. The five banks interviewed confirmed that the fundamental principles of the concept were sound and manageable as well as an interest in potentially bidding for being either Handling Bank or Prequalified Partner Bank under this mechanism; and
8. The banks interviewed expressed a preference for bidding for the Handling Bank assignment as it was considered to have a triple bottom-line effect by contributing to the bank's earnings, corporate social responsibility (CRS) and green financing – the Handling Bank role was considered to be of high profile and with a significant positive impact on the image of the bank – as well as its earnings.

In addition to internal assessment of the CREF Financial Intermediation mechanism an external assessment was carried out through an independent peer-review by an experienced development banker.<sup>8</sup> The conclusion of the review is that the mechanism is feasible and appropriate for CREF. However, a number of issues are highlighted:

- The success of the mechanism greatly hinges on “getting it right first time” – the development of a robust basis for tendering and contracting the Handling Bank and Partner Banks in terms of operational and management guidelines, terms of reference and contract documents. The peer-review contains a list of documents and formats that should be considered in connection with tendering and contracting the Handling Bank and Partner Banks;

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<sup>8</sup> Vagn Rasmussen, Chief Development Banker, Development Associates, Copenhagen, Denmark. Mr. Rasmussen has previously been engaged by Danida as consultant for the preparation and establishment of the Rural Energy Fund, Nepal.

- None-performing Partner Banks may be excluded and replaced. However, this is much more difficult in terms of the Handling Bank. Hence, extraordinary care must be taking in selecting the Handling Bank and in managing the contract;
- Selection criteria should in addition to financial and economic criteria also consider: “confidence, continuity and quality”; and
- The mechanism will also be able to attract funds from the participating banks to leverage CREF funds and given the liquidity position of banks they would also be willing to borrow funds from CREF at an interest contributing to the sustainability of the mechanism.

The peer-review comments to the CREF Concept Note are attached hereto as Annex VI.

## **5. Functional Overview of Key Partner Institutions**

This section outlines the role and key functions of the institutions engaged in implementation of the CREF core functions – subsidy fund management and provision of credit facilities. It should be noted that the role and functions of the NRREP Programme Steering Committee, the NRREP Compliance Unit, AEPC and the Prequalified Partner Banks will basically be the same irrespective of the institutional and legal model opted for CREF.

### **5.1 NRREP Programme Steering Committee**

The NRREP Programme Steering Committee decides on the overall priorities of the programme in accordance with the programme document, joint financing agreements, and other legal documents. Where major deviations from the programme document are considered necessary, the steering committee takes the decisions. The committee cannot alter overall programme objectives, but may recommend changes in immediate objectives. The mandate of the Programme Steering Committee includes approval of major planning documents, progress reports, work plans, budgets, audit reports, and decisions regarding major implementation issues. The committee also agrees on the timing and terms of reference for the joint programme reviews and will ensure follow-up of the recommendations made.

To ensure a high degree of efficiency in the decision making mechanism there will be six members of the Programme Steering Committee. The current members are the Secretary of Ministry of Science, Technology and Environment (Chairperson), a representative from the Ministry of Finance, the Ministry of Federal Affairs and Local Development, the Ministry of Energy, a representative from Development Partners as well as the Executive Director of AEPC (Member Secretary, Ex officio). In order to strengthen the oversight of CREF and its engagement with the financial sector it is recommended to expand the membership with a representative from Nepal Rastra Bank, who is also proposed as the Chairperson of the CREF Investment Committee. See also Section 5.2 below.

### **5.2 Alternative Energy Promotion Centre - AEPC**

The mandate of AEPC is to develop and promote renewable/alternative energy technologies in Nepal and its mission is to make renewable energy mainstream resource through increased access, knowledge and adaptability contributing for the improved living conditions of people in Nepal. The AEPC is the executing agency for the NRREP programme and the technical support services are being implemented through four technical components: i) community electrification and improved watermills; ii) solar; iii) biogas; and iv) solid biomass. A number of crosscutting components are supporting the technical components: i) institutional support; ii) productive end use; iii) carbon; iv) GESI; and v) monitoring.

The implementation of programme activities is done in a combination of APEC core managers and staff together with programme employed advisers. Overall management, planning and monitoring of programme activities are conducted centrally by AEPC. Most of the AEPC field based activities are conducted through Regional Service Centres (RSC), District Energy and Environmental Units (DEEU), private companies and consultants. RSCs are NGOs contracted by AEPC as service providers to cover all potential areas/districts of the country for the activities relating to field implementation. They work as a bridge/facilitator among various stakeholders such as private sector, field level service providers, project developers, communities, end users and AEPC. DEEUs are established under the District Development Committees with the assistance of AEPC for the coordination and promotion of renewable energy technologies at district level.

The RSCs and the DEEUs will also play an active role in preparing user groups/developers for accessing financial services from one or more of the Prequalified Partner Banks. The tasks will include informing them of all the mechanisms that have been established for the easy access to credit, orientation on risk mitigation, bookkeeping, tariff collection, repair/maintenance, fulfilling bank requirement, and different ways of repaying loans. They may also encourage developers to access loans for completing the project on time. AEPC and the RSCs and DEUs will be the focal point on the ground for the Prequalified Partner Banks – supporting demand-side management.

The strategic management link between AEPC and CREF is ensured through the Executive Director (ED) of AEPC being a member of the CREF Investment Committee and also Secretary to the NRREP Programme Steering Committee. At the operational level the link between AEPC, CREF and renewable energy project developers will be ensured through the establishment of an advisory unit attached to the office of the ED. The unit will be headed by an NRREP Senior Programme Adviser – National Project Facilitation Adviser. The job description for the National Project Facilitation Adviser is presented in Annex II. The unit will be responsible for *inter alia*:

- Be the focal point within AEPC for coordination and liaison with CREF Secretariat - subsidy fund management and credit facilities;
- Participate in management meetings of the CREF Secretariat - linking and promoting the agenda of AEPC;
- Participate in AEPC management meetings - reporting on subsidy fund management and credit facilities issues;
- Liaise with the CREF Secretariat in terms of the status of subsidy and loan applications;
- Participate in addressing subsidy and loan application disputes with project developers – representing the AEPC in such cases;
- Receive and analyse reports from the CREF Secretariat;
- Conduct orientation seminars jointly with CREF Secretariat for AEPC, RSC and DEEU staff on subsidy and credit financing of renewable energy projects;
- Participate with AEPC technical departments in promotion of renewable technologies - promoting access to subsidies and credit facilities;
- Support RSCs and REEUs in promoting investments in renewable energy projects;
- Assist project developers - jointly with AEPC technical staff - in developing bankable projects and in negotiations with CREF Prequalified Partner Banks - stimulate demands for renewable energy projects;
- Manage and coordinate the technical verification process of subsidy applications within AEPC ; and

- Participate in reviews of the Credit and Subsidy Policy and Delivery Mechanism.

The above tasks of the Adviser will facilitate that the institutional linkages between AEPC and CREF are well-defined and robust. It will, furthermore, strengthen the link between project developers and the financial institutions through its support to RCSs and DEEUs.

### **5.3 NRREP Compliance Unit**

The NRREP Compliance unit is responsible for quality assure of all financial management, planning and control systems of NRREP including CREF and to ensure compliance with the approved systems. The Compliance Unit will conduct random quality assurance/compliance audits in the CREF Handling Bank and in the Prequalified Partner Banks. Audits may also include site visits to verify technical aspects of projects receiving subsidies and/or credit facilities under the CREF scheme.

The Compliance Unit will, based upon their findings, advise the relevant CREF financial institutions as well as AEPC on how systems and procedures can be improved. The Compliance Unit will also provide a report stating overall findings of their assessments and quality assurance audits to the NRREP Programme Steering Committee through the lead development partner as well as to the CREF Investment Committee. The Compliance Unit will work in close consultation with the Secretariat of the CREF Investment Committee. It is the responsibility of the CREF Investment Committee to follow-up on findings and recommendations made by the Compliance Unit.

### **5.4 CREF Investment Committee and Secretariat**

The NRREP Programme Steering Committee will, given the specific focus of CREF on financial sector activities, establish a specialised subcommittee for CREF - the CREF Investment Committee with the overall responsibility of strategic management, planning and monitoring of CREF's operations and performance. The Committee will establish a small Secretariat to support it at the operational level. The ToR for the CREF Investment Committee and Secretariat are attached hereto as Annex I.

#### **The CREF Investment Committee**

The CREF Investment Committee is established by the NRREP Programme Steering Committee and is as such reporting to this committee. The core functions of the CREF Investment Committee will be:

- Establish the CREF institutional framework including developing terms of reference and selection criteria for the CREF Handling Bank, managing the tender process, contracting the Handling Bank and managing the contract. Overseeing the prequalification of Partner Banks;
- Establish and review on an annual basis the CREF strategic financial management framework including developing the investment profile; criteria for wholesale lending; developing monitoring system and procedures;
- Monitor the performance of the Handling Bank and the CREF portfolio; receive and commenting on plans, projections and reports from the Handling Bank; receive reports from the NRREP Compliance Unit and follow-up recommendations made; report to the NRREP Programme Steering Committee;
- Approve release of funds to the Handling Bank against financial projections and plans prepared by the Handling Bank and analysed by the Secretariat;
- Approve of capacity development programmes for the Handling Bank and Prequalified Partner Banks as developed by the Secretariat;
- Promote and create awareness about the CREF supported subsidy and credit facilities; and

- Establish and manage the Secretariat.

Members<sup>9</sup> of the CREF Investment Committee will include:

- Nepal Rastra Bank;
- Ministry of Finance;
- Ministry of Science, Technology and Environment;
- AEPC, Executive Director;
- Representative from the financial sector (former chairperson or CEO from one of the major commercial or development banks) be nominated by the Nepal Bankers Association;
- Representative from the private sector nominated by the Development Partners committing funds to CREF; and
- A representative from the group of Development Partners committing funds to CREF.

The proposed membership, the motivation for membership as well as the suggested profile of the committee members are presented in the ToR for the CREF Investment Committee in Annex I.

