



*SHARING THE WATER RESOURCES OF THE
ORANGE SENQU RIVER BASIN*



Feasibility Study for the Development of a Mechanism to Mobilize Funds for Catchment Conservation

Business Case
for the
ORASECOM Conservation Fund

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Executive Summary

A parallel study to this business case has demonstrated that viable conservation projects exist in the Orange-Senqu River Basin that require funding. Projects range from studies and monitoring, to implementation of interventions on priority transboundary conservation issues. Projects may be implemented by the parties, or by ORASECOM. Whatever the nature or implementation arrangements for the projects, funding for these projects is required. The ORASECOM agreement requires ORASECOM to recommend funding arrangements to accompany any project recommendations that the commission may make.

Accordingly, The ORASECOM Conservation Fund (OCF) has been proposed as a vehicle to obtain, manage and disburse finance from innovative funding sources, for conservation measures in the Orange-Senqu River Basin. The specific objectives of the OCF are:

- To identify priority conservation issues for funding, from the list of priority conservation issues identified in the ORASECOM strategy (Basin Wide Plan);
- To develop a funding strategy for the priority conservation issues;
- To develop projects to address the priority conservation issues, including feasibility and bankability;
- To source and manage funding for the priority conservation issues, including contract management and disbursement for projects;
- To monitor success of projects and funding, and to report on achievements.

Objectives and functions of the Fund are enabled by the legal form of the Fund, which conveys powers and responsibilities on the Fund. In addition, the legal form provides the legal framework within which the Fund operates and ensures good governance, accountability and transparency for the OCF. Accordingly, the legal form is a critical element in ensuring funder confidence in the OCF through creating the appropriate legal and governance structure for the OCF. The business case explores the legal form in depth, deploying a number of criteria to evaluate a decision tree on appropriate legal form. The recommendation arising from the detailed analysis is that the Fund be established as a charitable company in term of Section 21 of the South African Company's Act. The location was chosen owing to the legal proximity to ORASECOM, which will be hosting the Fund.

The organisational – institutional model for the Fund is explored in detail in the business case. Of the three conceptual options, the most appropriate initial model is for the Fund to conclude a management contract with ORASECOM, and thus for the Fund functions to be performed from within ORASECOM. This model strongly supports the close relationship between the OCF and ORASECOM, is cost effective as it reduces duplication and it maximise use of functioning structures and systems. As the work of the Fund increases, so it may be appropriate to move the functions out of ORASECOM into a separate institution. This would be seen as an evolution of the Fund into an increasingly autonomous entity. Starting with the hosting arrangement with ORASECOM (management contract) does not preclude this evolution of the Fund.

Governance of the Fund reflects the emerging understanding and principles of good corporate governance. A governing body is established for the Fund, which assumes governance oversight and fiduciary responsibilities for the Fund. This body is critical in conveying confidence to funders, partner institutions and broader stakeholders. It is proposed that the governing body consist of between 5 and 11 directors, comprise of representatives of:

- Departments of Water Affairs of the Member States;

- The ORASECOM Executive Secretary;
- Donors, selected through the donor forum;
- Private sector, selected through the stakeholder committees; and
- Civil society; selected through the stakeholder committees.
- The fund manager (Fund CEO where applicable) should attend board meetings, but in a non-voting capacity.

Based on the purpose and nature of the institution, the following competencies must be represented on the board:

- Understanding of water related conservation issues in the basin and beyond;
- Understanding of mitigation measures – technical and non-technical;
- Understanding of the donor environment, accountability and credibility to donors;
- Legal and compliance competency;
- Financial competency and some knowledge of fund management; and
- Human resource competency.

Strategy development is an important element of governance and one of the key responsibilities of the governing body. In the case of the OCF, given the close relationship with ORASECOM, the ORASECOM strategy (the Basin Wide Plan) serves as the umbrella strategy for the Fund, with the priority interventions identified for OCF funding compiled out of the priority conservation issues identified in the Basin Wide Plan. Accordingly, the OCF does not develop an independent strategy, but rather a strategy nested within the Basin Wide Plan. The Fund will develop an independent funding and financial strategy.

The organisational implications of the Fund reflect the institutional-organisational model: the management contract arrangement with ORASECOM. Despite a wide range of functions required for the Fund, it is anticipated that these functions can all be conducted by a Fund manager sitting inside ORASECOM, in the first instance. As the work-load of the Fund increases, so additional capacity may be required. However, at the outset, a single fund manager reporting to the Executive Secretary will suffice.

The financial model for the fund reflects this lean structure, with only limited establishment and low operational costs. Whilst the OCF functions are managed within ORASECOM according to a management contract, an annual budget of R1.6 million is required. Initial once-off establishment costs of circa R200, 000 are anticipated.

This business case was presented to the project steering committee and the ORASECOM Technical Task Team in early March 2009, and to the ORASECOM Legal task Team and ORASECOM Council in April 2009. Comments arising from these key consultations have been incorporated into the document.