Given the level of engagement of commercial banks in the CREF mechanism and the responsibility of Nepal Rastra Bank in regulating and supervising the banks, it is proposed that Nepal Rastra Bank chair the committee. Management will be by consensus and cases that cannot be resolved will be referred to the NRREP Steering Committee. The Head of the Secretariat will also serve as secretary to the CREF Investment Committee – in consultation with the Chair call meetings, compile and circulate documents, take minutes etc. - and the CEO of the Handling Bank may be invited to attend the meetings as Ex-officio. The committee may also invite other resource persons as observers.

The Chair will report to the NRREP Programme Steering Committee and will ensure that CREF supported interventions will be fully aligned to the objectives and thrust of the NRREP programme. The participation of the ED of AEPC will ensure that the close collaboration between CREF and AEPC is institutionalised. Representatives from the private sector will facilitate that CREF will be responsive to the needs and challenges of the private sector.

### **The Secretariat**

The CREF Investment Committee will establish a lean secretariat as its operational arm, which will provide day-to-day support for the implementation of its mandate and tasks. The NRREP programme will initially fund the Secretariat out of funds earmarked for the CREF Component. However, the Secretariat will eventually be financed out of revenue generated by CREF investments and interest earnings. The Secretariat will play a key role in developing and implementing capacity building programmes for the financial institutions participating in implementation of CREF programme activities. The Secretariat will on an annual basis assess the need for capacity development and design programme responding to the needs in close collaboration with the respective institutions for the approval of the CREF Investment Committee. Capacity building activities will be outsourced to prequalified service providers in agreement with the individual banks. The Secretariat will also support the financial institutions with monitoring the performance of the CREF portfolio including on-site inspections.

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<sup>9</sup> Members from GoN should be at least 1st class level – Joint Secretary

Together with the participating financial institutions, the Secretariat will support supply-side management for the development and financing of renewable energy projects, while AEPC and its outreach structures is supporting demand-side management.

The Secretariat will, furthermore, support with analysis of reports and information from the Handling Bank and Prequalified Partner Banks and in drafting reports to the CREF Investment Committee and to the NRREP Programme Steering Committee. It will play an active role in monitoring the performance of the participating institutions. Disputes and complains relating to the subsidy funds, which cannot be resolved internally between the Handling Bank and AEPC, will be referred to the CREF Investment Committee through the Secretariat. The Secretariat will establish close working relations with the NRREP Compliance Unit and facilitate its work.

The Secretariat will be housed by the Handling Bank in order to ensure close and efficient interaction on a daily basis. The Handling Bank will also accommodate meetings of the CREF Investment Committee. It is envisaged that the Secretariat will have a professional staff of two – one specialised in management and monitoring and the other specialised in capacity development of financial institutions. The Secretariat may employ support staff as approved by the CREF Investment Committee. The Secretariat will initially be paid for by the NRREP programme, but should in the long-term be financed out of CREF retained earnings.

**The Management and Monitoring Specialist – Head of Secretariat** will be overall responsible for managing the relationship with the Handling Bank and other participating financial institutions and for monitoring their performance in accordance with signed agreements. He/she will develop and implement a monitoring framework for the performance of all CREF related activities including efficiency and effectiveness of funding instruments as well as impact assessment at end-users level. He/she will review the subsidy fund management mechanism, the wholesale lending strategy, the retail lending, the investment strategy and on a regular basis monitors the implementation against agreed performance indicators. Monitoring work may be carried out directly by the Specialist or in collaboration with service providers contracted on a transparent and competitive basis. An initial task will be to do a mapping and pre-qualification of relevant service providers. The Specialist will work closely with the Capacity Development Specialist in defining and implementing capacity development programmes. A key task is also the development and implementation of the CREF Communication Strategy, which will aim at promoting and creating awareness about the facilities available through CREF and the partner financial institutions with the support of AEPC. He/she will be responsible for the management of the Secretariat and will report to the CREF Investment Committee. The job description for the Management and Monitoring Specialist is attached as Annex III

**The Capacity Development of Financial Institutions Specialist** will be overall responsible for capacity development needs assessment of the participating financial institutions, and development and implementation of capacity building programmes. Capacity assessment will be done once a new financial institution enters the programme and regularly on an annual basis. The assessment and implementation will be done in close collaboration with the HR and Training Departments of the participating financial institutions. Capacity development programmes will include product development; loan appraisal and supervision systems and procedures; management and staff training. Capacity development programmes will be implemented directly by the specialist or in collaboration with service providers contracted on a transparent and competitive basis. An initial task will be to do a mapping and pre-qualification of relevant service providers. He/she will support participating financial institutions in the promotion of financial instruments available under CREF financing agreements and



in this connection also work closely with AEPC technical units as well as Regional Service Centres, District Energy and Environment Units and private sector entrepreneurs. The Capacity Development Specialist will report to the Portfolio Management and Monitoring Specialist. The job description of the Capacity Building Specialist is included as Annex IV

## 5.5 CREF Handling Bank

The CREF Handling Bank will be contracted by and reporting to the CREF Investment Committee as the apex financial institution. It will be selected on a transparent and competitive basis. The Handling Bank will have three core functions for the CREF portfolio: i) Wholesale lending to prequalified partner banks; ii) Subsidy Fund Management; and iii) Investment Management. The contract with the Handling Bank will be a performance-based management contract in order to ensure that subsidy applications are processed within the agreed time limits and that credit funds are actively engaged in the financing of renewable energy projects.

The **Wholesale Lending** core function will make credit facilities available to finance renewable energy technology projects. Projects will be developed on a demand-driven basis with the support of the technical departments of AEPC. Bankable projects will be presented to one or several of the prequalified partner banks, which will appraise the project against its lending policies and criteria. The prequalified partner banks can apply to the CREF Handling Bank for refinancing of the loan against criteria agreed between the Handling Bank and the CREF Investment Committee. The Handling Bank will appraise and approve loans against criteria agreed upon with the CREF Investment Committee. However, the bank will utilise its infrastructure, systems and procedures as well as manpower for the loan appraisal and supervision. The Handling Bank will take the risk on lending to the Partner Banks, which in turn take the risk on lending to the renewable energy projects.

The **Subsidy Fund Management** will be done in compliance with the Government's subsidy policy and delivery mechanism. The AEPC will be responsible for receiving subsidy applications – the point of entry – and for assessing and approving the applications from a technical perspective. Once they are approved by AEPC they will be forwarded in weekly batches to the Handling Bank, which will be responsible for the financial assessment of applications and releasing subsidy funds. A copy of the subsidy recommendation report will be forwarded separately by AEPC to the Secretariat for monitoring purposes. Subsidies can be stand-alone subsidies or part of a loan package for the financing of a renewable energy project. The REF subsidy mechanism model – application and approval process - is currently being assessed by a “Value for Money Audit” commissioned by the Embassy of Denmark. This audit will feed into a more detailed assessment study by Ernst & Young, commissioned by DFID, which will make recommendations for the future management of the subsidy application and approval process. These recommendations will be adopted by the Handling Bank and form the basis for how best to establish the internal processes and procedures for subsidy fund management.

The principle behind the **Investment Management** core function is that the CREF funds should not be left as idle funds. Funds are either used for subsidy purposes promoting the renewable energy technologies or are lend out as credit facilities. CREF funds not dispersed by the Handling Bank as well as loan recoveries should be invested in order to generate new funds and ultimately make the CREF scheme self-financing and sustainable. The CREF Investment Committee will develop an investment profile, which will guide the Handling Bank in investing surplus funds. Interest earnings will be used to finance the CREF operations e.g. CREF Investment Committee, Secretariat, possible

fees for subsidy fund management and contribute to the sustainability of the CREF institutional framework.

## 5.6 Prequalified Partner Banks

The CREF Investment Committee and the Handling Bank will joint prequalify a number – say five to 10 – financial institutions, which will serve as the retailers of the CREF credit facilities – second-tier financial institutions. The prequalification will be done against detailed terms of reference for the assignment and selection will be based on well-defined criteria and done in a transparent process. The list of prequalified partner banks will be made widely available to all interest groups including business associations, district and village development committees, community groups, potential developers and the AEPC management and staff.

Prequalified Partner Banks will be encouraged to form strategic alliances with Local Financial Institutions (LFI) in order to deepen their outreach to rural and remote areas of Nepal.

Once a bankable project has been identified, formulated and assessed by the project developers with the assistance of the AEPC technical departments or complimentary services providers<sup>10</sup> it will be presented to one or more of the prequalified partner banks for financing. The bank will appraise the project against its internal lending policies and criteria. When the loan has been approved by the prequalified partner bank it can apply to the CREF Handling Bank for having the loan refinanced using the CREF wholesale lending window – banks may also agree with the Handling Bank to refinance loans on a replenishment basis. The prequalified partner bank carries the risk vis-à-vis the end user – the project developers – and the Handling Bank carries the risk vis-à-vis the prequalified partner bank. The option of introducing insurances schemes for the financing of renewable energy projects may be explored by the Secretariat once established.

The prequalified partner banks will work closely with the AEPC technical departments, Regional Service Centres, District Energy and Environmental Units and other complimentary service providers in identifying and assessing project opportunities as well as during the implementation of the project. Project identification will in principle be demand-driven, however, the banks and AEPC may actively stimulate such demand. The partner banks will as a basis for their loan appraisal use technical documentation from AEPC or the complimentary service provider such as feasibility studies. However, the banks may also use internal or external expertise to validate the project documentation and to carry out independent analysis of feasibility of the projects.

## 6. Fund Management

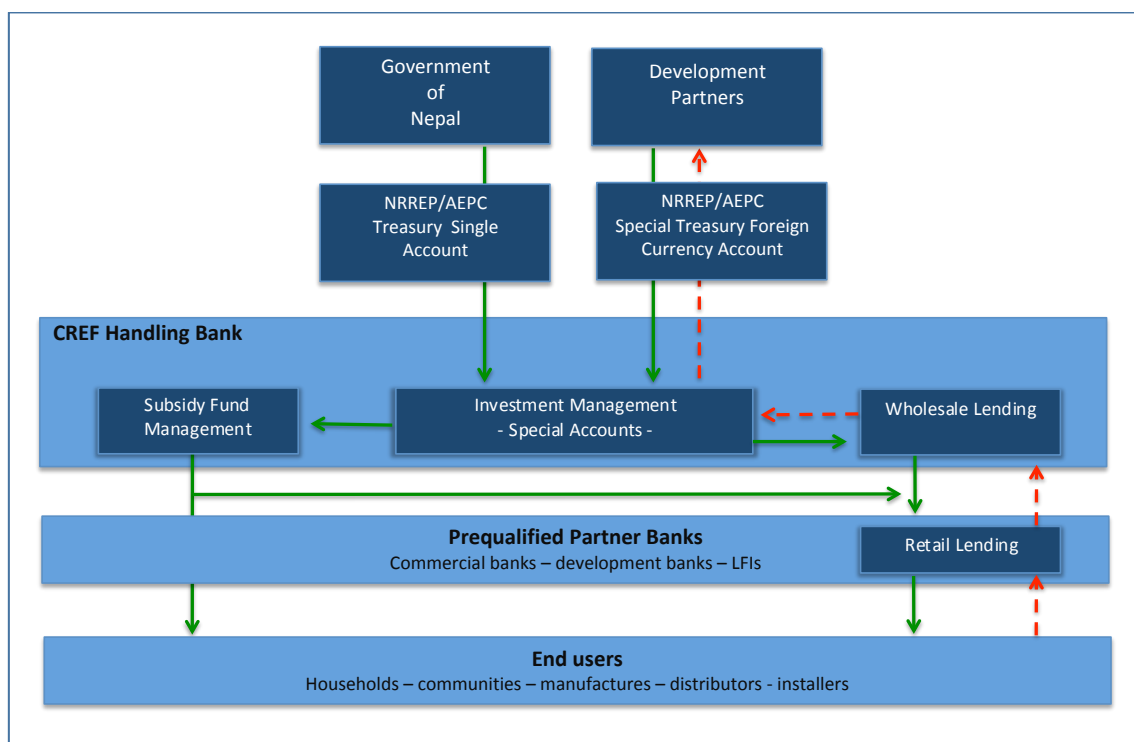
### 6.1 Flow of Funds

Flow of funds will be in accordance with the design in the NRREP Programme Document and the CREF Component Description. Funds from the Government – grant subsidies – will be transferred to the Handling Bank. Funds from development partners – grants and loans to the Government - will be disbursed to the Handling Bank through the NRREP/AEPC Special Treasury Foreign Account. Loans from development partners will be repaid by the Government through loan recoveries by the Handling Bank, which are transferred to the NRREP/AEPC Special Treasury Foreign Account.

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<sup>10</sup> Complimentary services providers are consulting engineers, business service providers and other private sector companies, which are required to coordinate their activities with the technical departments of AEPC

Funds will be kept by the Handling Bank in special earmarked investment accounts – revenue-earning accounts - until disbursed as subsidies or loans. Interest earnings will be used to finance the CREF operations e.g. CREF Investment Committee, Secretariat, possible fees for subsidy fund management and contribute to the sustainability of the CREF concept. Subsidies will be disbursed in accordance with the Government’s subsidy policy and delivery mechanism and against subsidy applications verified by AEPC. Subsidies will either be stand-alone subsidies or part of a loan package for a renewable energy project. Loan funds will be disbursed against loan agreements with the Prequalified Partner Banks in accordance with criteria set by the CREF Investment Committee. Loan recoveries will be paid into the special accounts under Investment Management either for repayment to the respective development partner through Government or to be relend to finance new renewable energy projects. The Handling Bank as well as the Prequalified Partner Banks are expected to leverage the CREF funds with own funds for the lending to renewable energy projects. All loans channelled through the Handling Bank will be in Nepalese Rupees.



## 6.2 Fiduciary Risk Management

CREF funds will be channelled for financing of renewable energy projects through private commercial banks (Class “A”)<sup>11</sup> – the Handling Bank and Prequalified Partner Banks. Funds will be managed in accordance with established systems and procedures of the participating financial institutions, which have been selected against carefully designed criteria. Lending risks will be the responsibility of the banks e.g. the Handling Bank takes the risk on the Prequalified Partner Bank, which in turn takes the risk on the project developer. Furthermore, the banks will be subject to external as well as internal auditing and supervision including:

- Compliance with NRB banking rules and regulations;
- Supervision by NRB;
- Banks internal and annual audits;

<sup>11</sup> NRB will be further consulted about the option of including Class “B” banks as Prequalified Partner Banks

- NRREP compliance audits;
- NRREP annual audits;
- NRREP value for money audits; and
- Performance monitoring by CREF Investment Committee and Secretariat.

## 7. Key Risks and Assumptions

### 7.1 Risks

Risks	Probability	Impact	Mitigation
1. The political situation continue to be fragile and government structures of an interim nature at national as well as at local levels	High	Medium	Maintain a sound balance of private sector and public sector interventions.
2. Political interference	High	High	Funding of CREF activities will be subject to approval of annual plans and follow transparent and accountable procedures. The strategic management and oversight of CREF will be done by the CREF Investment Committee, which has a sound balance of public and private membership.
3. Bankruptcy of the Handling Bank	Low	High	The Handling Bank will be selected against carefully designed eligibility criteria and it will furthermore be subject to regular supervision by the NRB as well as by the NRREP Compliance Unit and the CREF Investment Committee
3. A continued high level of corruption will discourage private sector investments in renewable energy technologies including project development, manufacturing, distribution, installation	Medium	Medium	The NRREP Compliance Unit will frequently undertake systems and compliance audits of all participating partners. Promotion of corporate social responsibility and good governance in all CREF partner institutions.
4. Low private sector investments due to uncertainties and unpredictable private sector policies and regulations	Medium	Medium	Participating financial institutions will be encouraged and supported in policy analysis and monitoring especially of policies relating to financial and private sector development. They will also be able to engage in policy dialogue through the CREF Investment Committee and the NRREP Steering Committee, which include representation from MoF and NRB.

## 7.2 Assumptions

The CREF Financial Intermediation mechanism is based upon a number of critical assumptions:

- The Government of Nepal will continue to promote renewable energy technologies including targeting the poor and marginalised groups of the society;
- The new Three-Year Plan will maintain the objective to increase the involvement of the private sector as a development partner of the Government in the areas of investment, production, distribution, social development and employment generation. The new Three-Year Plan will also maintain the emphasis on the need to expand accessibility of banking services in all sectors of the economy as well as in rural areas;
- CREF will be able to generate its own source of revenue from interest earnings and such funds will be fully retained in CREF for the financing of the institutional framework and contribute to its sustainability; and
- Subsidies will in the long-term be phased out and replaced by credit facilities and the management of credit facilities will be the responsibility of the private sector.

## 8. Interim Arrangements

The Joint Financing Arrangement between the Government and Development Partners for the NRREP stipulates that until agreed modality and structure for CREF is approved and functional, the NRREP contribution (funds) for CREF will be managed based on the existing Rural Energy Fund (REF) mechanisms for the subsidies and a system for credit facilities will be added, in agreement with the Government and bilateral and multilateral development partners. In this connection current REF staff will be extended until CREF is established, which is expected to be accomplished by July 2013. It has, furthermore, been agreed that AEPC will engage a National Project Facilitation Adviser on a fix-term contract (3-6 months) to support the ED in the interim period. The main task of the National Project Facilitation Adviser would be to assist in and advice on formalising and establishing the CREF Financial Intermediation mechanism including:

- Advise the AEPC management on institutional and legal arrangement for CREF;
- Participate in meetings of the CREF Task Force and serve as its secretary;
- Participate in the work of the CREF Senior Adviser and Working Group;
- Participate in the establishment of the CREF Investment Committee and Secretariat;
- Support in the recruitment of staff for the Secretariat;
- Contribute to the development of operational guidelines for the Secretariat;
- Contribute to the documentation for tendering and contracting the Handling Bank (ToR, management and operational guidelines, selection criteria);
- Contribute to the documentation for tendering and contracting the Prequalified Partner Banks (ToR, management and operational guidelines, selection criteria); and
- Manage and coordinate the technical verification of REF subsidy applications.

The fix-term position will once CREF is established be converted into an NRREP Senior Programme Adviser position at AEPC – National Project Facilitation Adviser. The Adviser will advise the Executive Director in matters relating to promotion of subsidy and credit financing of renewable energy projects and be responsible for the efficient and effective operational linkage between AEPC – CREF and renewable energy project developers (see also Section 5.2.)

## 9. Process Action Plan

The concept of the CREF Financial Intermediation mechanism has been agreed to by the development partners and the AEPC. In order to formalise and establish CREF accordingly the following Process Action Plan is proposed. The plan is largely based on agreements reached at the joint meeting on 10 January 2013.

	Tasks	Timing	Responsibility
1.	NRREP Steering Committee acknowledge the approval by AEPC Board	27 February	NRREP Steering Committee
2.	The CREF Financial Intermediation mechanism will be included in the Credit and Subsidy Delivery Mechanism – currently under revision – as the agreed modality for credit delivery and subsidy fund management	March	ED
3.	Final Draft CREF Financial Intermediation Mechanism	8 March	CREF Adviser
4.	Recruitment of AEPC National Project Facilitation Adviser – initially as short-term adviser	March	ED/EoD
5.	Final approval by Government of Nepal	March	ED
6.	Establish the CREF Investment Committee and Secretariat	March	NRREP Steering Committee
7.	Recruit staff for the Secretariat	March	CREF Investment Committee
8.	Develop detailed documentation for the participating financial institutions – tender documents, ToR, operational and management guidelines for subsidy management, credit operations and investment management	March	Consultant
9.	Develop operational guidelines for Secretariat	March	Consultant
10.	Tender and contract the Handling Bank	Apr/May	CREF Investment Committee
11.	Tender and contract the Partner Banks	May/June	CREF Investment Committee
12.	CREF Launch	July	CREF Investment Committee

The development of detailed documentation for the CREF financial intermediation mechanism will receive technical support from DFID, which has contracted Ernst & young, India, for this assignment. The documentation to be develop has been identified in the peer review of the CREF mechanism and may include as appropriate:

- Draft Operational Manual for the Secretariat’s activities and procedures
- Tender materials for the Handling Bank, incl. detailed ToR.  
Envisaged Flow of Funds; Wholesale Lending Strategy and Criteria, including Risk Sharing Conditions; Retail Lending Strategy and Criteria, including Risk Sharing Conditions; Subsidy Fund Management; and Investment Arrangements, Interest Policy, Investment Policy and Strategy for CREF Credit Funds.  
Eligibility Criteria for Selection of Handling Bank, incl. Bidding Procedures, Scoring Matrix and Evaluation Procedures
- Subsidy Funds Management Draft Agreement with Handling Bank

- Credit Funds Management and Investment Draft Agreement with Handling Bank
- Wholesale Credit Draft Agreement with Handling Bank
- Draft Contract with Handling Bank
- Standard MoU between Handling Bank and Donors

And – concerning PPBs (prequalified partner banks):

- Eligibility Criteria for PPBs
- Matrix for Evaluation of PPBs
- Format for Invitation to PPBs
- Notification of Selection of PPBs
- Subsidiary Re-Financing Draft Agreements between Handling Bank and PPBs
- Draft Contract with PPBs

And – depending on decisions concerning detailed implementation conditions and procedures:

- Formats for Notification of PPBs signatory authorities
- Formats for Annual PPBs Budgets for Re-Financing Requests, individual and consolidated
- Formats for Re-Financing Requests, individual and consolidated
- Formats for Repayment Schedules, individual and consolidated
- Formats for Overall Re-Financing Budgets, based on PPBs Budgets and Repayment Schedules
- Formats for Notification of Transfers to PPBs
- Formats for Confirmation of Disbursements
- Formats for Notification of Repayments
- Formats for Periodic Reports of Outstanding Balances per PPBs, individual and consolidated
- Monitoring Plans
- Formats for Minutes of Monitoring Visits
- Formats for Registration of Documents for PPBs files

## Annex I – ToR CREF Investment Committee and Secretariat

Draft 07.03.13

### 1. Background

The NRREP Programme Steering Committee is the highest decision-making mechanism concerning overall priorities of the programme in accordance with the programme document, government programme agreement and other legal documents. The Steering Committee reports to the Government of Nepal and the Development Partners through the lead development partner (Embassy of Denmark).

The NRREP Programme Steering Committee is overall responsible for the implementation of all programme components including CREF. Given the specific focus of CREF on financial sector activities, it will establish a specialised subcommittee – the CREF Investment Committee. The CREF Investment Committee established under and reporting to the NRREP Programme Steering Committee and will be delegated the responsibility for strategic management and oversight of the CREF activities as per Bilateral and Joint Financing Agreements of the Government and Development Partners.

### 2. Mandate and Scope

The role of the CREF Investment Committee is to provide overall oversight of and guidance on the priorities of the NRREP programme in respect of the CREF's core functions: i) subsidy fund management; ii) promotion of credit services to the renewable energy sector through provision of wholesale lending, capacity development of participating financial institutions and monitoring the efficiency and effectiveness of the financial schemes; and iii) investment management. The Secretariat will serve as the operational arm of the CREF Investment Committee and will provide day-to-day support for the implementation of its mandate and tasks.

### 3. Composition

Members<sup>12</sup> of the CREF Investment Committee will include:

- Nepal Rastra Bank;
- Ministry of Finance;
- Ministry of Science, Technology and Environment;
- AEPC, Executive Director;
- Representative from the financial sector (former chairperson or CEO from one of the major commercial or development banks) be nominated by the Nepal Bankers Association;
- Representative from the private sector nominated by the Development Partners committing funds to CREF; and
- A representative from the group of Development Partners committing funds to CREF.

The proposed membership, the motivation for membership as well as the suggested profile of the committee members are presented in the matrix overleaf.

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<sup>12</sup> Members from GoN should be at least 1st class level – Joint Secretary



Proposed Member	Motivation	Suggested Profile
Nepal Rastra Bank (proposed as Chair)	The CREF financial intermediation mechanism will be implemented through commercial banks and funds will be invested in these banks. NRB has the mandate to regulate, monitor and supervise the financial sector and as such will contribute to the efficiency of the CREF mechanism as well to fiduciary risk management.	The Executive Director or his/her designate, Bank & Financial Institutions Regulations Department. This department has the mandate to regulate, monitor and supervise the commercial and development banks engaged in the CREF mechanism.
Ministry of Finance	MoF is responsible for the Treasury function of GoN and as such is also responsible for funds received from development partners for CREF. All funds to CREF will be channelled through MoF.	Joint Secretary, Financial Sector Management Division. The division is responsible to develop and expand the banking and financial sector including policy development, promote outreach, undertake reach and studies.
Ministry of Science, Technology and Environment	MSTE is the parent ministry of AEPC and is the executing agency for the NRREP. It is overall responsible for promotion and development of the renewable energy sector including the policy framework.	Joint Secretary responsible for policy and planning for the renewable energy sector. The Joint Secretary will add value to the public-private dialogue on the planning and policy framework for the sector.
Alternative Energy Promotion Centre	AEPC has the mandate to develop and promote renewable energy in Nepal. Through its technical components and outreach network it is promoting and developing projects, which may receive funding from CREF in the form as subsidy and/or credit through the participating banks.	The Executive Director will be nominated by MSTE to represent AEPC on the committee in his capacity as head of AEPC, NRREP Programme Director and Secretary/Ex-officio member of the NRREP Programme Steering Committee.
Financial Sector Representative	The CREF mechanism will be implemented through commercial banks and the success hinges greatly on their performance. Hence, a financial sector representative will add value in solving specific issues, engage in the policy dialogue and in advancing the mechanism.	The Nepal Bankers Association will nominate a prominent business leader with past experience as CEO or Chair of one of the major commercial or development banks. The representative should not hold a current executive position in the banking sector in order to avoid possible conflict of interest.
Private Sector Representative	The private sector is a key partner and beneficiary in development of renewable energy projects. The private sector should be represented to present and resolve issues affecting the efficient performance of private sector stakeholders at operational as well as at policy level.	A prominent business leader from the private sector will be nominated by the development partners. The representative should be able to add value to the public-private dialogue on renewable energy sector development and to ensure the CREF mechanism remains responsive to the needs of the private stakeholders. He or she should not be directly or indirectly engaged in the implementation of projects financed through CREF.
Representative of Development Partners Committing Funds to CREF	The Development Partners are contributing to the CREF mechanism with financial and technical support. They should be presented to engage in the policy dialogue, to advance their agenda and to explore options for providing further support to CREF.	The Development Partners committing funds to CREF will jointly select a representative to sit on the CREF Investment Committee.

Given the level of engagement of commercial banks in the CREF mechanism and the responsibility of Nepal Rastra Bank in regulating and supervising the banks, it is proposed that Nepal Rastra Bank chair the committee. Management will be by consensus and cases that cannot be resolved will be referred to the NRREP Programme Steering Committee.

The Head of the Secretariat will also serve as secretary to the CREF Investment Committee– in consultation with the Chair call meetings, compile and circulate documents, take minutes etc - and the CEO of the Handling Bank may be invited to attend the meetings as Ex-officio. The committee may also invite other resource persons as observers.

The Chair will report to the NRREP Programme Steering Committee and will ensure that CREF supported interventions will be fully aligned to the objectives and thrust of the NRREP programme. The participation of the ED of AEPC will ensure that the close collaboration between CREF and AEPC is institutionalised. Representatives from the private sector will facilitate that CREF will be responsive to the needs and challenges of the private sector.

#### **4. Core Functions**

- Establish the CREF institutional framework including developing terms of reference and selection criteria for the CREF Handling Bank, managing the tender process, contracting the Handling Bank and managing the contract. Overseeing the prequalification of Partner Banks;
- Establish and review on an annual basis the CREF strategic financial management framework including developing the investment profile; criteria for wholesale lending; developing monitoring system and procedures;
- Monitor the performance of the Handling Bank and the CREF portfolio; receive and commenting on plans, projections and reports from the Handling Bank; receive reports from the NRREP Compliance Unit and follow-up recommendations made; report to the NRREP Programme Steering Committee;
- Approve release of funds to the Handling Bank against financial projections and plans prepared by the Handling Bank and analysed by the Secretariat;
- Approve capacity development programmes for the Handling Bank and Prequalified Partner Banks as developed by the Secretariat;
- Advice GoN/AEPC on subsidy policy issues especially in relation to optimising the subsidy/credit mix;
- Promote and create awareness about the CREF supported subsidy and credit facilities; and
- Establish and manage the Secretariat.

#### **5. Working Procedures**

- The CREF Investment Committee will meet at least on a quarterly basis. Meetings will be coordinated with the meetings of the NRREP Programme Steering Committee in order for the Chairperson to be able to report to the Programme Steering Committee. Ad-hoc meetings may be called by either member of the committee;
- The secretariat for the CREF Investment Committee will be the Secretariat established under the committee;
- The Secretariat shall announce the meetings with at least two weeks' notice. All documentation for the meetings shall be distributed to the members at least one week in advance together with a draft agenda;

- The members of the CREF Investment Committee may invite resource persons/stakeholders to address a specific issue on the agenda in order to clarify issues or offer specialised expert knowledge to the discussion, if required;
- The Secretariat is responsible for drafting the minutes of the CREF Investment Committee meetings and distributing these to the members;
- The Secretariat is established to be the operational arm of the CREF Investment Committee; and
- Members of the CREF Investment Committee will be paid honorarium for their work as committee members in accordance with guidelines of the Government and financial sector institutions.

## 6. The Secretariat

The CREF Investment Committee will establish a lean secretariat as its operational arm, which will provide day-to-day support for the implementation of its mandate and tasks. The Secretariat will play a key role in developing and implementing capacity building programmes for the financial institutions participating in implementation of CREF programme activities. The Secretariat will on an annual basis assess the need for capacity development and design programme responding to the needs in close collaboration with the respective institutions for the approval of the CREF Investment Committee. Capacity building activities will be outsourced to prequalified service providers in agreement with the individual banks. The Secretariat will also support the financial institutions with monitoring the performance of the CREF portfolio including on-site inspections.

The Secretariat will, furthermore, support with analysis of reports and information from the Handling Bank and Prequalified Partner Banks and in drafting reports to the CREF Investment Committee and to the NRREP Programme Steering Committee. It will play an active role in monitoring the performance of the participating institutions. Disputes and complains relating to the subsidy funds, which cannot be resolved internally between the Handling Bank and AEPC, will be referred to the CREF Investment Committee through the Secretariat. The Secretariat will establish close working relations with the NRREP Compliance Unit and facilitate its work.

The Secretariat should be housed by the Handling Bank, which will also accommodate meetings of the CREF Investment Committee. It is envisaged that the Secretariat will have a professional staff of two – one specialised in capacity development of financial institutions and the other in portfolio management and monitoring. The Secretariat may employ support staff as approved by the CREF Investment Committee.

**The Management and Monitoring Specialist – Head of Secretariat** will be overall responsible for managing the relationship with the Handling Bank and other participating financial institutions and for monitoring their performance in accordance with signed agreements. He/she will develop and implement a monitoring framework for the performance of all CREF related activities including efficiency and effectiveness of funding instruments as well as impact assessment at end-users level. He/she will review the subsidy fund management mechanism, the wholesale lending strategy, the retail lending, the investment strategy and on a regular basis monitors the implementation against agreed performance indicators. Monitoring work may be carried out directly by the Specialist or in collaboration with service providers contracted on a transparent and competitive basis. An initial task will be to do a mapping and pre-qualification of relevant service providers. The Specialist will work closely with the Capacity Development Specialist in defining and implementing capacity development programmes. A key task is also the development and

implementation of the CREF Communication Strategy, which will aim at promoting and creating awareness about the facilities available through CREF and the partner financial institutions with the support of AEPC. He/she will be responsible for the management of the Secretariat and will report to the CREF Investment Committee.

**The Capacity Development of Financial Institutions Specialist** will be overall responsible for capacity development needs assessment of the participating financial institutions, and development and implementation of capacity building programmes. Capacity assessment will be done once a new financial institution enters the programme and regularly on an annual basis. The assessment and implementation will be done in close collaboration with the HR and Training Departments of the participating financial institutions. Capacity development programmes will include product development; loan appraisal and supervision systems and procedures; management and staff training. Capacity development programmes will be implemented directly by the specialist or in collaboration with service providers contracted on a transparent and competitive basis. An initial task will be to do a mapping and pre-qualification of relevant service providers. He/she will support participating financial institutions in the promotion of financial instruments available under CREF financing agreements and in this connection also work closely with AEPC technical units as well as Regional Service Centres, District Energy and Environment Units and private sector entrepreneurs. The Capacity Development Specialist will report to the Portfolio Management and Monitoring Specialist.

## Annex II – Job Description: National Project Facilitation Adviser

<b>Job Title</b>	: AEPC National Project Facilitation Adviser
<b>Component</b>	: CREF Component
<b>Duty Station</b>	: AEPC
<b>Responsible to</b>	: Executive Director AEPC

### Background

The AEPC (the Alternative Energy Promotion Centre) is mandated to develop and promote renewable and alternative energy technologies. It has established an outreach structures through Regional Service Centres (RSC) and District Energy and Environmental Units (DEEU). Through these structures AEPC are supporting project developers (communities, households, manufacturers, installers, distributors) in preparing bankable projects to be presented to the Prequalified Partner Banks and LFIs (Local Finance Institution). AEPC is, furthermore, the point of entry for subsidy applications and is responsible for the technical verification before submitting to the Handling Bank for financial verification and payment in accordance with the Government's Subsidy Policy and Delivery Mechanism. AEPC through its technical components and outreach structures will support demand-side management, while CREF through the Secretariat and the selected financial institutions supports supply-side management for the development and financing of renewable energy technologies.

### Overall Purpose

A National Project Facilitation Adviser will be recruited by NRREP to assist the Executive Director in supporting technical components and Regional Service Centres in identifying and developing bankable projects with the project developers. The Adviser will be responsible for ensuring a smooth and effective processing of subsidy applications within RSCs, DEEUs and AEPC. He or she will also be responsible for the coordination and liaison with the CREF (Central Renewable Energy Fund) Secretariat.

### Main Task

The AEPC National Project Facilitation Adviser will be responsible for *inter alia*:

- Conduct orientation seminars jointly with CREF Secretariat for AEPC, RSC and DEEU staff on subsidy and credit financing of renewable energy projects;
- Participate with AEPC technical departments in promotion of renewable technologies and projects - promoting access to subsidies and credit facilities;
- Support RSCs and DEEUs in promoting investments in renewable energy projects;
- Assist project developers - jointly with AEPC technical staff - in developing bankable projects and in negotiations with CREF Prequalified Partner Banks and LFIs - stimulate demands for renewable energy projects;
- Support banks as a resource person in project cycle management including addressing non-performing loans;
- On a regular basis undertake field visits jointly with AEPC technical staff to RSCs, DEEUs and project sites;
- Be the focal point within AEPC for coordination and liaison with CREF Secretariat - subsidy fund management and credit facilities;
- Participate in management meetings of the CREF Secretariat - linking and promoting the agenda of AEPC;
- Participate in AEPC management meetings - reporting on subsidy fund management and credit facilities;

- Manage and coordinate the technical verification process of subsidy applications within AEPC and ensure proper documentation;
- Ensure proper subsidy database/MIS system within AEPC technical components, which will feed into the database system of the Handling Bank;
- Coordinate with AEPC Monitoring component for the timely monitoring and supervision of projects receiving subsidy financing;
- Liaise with the CREF Secretariat in terms of the status of subsidy and loan applications;
- Participate in addressing subsidy and loan application disputes with project developers – representing the AEPC in such cases;
- Receive and analyse reports from the CREF Secretariat;
- Participate with the Secretariat in the preparation and follow-up on the annual work plan and budget for the CREF component; and
- Participate in reviews of relevant policies including the Credit and Subsidy Policy and Delivery Mechanism.

### **Qualifications and Experience**

- Education – minimum requirement is at Master level in finance, economics or banking;
- Minimum of seven years of relevant work experience with project development and financing or 10 years of work experience at Bachelor degree in relevant discipline;
- Relevant work experience from the renewable energy sector and with working with programmes financed by development partners will be added advantages;
- Conversant in utilisation of computer applications including Microsoft Office package;
- Excellent communication and presentation skills;
- Excellent interpersonal skills and proven track record in team work;
- Fluency in spoken and written Nepali and English.

### **Terms and Conditions of Employment**

- One year contract with the possibility of annual extensions subject to performance;
- The position will be based on the NEX salary guidelines at level NPPP 3; and
- Benefits and allowances in accordance with the NRREP guidelines.

## Annex III – Job Description: CREF Management and Monitoring Specialist and Head of Secretariat

<b>Job Title</b>	: CREF Management and Monitoring Specialist and Head of Secretariat
<b>Component</b>	: CREF Component
<b>Duty Station</b>	: CREF Secretariat
<b>Responsible to</b>	: CREF Investment Committee

### Background

The Central Renewable Energy Fund (CREF) will be established as the financial intermediation mechanism for the renewable energy sector under the National Rural and Renewable Energy Programme (NRREP). The objective of CREF is as the core financial mechanism to be responsible for the effective delivery of subsidies and credits to the renewable energy sector.

The CREF Financial Intermediation Mechanism will be implemented through private commercial and development banks selected on a transparent and competitive basis in accordance with well-defined eligibility criteria. A Handling Bank – the apex financial institution - will be responsible for managing the core functions of CREF i.e. wholesale lending to Prequalified Partner Banks; Subsidy Fund Management; and Investment Management. A number of Prequalified Partner Banks – the second-tier financial institutions - will be responsible for the retailing of CREF funds to eligible projects in the renewable energy sector. In order to enhance the outreach, the banks will be required to form strategic alliances with local financial institutions (LFI).

The NRREP Programme Steering Committee under the chairmanship of the Secretary, Ministry of Science, Technology and Environment (MSTE) decides on the overall priorities of the programme and is overall responsible for the implementation of all components including CREF. Given the specific focus of CREF on financial sector activities, a specialised subcommittee will be established for the strategic management and oversight of the CREF financial intermediation mechanism – the CREF Investment Committee. The membership of the Investment Committee will reflect the nature of CREF and include representation from Ministry of Finance, Nepal Rastra Bank, MSTE, AEPC, the private sector and the development partners.

The CREF Investment Committee will establish a Secretariat as its operational arm. The Secretariat will be responsible for monitoring the performance of the selected banks, promote CREF activities, capacity assessment and development, and for liaison and coordination with AEPC. It will initially be financed out of NRREP funds, will have a professional staff of two and be housed in the Handling Bank in order to facilitate close and efficient interaction on a daily basis.

### Overall Purpose

The Management and Monitoring Specialist – Head of Secretariat will be overall responsible for managing the relationship with the Handling Bank and other participating financial institutions and for monitoring their performance in accordance with signed agreements. The Specialist will work closely with the Capacity Development Specialist in defining and implementing capacity development programmes. He/she will work closely with the AEPC National Project Facilitation Adviser in all aspects of development and financing of renewable energy projects including access to subsidies and credit facilities. The Specialist will be responsible for the management of the Secretariat and will report to the CREF Investment Committee.

**Main Task**

The CREF Management and Monitoring Specialist – Head of Secretariat will be responsible for *inter alia*:

- Advise the CREF Investment Committee on the CREF financial intermediation mechanism including the policies, strategies and criteria relating to wholesale lending, the retail lending, and the investment of CREF funds;
- Develop and implement a monitoring framework for the performance of all CREF related activities including efficiency and effectiveness of funding instruments as well as impact assessment at end-users level;
- On a regular basis monitors the implementation of the CREF financial intermediation mechanism through the Handling Bank and the Prequalified Partner Banks against agreed performance indicators;
- Support the work of the NRREP Compliance Unit and follow-up on recommendations made;
- Support banks as a resource person in project cycle management including addressing non-performing loans;
- On a regular basis undertake field visits jointly with bank staff to RSCs, DEEUs and project sites;
- Participate in reviews of relevant policies including the Credit and Subsidy Policy and Delivery Mechanism;
- Undertake an initial mapping and pre-qualification of relevant service providers to support financial monitoring activities;
- Develop and implement a CREF Communication Strategy, which will aim at promoting and creating awareness about the facilities available through CREF financial intermediation mechanism and through AEPC, RSCs and DEEUs;
- Develop and maintain a CREF knowledge-based management information system for documentation and dissemination of lessons learned and best practices in the financing of renewable energy projects;
- Prepare the CREF annual work plan and budget in close collaboration with AEPC and the Handling Bank and present to the CREF Investment Committee;
- Responsible for reporting to the CREF Investment Committee on the performance of CREF financial intermediation mechanism against work plans, budgets, targets and indicators;
- Responsible for the efficient management of the Secretariat and the resources allocated, including offices and facilities made available by the Handling Bank, in accordance with approved operational manual;
- Supervise and guide the work of the CREF Capacity Building Specialist;
- Act as Secretary to the CREF Investment Committee and as such being responsible for calling meetings, circulating and managing documentation, drafting minutes and follow-up recommendations made;
- Establish close collaboration with AEPC management, technical components and the National Project Facilitation Adviser in the promotion and development of renewable energy projects; and
- Support activities initiated under the NRREP programme including audits, reviews, appraisals, planning of new support through CREF and other programme activities; and
- Any other tasks which may be required for the efficient and effective operations of the Secretariat.



**Qualifications and Experience**

- Education – minimum requirement is at Master level in finance, economics or banking;
- Minimum of 10 years of relevant work experience with project development and financing;
- Relevant work experience from renewable energy sector development and with working with programmes financed by development partners will be added advantages;
- Conversant in utilisation of computer applications including Microsoft Office package;
- Excellent communication and presentation skills;
- Excellent interpersonal skills and proven track record in team work;
- Fluency in spoken and written Nepali and English.

**Terms and Conditions of Employment**

- One year contract with the possibility of annual extensions subject to performance;
- The position will be based on the NEX salary guidelines at level NPPP 4; and
- Benefits and allowances in accordance with the NRREP guidelines.

## Annex IV – Job Description: CREF Capacity Building Specialist

<b>Job Title</b>	: CREF Capacity Building Specialist
<b>Component</b>	: CREF Component
<b>Duty Station</b>	: CREF Secretariat
<b>Responsible to</b>	: CREF Management and Monitoring Specialist and Head of the Secretariat.

### Background

The Central Renewable Energy Fund (CREF) will be established as the financial intermediation mechanism for the renewable energy sector under the National Rural and Renewable Energy Programme (NRREP). The objective of CREF is as the core financial mechanism to be responsible for the effective delivery of subsidies and credits to the renewable energy sector.

The CREF Financial Intermediation Mechanism will be implemented through private commercial and development banks selected on a transparent and competitive basis in accordance with well-defined eligibility criteria. A Handling Bank – the apex financial institution - will be responsible for managing the core functions of CREF i.e. wholesale lending to Prequalified Partner Banks; Subsidy Fund Management; and Investment Management. A number of Prequalified Partner Banks – the second-tier financial institutions - will be responsible for the retailing of CREF funds to eligible projects in the renewable energy sector. In order to enhance the outreach, the banks will be required to form strategic alliances with local financial institutions (LFI).

The NRREP Programme Steering Committee under the chairmanship of the Secretary, Ministry of Science, Technology and Environment (MSTE) decides on the overall priorities of the programme and is overall responsible for the implementation of all components including CREF. Given the specific focus of CREF on financial sector activities, a specialised subcommittee will be established for the strategic management and oversight of the CREF financial intermediation mechanism – the CREF Investment Committee. The membership of the Investment Committee will reflect the nature of CREF and include representation from Ministry of Finance, Nepal Rastra Bank, MSTE, AEPC, the private sector and the development partners.

The CREF Investment Committee will establish a Secretariat as its operational arm. The Secretariat will be responsible for monitoring the performance of the selected banks, promote CREF activities, capacity assessment and development, and for liaison and coordination with AEPC. It will initially be financed out of NRREP funds, will have a professional staff of two and be housed in the Handling Bank in order to facilitate close and efficient interaction on a daily basis.

### Overall Purpose

The CREF Capacity Development Specialist will be overall responsible for capacity development needs assessment of the participating financial institutions, and development and implementation of capacity building programmes. Capacity assessment will be done once a new financial institution enters the programme and regularly on an annual basis. The assessment and implementation will be done in close collaboration with the HR and Training Departments of the participating financial institutions. Capacity development programmes will include product development; loan appraisal and supervision systems and procedures; management and staff training. Capacity development programmes will be implemented directly by the specialist or in collaboration with service providers contracted on a transparent and competitive basis. The Capacity Development Specialist will report to the CREF Management and Monitoring Specialist and Head of the Secretariat.

### Main Task

The CREF Capacity Development Specialist will *inter alia* be responsible for:

- Develop an overall capacity building policy and strategy, which will focus on development of products suitable for financing projects in the renewable energy sector, related manpower development and enhance outreach of the participating banks for the approval of the CREF Investment Committee;
- Develop a general approach and methodology for capacity assessment and tailor-made for each of the participating financial institution including LFIs in close collaboration with the respective HR and Training Departments;
- Undertake capacity development needs assessment in each institution and develop and capacity building plan for the approval of the CREF Investment Committee and the respective bank/LFI;
- Undertake a mapping and pre-qualification of relevant service providers;
- Responsible for implementation of the capacity development plan in close collaboration with the respective HR and Training Departments – either directly or by contracting prequalified service providers;
- Undertake impact assessment of the capacity building support and document lessons learned and best practices in this field;
- Facilitate support to the participating financial institutions in enhancing their outreach for project development and monitoring capacity;
- Support banks as a resource person in relation to the efficient operations of the CREF financial intermediation mechanism;
- On a regular basis undertake field visits jointly with bank staff to LFIs, RSCs, DEEU and project sites;
- Promote financial instruments available under CREF financing intermediation mechanism and in this connection also work closely with AEPC technical units, chief Operations Adviser as well as Regional Service Centres, District Energy and Environment Units and private sector entrepreneurs;
- Contribute to the CREF annual work plan and budget in close collaboration with AEPC and the Handling Bank and present to the CREF Investment Committee;
- Establish and maintain a knowledge-based management information system of capacity building initiatives and lessons learned and best practices developed in this field; and
- Contribute to progress and other performance reports on the CREF financial intermediation mechanism against work plans, budgets, targets and indicators.

### Qualifications and Experience

- Education – minimum requirement is at Master level in Human Resource Development, institutional, management and skills development;
- Minimum of seven years of relevant work experience with human resource development and management training and mentoring or 10 years of work experience at Bachelor degree in relevant discipline;
- Relevant work experience from financial sector development and with working with programmes financed by development partners will be added advantages;
- Conversant in utilisation of computer applications including Microsoft Office package;
- Excellent communication and presentation skills;
- Excellent interpersonal skills and proven track record in team work;
- Fluency in spoken and written Nepali and English.

### Terms and Conditions of Employment

- One year contract with the possibility of annual extensions subject to performance;
- The position will be based on the NEX salary guidelines at level NPPP 3; and
- Benefits and allowances in accordance with the NRREP guidelines.

## Annex V – Case Studies on past AEPC/ESAP Experience

### 1. Hydro-debt Fund – Case Study

#### 1.1. Background

The current subsidy for MHP ranges between 30% and 50% of the total cost of the project and including equity, there is still a fund gap of 10% to 40% of the total cost of the project. Therefore, there is a need for filling this gap, either through a direct lending or lending via a local financial institution. There are several concerns of the potential investors. The lack of knowledge on MHPs, reliable local partners, repayment and security issues, among others, are prominent factors for the investors mainly located in urban areas. Availability of long-term funds is also a factor. Therefore, the Micro Hydro Debt Fund (MHDF) was established under AEPC, which is earmarked solely for lending to MHPs. GIZ and AEPC expect that the Banks would be more familiar with MHPs by “learning by doing”. After few successful endeavours, Banks shall find the portfolio to be profitable and in the long run, use their own funds to finance MHPs in future. The MHDF is placed at competitively selected financial institutions. Himalayan Bank and Clean Energy Development Bank have been selected as the two partners and the fund has been equally placed at these two banks.

#### 1.2. Objective and Scope

- The overall objective of the fund is to improve the access to the rural population to clean energy solution by providing credit for off-grid MHPs. The fund envisages more than 400 kW of additionally generated electricity to bring electricity to roughly 19,000 individuals covering as many as 3,500 households, 6,500 people in social infrastructure institutions and 600 people benefitting from productive end uses.
- The fund shall also demonstrate that lending to the rural micro-hydro sector can be profitable and a commercially sustainable business. Moreover, the pace of rural electrification shall also increase with the efforts stimulating agro-processing and other income generating enterprises enhancing livelihood of the rural poor.

The entire budget came from GIZ. Initially, the fund itself was Euro 500,000 with a technical aid fund of Euro 42,000. With the success of the model, GIZ added Euro 600,000 (TA: Euro 50,000).

#### 1.3. Implementation Modality

**AEPC:** provides overall technical support, approves subsidy, chairs the steering committee

**RSC/DEEU/S:** coordination with potential MHPs for generating sufficient demand by organizing awareness/orientation classes so that more projects and LFIs get the required information, accompany banks for field visits. This activity is embedded in the annual work plan of the RSCs for better implementation.

**Financial Partners** (selection, outreach, products (loan terms and conditions), capacity building, monitoring and supervision

- Selection of fund administrators (HBL and CEDBL) was done in a competitive basis against approved evaluation criteria and presentation
- Both direct and indirect lending is possible. So far banks are comfortable lending directly, in terms of outreach. The banks are targeting “not so remote projects” or “low hanging fruits” so far. Therefore, outreach needs to be up-scaled.
- Loan terms and conditions:
  - Banks pay nominal interest (3.5 -5%) to AEPC, quarterly
  - Risk sharing is 50/50 between the fund and the banks
  - Maximum 12% permissible while lending
  - Field trips sponsorships, capacity building possible
  - Support to Projects from 10-100kW
  - Up to 40% debt financing possible with pure project financing approach
  - Insurance done for first three years by ESAP/RERL

So far, the banks are directly involved in monitoring and supervision of the portfolio. There has been no need for capacity building on the part of the partner banks through the TA, as they were already “trained” and “oriented” under ESAP II on MHP financing.

#### **Community Awareness and Mobilisation**

Done with the support from DEEU/DEES, RSCs. Specially, RSCs organize such activities as a part of their annual work plan. They invite, preferably, 10 potential MHPs and LFI in the vicinity of these MHP for an orientation by REF. The two-day long classes provide all the potential MHPs on the documentary requirement of banks, solving equity issues, solving repayment issues, reaching a financial closure, etc. At the end of the two-day session, MHPs can prepare a complete file along with the required documents. The participants can also answer questions, which the banks generally ask.

#### **Loan Portfolio and Performance:**

HBL	Loan Amount	Capacity	Remarks
Total 10 projects	NPR. 24 million	346 kW	No default reported so far
<b>CEDBL</b>			
Total 9 projects	NPR. 16 million	339 kW	No default reported so far

#### **4. Lessons Learned**

- Public land as a collateral is a problem
- Time taken for assessment is the deterrent factor for the banks
- Fulfilling documentary requirement by MHPUC is lengthy, hence, assessment by banks is lengthy
- More banks need to be inducted and more training and capacity building needed

## 2. Credit Financing Solar Home System – Case Study

### 2.1. Background

Despite subsidy being available for SHS, there is still a fund gap. For those households, which can pay upfront, they are benefitting from using SHS. For those, who can't pay upfront, they still can't access the technology. Therefore, a need was felt for filling this gap. However, there are several concerns of the potential investors. The lack of knowledge on SHSs, reliable local partners, repayment and security issues, among others, are prominent factors for the investors mainly located in urban areas. Availability of long-term funds is also a factor. Therefore, AEPC, under its Energy Sector Assistance Program II, implemented a project called "Credit Financing SHS". AEPC expected that the Banks would be more familiar with SHS financing by actually lending. After successful implementation, Banks would find the portfolio a profitable one and upscale lending in future.

### 2.2. Objective and Scope

The overall objective of the project was to find viable models such that SHS can be disseminated via the mixture of subsidy, equity and a loan component.

The budget came from ESAP II and the total fund that was used for this project was slightly over NPR. 22 million for a three-year implementation.

### 2.3. Implementation modality

#### Role of different stakeholders

**AEPC:** provided overall technical support, approved subsidy, provided funds through ESAP II

**Consultants:** development of vendor and credit financing mechanisms, selection of local financial institutions, coordination with partner banks, generating sufficient demand by organizing awareness/orientation classes, accompany banks for field visits, conducting different capacity building trainings, reporting.

#### Financial Partners

- Selection of wholesale lending banks was done in a competitive basis against approved evaluation criteria. Interested banks were also selected as partners based on their commitment.
- Both wholesale lending to a local financial institution and vendor financing is possible.
- Loan terms and conditions:
  - Banks used their own funds at commercial rates
  - No risk sharing
  - Field trips sponsorships, capacity building possible
  - Supported 42 local financial institutions from 14 districts
  - Insurance done by ESAPII

So far, the banks are directly involved in monitoring and supervision of the portfolio.

### **Community Awareness and Mobilisation**

- Specialized training of trainers was done. The trainers are from the LFIs themselves. These trainers would go to rural areas and create awareness to a mass of 50 to 100 people so that they install SHS through credit.
- Local social mobilizers are hired in each district to monitor the performance of all LFIs.
- One person recommended by LFI is trained for Level I course for prompt service delivery

### **Loan Portfolio and Performance:**

- Over NPR. 23 million wholesale loan provided by urban partner banks
- Over NPR. 40 million loan provided by LFI to individual users
- Over 9,000 SHS disseminated via this approach
- No default reported by banks and in many cases all loans have been fully repaid within the tenure
- Multiple loan provided by banks once the partnership was built between the LFIs and themselves
- Loans to other sector (microfinance) was also provided
- Micro-insurance of over 2,200 SHS was done

### **2.4. Lessons Learned**

- Physical inspection of LFIs prior to selection is necessary
- There should be no gap of subsidy during the course of implementation
- After sales service is of paramount importance for timely repayment of loan
- Consultation with Solar Electric Manufacturers' Association is necessary

### 3. Credit Financing of the Biogas Plant – Case Study

#### 3.1. Background

Biogas Credit Fund was established in the year 2000 under the Alternative Energy Promotion Centre (AEPC) with grant support of 2.5 million Euro from KfW to the GoN. The credit fund would be provided to the MFIs, which would further on lend to the biogas consumers.

#### 3.2. Objective and Scope

- To improve the local MFI to flow the credit in biogas plant.
- To improve the biogas credit easily, to the poorer farmers, especially in the rural areas of the country.
- To extend the credit facility in the areas where existing banks are not providing biogas credit easily and or adequately.
- To improve the local MFIs in the promotional activities for the development of biogas technology.

The GoN agreed to provide all the necessary technical support through AEPC. The budget consisted mainly of the Euro 2.5 million and the interest earned through the fund.

#### 3.3. Implementation modality

##### The main roles and responsibilities of AEPC are:

- Management and operation of the credit fund.
- Maintenance of proper record as credit fund.
- Sanction, disbursement and collection of the credit.
- Supervision and monitoring of the credit provided.
- Conduction of necessary trainings.
- Auditing of biogas credit fund, after the completion of each fiscal year, by an independent registered auditor.
- Other related activities as required.

**DEEU:** DEEU/s provide due recommendation along with the loan application of the concerned MFIs so that the MFIs are able to receive loan from AEPC.

**RSCs:** if loan is applied from MFI, the MFI within the working area of RSC/RRESC will be informed through a letter from RSC/RRESC to submit all the available information.

##### Financial Partners

Selection of the Financial Partners is done as per the following:

- The FIs minimum loan repayment rate must be 90%
- The FIs should not have been black listed by other organizations, especially the central bank.
- Basically the MFI must be a registered institution under one of the following:
  - Co-operative Act 2048.
  - Financial Intermediary Act 2055.



- Bank and Financial Institution Act 2063.
- Nepal Rastra Bank Act 2058.

#### **Loan terms and conditions:**

- AEPC will disburse the average amount of a maximum Rs. 25,000 (In words Twenty five Thousand only) per plant to MFI.
- AEPC Charge the Interest 6% & MFIs will be charge Maximum 14% to own their customers.
- The reimbursement application should be made within Three year (36<sup>th</sup> Months) from the date of reimbursement.
- The MFI should prioritize the disadvantaged groups, *dalits, janajatis* and women etc. while providing loans
- AEPC strongly supervision, inspection and monitoring of the MFIs in timely as a standard format.
- AEPC will not take any responsibility in case of loan due of any clients of MFIs.

#### **Community Awareness and Mobilisation**

Done by Biogas Company & MFIs in collaboration.

#### **Loan Portfolio and Performance:**

Situation of Biogas Credit Fund End of Magh, 2069 (11<sup>th</sup> February 2013)

- Number of beneficiary MFIs: **442**
- Total Loan Investment NPR. **333 million**
- Total Loan Repayment NPR. **286 million**
- Total Loan Outstanding NPR. **47 million**
- Installed Number of Plant through Credit approx **25,000**
- Total Coverage Number of Districts **47**

#### **3.4. Lessons Learned**

- To minimize risk, AEPC should have the collateral security for the loan.
- Abrupt stoppage of the BCU activities has huge effect to the loan repayment. Therefore, there should be a clear-cut policy on continuation or discontinuation of the BCU activities
- Training, capacity building & awareness program should be embedded in the program, specially to the MFIs and the potential users
- Source of repayment needs to be determined prior to loan disbursal
- Field visit needs to be conducted before approval/disbursal of loan

## Annex VI – Peer-Review of CREF Concept<sup>13</sup>

The following comments, as requested in your mail are based on a reading of the “Concept Note – CREF Institutional Model” as come across during the reading. The comments may not be complete, and you are welcome to revert with additional questions, which I shall then try to clarify to the best of my ability.

As I told you, I was in Nepal around 10 years ago on a team assigned to provide Technical Assistance to Danida’s Energy Sector Programme for preparations of the establishment of a Rural Energy Fund (REF). We did make progress at that time, but as a Task Force, which we were to advise, had not been established, our efforts took an alternative direction. From your Concept Note it appears that developments in Nepal have now cleared the way for a conclusion of what was attempted started at that time.

Furthermore, I have been working in a number of countries with constructions and designs similar to those you are aiming at, covering detailed design and specifications of criteria, conditions and procedures, and assisting with finalising negotiations and agreements with Fund Holding Bank and Participating Financial Institutions in Armenia, Moldova and Nicaragua, and with overall support to a similar programme in Bolivia.

So, here are my comments:

- i. Firstly and importantly, I am strongly in favour of your “third option”, using the commercial banking system for the handling and administration of the funds, for a variety of reasons, some of which as mentioned by you strictly objective (efficient, effective, lean, flexible), and others for reasons of minimising fiduciary risks. – This was actually also among the recommendations given by the assignment 10 years ago.

Also, as I see it, credibility in the whole complex of investments in/financing of renewable energy activities, which – after all – would always contain an element of a business proposition, would be strengthened in the general public as well as in the business society, with the establishment of a fruitful collaboration between relevant government institutions and the private sector, here the commercial banking sector.

- ii. Having worked with these issues as a development banker in a number of countries, I would propose the following in order to avoid confusing myself with terminologies:

FHB (Fund Holding Bank) =	The bank selected for Subsidy Fund Management, Investment Management and overall administration of Wholesale Lending
PFI’s (Participating Financial Institutions) =	Retail Financial Institutions: Receiving applications for subsidies/credit from end-borrowers – applying for re-

<sup>13</sup> The review was undertaken by Vagn Rasmussen, Chief Development Banker, Development Associates, Copenhagen, Denmark. Mr. Rasmussen has previously been engaged by Danida as consultant for the preparation and establishment of the Rural Energy Fund, Nepal.

	financing from Fund Holding Bank – and lending to end-borrowers
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- iii. An aspect which deserves consideration is the establishment of funding mechanisms with a reasonable balance between flexible and practical procedures and bureaucratic control, probably mostly required as regards subsidies, but also relevant for re-financing of loans. From your Concept Note it appears that great importance is put on keeping the planned CREF institution as lean and simple as possible, aiming at optimizing a “buying-into” the existing infrastructure of FHB and PFIs. The success of this will depend on optimum co-operation between CREF, FHB and PFIs, based on the formulation of very clear and comprehensive conditions and procedures in agreements to be established.
- iv. The seven “guiding principles” appear to be very appropriate
- v. Please be aware that:
- a) Interest earned on funds provided by Danida may present an issue of such earnings being demanded repaid to Denmark, unless agreements are properly formulated.
- b) Clearly define the final destination for funds provided by Danida at the conclusion of the project/programme, or at least develop a formulation stating that such a decision is to be made (by whom?) at a certain time (which?).
- vi. Although I am not up to date with the present situation in Nepal, I would assume long/longer-term funds to be in short supply in the Nepalese banking system, thus probably making the intended re-financing mechanism attractive to financial institutions. Whether PFIs would be willing to leverage CREF funding with own funds is of course to be seen during implementation, but the threat of sanctions by Nepal Rastra Bank for not lending to deprived sectors would probably be a good motivation for banks to participate actively.
- vii. Re. Conceptual Framework:  
As regards the proposed model, I would just point at the fact that in principle there is an important difference between FHB and PFIs. While it will be relatively simple to define and measure the performance and responsibilities of PFIs and replace a PFI if necessary, the performance of FHB is not so easily measured and a replacement would be more complicated. Thus, while the FHB should of course be selected on a transparent and competitive basis, it would also be important that not only economic – but also “confidence, continuity and quality” aspects are given due consideration.
- viii. Re. Outreach Aspects:  
As I recall from the assignment 10 years ago, the issue of only few banks having sufficient geographical outreach to make a meaningful impact in some regions and districts was to be taken into account. Although, as also mentioned above, I am not up to date with the present situation in Nepal, I would assume that this issue still exists and that, therefore, it would be important first to get those PFIs with the best outreach on board – and, furthermore, to look into possible solutions either to make local financial institutions into direct PFIs or to establish outreach linkages between PFIs and such local financial institutions.

ix. Re. NRREP Programme Steering Committee:

In order to ensure proper and good co-operation between CREP and Fund holding Bank/PFIs, it is important that all overall priorities, criteria and procedures be properly and precisely established and defined from the outset, in advance of programme initiation (it is mentioned, for instance, under 5.1 that “changes in immediate objectives may be recommended”). Priorities, criteria and procedures to be established and defined must cover all issues mentioned under 5.2, **and** furthermore, detailed specific technical criteria, procedures and arrangements between all participants and beneficiaries of the programme.

It should be realised that when the programme is started and (possible) long-term financing issued, it would create unwanted disturbances if “rules of the game” are changed or adjusted.

Thus, it would really pay to be meticulous in the establishment and definition of detailed technical criteria, conditions and procedures covering all aspects, including subsidiary loan agreements with PFIs and all participants and beneficiaries of the programme. In other words: “If started well, it can work well”.

x. Re. CREF Investment Committee:

In point 2: The Investment Committee should also “establish and review criteria for retail lending”

xi. Re. The Secretariat:

a) Would the professional staff of the Secretariat be provided, and paid, by the Fund Holding Bank or by the programme? – or would it just be housed in Fund Holding Bank, and paid by the programme? – It might actually be both, and this issue is among those, which should be included in negotiations with Fund Holding Bank.

b) Depending on developments, it may be necessary to appoint a “leader” of The Secretariat, and reconsider its envisaged staffing.

xii. Re. CREF Fund Holding Bank:a) Subsidy Fund Management:

It is mentioned that subsidies will be forwarded in weekly batches? Is it not the initial intention that all funds are to be placed in, and for administration by, the Fund Holding Bank?

b) Investment Management:

Would it not be necessary to keep subsidy funds (which can be described as “one shot injections”), and credit funds (which by definition will rotate) strictly separate? Depending on the type of funds, alternative suitable revenue generating investment options may be applied.

c) Wholesale Lending:

It is mentioned under this point that “the bank will use its infrastructure, systems and procedures as well as manpower for the loan appraisal and supervision”? – In my optic this will go for PFIs – not for the Fund Holding Bank?

xiii. The “risk issue”:

While it is obvious that risk of non-repayment of loans by end-borrower is to be

borne by the respective PFIs, who have appraised and evaluated loan applications and taken collateral as required, it is less clear to me what risk of non-repayment of loans is to be carried by FHB:

a) If we talk about risk of failure by PFIs (i.e. collapse) which, with a proper selection done by the CREF Investment Committee under the Chairpersonship of Nepal Rastra Bank, may be considered less likely, I am firstly of opinion that pre-qualification of PFIs should be the responsibility of the CREF Investment Committee (with FHB only in an observer role); and secondly that it would therefore not be reasonable to hold FHB responsible for possible collapses of PFIs.

b) If it is envisaged that FHB is to share the risk of non-repayment of loans by end-borrower with PFI, a rather complicated dual role of handling fund/investment management and wholesale lending and at the same time participating in the evaluation and appraisal of individual loan applications would be given to FHB. This, of course, could be done, but it would complicate – in my opinion – the formulations of authorities and responsibilities in agreements.

xiv. Re. “What is in it for the Fund Holding Bank”?

My immediate reaction to this question is that it could be an interesting proposition for an FHB, and that in my opinion CREF would be in a favourable position for getting into constructive negotiations with potential FHB candidates. I would estimate, depending on the conditions agreed upon and the overall situation of the Nepalese financial system, that a Fund Holding Bank would be willing to pay a certain interest (to be negotiated) for holding funds at such a volume.

**However**, before reaching a final conclusion it will be necessary to clarify some issues of the financial sector in Nepal, and establish an exact definition of authorities and responsibilities of the Fund Holding Bank and of PFIs, which would also make it possible to estimate incomes and expenses of the respective participants, such as:

a) The cost of funds situation in Nepal’s financial system? – Central Bank’s refinancing rates? – Commercial banks’ market lending rates? – etc.,

b) An exact definition of the risk sharing, for non-repayment of interest as well as principal, between FHB, PFIs and CREF – and in this connection also the proportional functions, and risk sharing between subsidies and credit funds. On this issue I would have thought, as mentioned above, that Fund Holding Bank were not to carry risk of non-repayment of individual loans, which is to be carried by PFIs. The risk of PFIs failing to repay to CREF is to be mitigated by a careful screening and selection of PFIs.

c) It will be necessary to consider and define the rate of interest to be paid by end-borrowers, as is probably already done (on subsidies? – as well as credit funds). – Shall it be market rate of interest? – or shall there be interest subsidies on certain environmental-supportive projects, sectors? – geographic considerations? etc.

When this has been clarified, and on the basis of the outcome of the above mentioned, the CREF should initiate negotiations with Fund Holding Bank and PFIs to establish arrangements and conditions, which can satisfy all participants in the most optimal way.

Conclusion:

In addition to considerations about the overall points raised above, I would again mention that the setting up and arrangement of the model is an exercise requiring proper and careful preparations, and it is important to get it right from the outset.

As I see it, initial arrangements needed to describe and clarify the technical requirements from and actions by the respective participants would need to include, possibly among others – to be discussed and agreed:

- ToR for CREF Investment Committee and Secretariat, including initial Draft Manual for the Secretariat's activities and procedures
- Tender materials for FHB, incl. detailed ToR; Envisaged Flow of Funds; Wholesale Lending Strategy and Criteria, including Risk Sharing Conditions; Retail Lending Strategy and Criteria, including Risk Sharing Conditions; Subsidy Fund Management and Investment Arrangements, Interest Policy, Investment Policy and Strategy for CREF Credit Funds, Eligibility Criteria for Selection of FHB, incl. Bidding Procedures, Scoring Matrix and Evaluation Procedures
- Subsidy Funds Management and Investment Draft Agreement with FHB
- Credit Funds Management and Investment Draft Agreement with FHB
- Wholesale Credit Draft Agreement with FHB
- Draft Contract with FHB
- Standard MoU between FHB and Donors

And – concerning PFIs:

- Eligibility Criteria for PFIs
- Matrix for Evaluation of PFIs
- Format for Invitation to PFIs
- Notification of Selection of PFIs
- Subsidiary Re-Financing Draft Agreements between FHB and PFIs
- Draft Contract with PFIs

And – depending on decisions concerning detailed implementation conditions and procedures:

- Formats for Notification of PFIs' signatory authorities
- Formats for Annual PFI Budgets for Re-Financing Requests, individual and consolidated
- Formats for Re-Financing Requests, individual and consolidated
- Formats for Repayment Schedules, individual and consolidated
- Formats for Overall Re-Financing Budgets, based on PFI Budgets and Repayment Schedules
- Formats for Notification of Transfers to PFIs
- Formats for Confirmation of Disbursements
- Formats for Notification of Repayments
- Formats for Periodic Reports of Outstanding Balances per PFI, individual and consolidated
- Monitoring Plans
- Formats for Minutes of Monitoring Visits
- Formats for Registration of Documents for PFI files

3<sup>rd</sup> January 2013  
Vagn Rasmussen