Table of Contents

Executive Summary	i
Table of Contents	iii
1 Introduction	1
1.1 Background	1
1.2 Process to date	1
1.3 Purpose of this document.....	2
1.4 Structure of the document.....	2
2 Motivation for the Fund.....	3
2.1 The conservation situation	3
2.1.1 The key conservation issues	3
2.1.2 Need and opportunities for basin conservation.....	6
2.2 Response to the opportunity: the ORASECOM Conservation Fund	6
2.2.1 Purpose	7
2.2.2 Functions	7
3 Legal form	9
3.1 Available legal forms	9
3.2 Assessment of legal form	10
3.2.1 Assessment criteria.....	10
3.2.2 Applying the assessment criteria.....	12
3.2.3 Conclusion of the assessment.....	15
3.3 Comparing trusts and charitable companies.....	15
3.3.1 Legal regimes in the member states.....	15
3.3.2 Trusts.....	17
3.3.3 Company.....	17
3.3.4 Summary: trust vs. company.....	17
3.4 Legal location of the Fund	20
3.5 Conclusion of the legal form analysis	20
4 Institutional Arrangements.....	21
4.1 Institutional linkages with ORASECOM	21
4.1.1 Institutional models for the Fund	21
4.1.2 Conclusion of the institutional model analysis	23
4.2 Institutional arrangement with other institutions	24
5 Fund Governance	26

5.1	Good governance.....	26
5.2	Governing body.....	26
5.2.1	Purpose	26
5.2.2	Code of conduct.....	27
5.2.3	Composition	27
5.2.4	Nomination.....	28
5.2.5	Tenure	28
5.2.6	Management of the institution	28
5.3	Strategy development	29
5.4	Fund management.....	29
5.4.1	Management arrangements	29
5.4.2	Fund manager.....	31
5.5	Governance systems and control	32
5.5.1	Planning systems.....	32
5.5.2	Management appraisal and performance management.....	33
5.5.3	External and internal audit.....	33
5.5.4	Reporting	34
6	Organisational and HR considerations	35
6.1	Functional description	35
6.2	Organisational structure	36
7	Financial considerations.....	38
7.1	Financial arrangements.....	38
7.2	Financial requirements of the Fund	39
7.3	Cost of the OCF	39
7.3.1	Cost-model assumptions.....	39
7.3.2	Establishment costs	39
7.3.3	Operating budget	39
7.3.4	Cost summary.....	39
7.4	Sources of finance	40
7.4.1	Contributions from the Parties.....	40
7.4.2	Donor Funds	40
7.4.3	Investment income	41
7.4.4	Charges or taxes.....	41
7.4.5	Summary.....	42
7.5	Financial systems.....	42
8	Risk analysis	43
8.1	Identification of key risks	43
8.2	Risk quantification and management.....	44

9 Implementation considerations 45

Appendix A 46

 Examples of interventions to priority conservation issues 46

Appendix B 50

 Review of Conservation Funds 50

APPENDIX C 67

 ORASECOM Institutional Review 67

1 Introduction

1.1 Background

The Orange-Senqu River originates in the highlands of Lesotho and stretches over 2 300km from the source to its mouth on the Atlantic Ocean. The river system is one of the largest river basins in Southern Africa with a total catchment area of 850,000km² inside Lesotho, Botswana, Namibia and South Africa. The natural mean annual runoff at the mouth is estimated at 11,500Mm³.

Supplying the economic heartland of South Africa, the basin has been extensively altered and its water resources widely utilised. Given competing demands and complex socio-economic drivers within the basin, significant management problems exist relating to both water quantity and quality, and to environmental quality. The riparian countries have for some time recognised that a basin-wide integrated approach has to be applied in order to find sustainable solutions to these problems and that this approach must be anchored in a strong political will.

Within this context, one of the key responsibilities of ORASECOM will be to promote the conservation of the catchment through the development of indicators and the monitoring of these indicators as well as the implementation of conservation measures/programmes. This will be for the benefit of all stakeholders since it will be one of the support measures that ensure that development is sustainable. Clearly there is a cost attached to these measures and there will be a need to develop processes and mechanisms to ensure that funds are mobilised on a continuous basis to meet these costs.

Accordingly, in April 2008 the ORASECOM Secretariat invited tenders for a project entitled: "Feasibility Study for Development of Mechanism to Mobilize Funds for Catchment Conservation". This tender was awarded to Pegasys Strategy and Development (Pty) Ltd in September 2008. The project objective is stated as "*propose a mechanism for the mobilisation of funds for the conservation of the basin's water and associated natural resources*". Given that the project is at a feasibility level, the project requires that innovative mechanisms to Fund conservation measures are investigated and are developed into a business case that describes the conceptual model, requisite institutional arrangements and the technical elements of funding and disbursement, and that demonstrates the viability of the mechanism.

1.2 Process to date

The project was composed of three phases:

- a 2-month inception phase;
- a 3-month consultative phase; and
- a 2-month reporting phase.

The inception phase included a detailed review of: (1) the conservation situation and issues in the Basin; (2) the possible financial instruments for conservation in the Basin (including a detailed review of Funds); and (3) of the ORASECOM institutional arrangements that define the nature of ORASECOM's engagement.

The inception report was presented to the first stakeholder workshop, with recommendations on a suitable financial mechanism for ORASECOM's engagement with priority conservation issues in the basin. The recommendation arising from the workshop was to investigate the development of a Fund¹ as a financial vehicle to route finance² to priority conservation interventions, based on a defined conservation finance strategy.

A draft business case for the Fund was developed through the consultative phase, and was presented to the consultative workshop to test and further develop the emerging understanding. In addition, the emerging business case was tested with the ORASECOM Legal Task Team and ORASECOM Council. This process has significantly enriched the business case, leading to finalisation of the business case for implementation.

1.3 Purpose of this document

This document is the final business case for the ORASECOM Conservation Fund. It has been presented, tested and improved through the Project Steering Committee and stakeholder workshops in March 2009, and through the ORASECOM Legal Task Team and ORASECOM Council presentation in April 2009.

1.4 Structure of the document

The document follows a relatively standard structure for a business case (motivation) for an institution. It begins with a description of the purpose and functions of the institution (chapter 2), which informs the appropriate legal / legal form of the institution (chapter 3). Then the key institutional arrangements for the Fund are investigated, including the most appropriate institutional model (chapter 4), leading to governance considerations (chapter 5), a discussion on organisational arrangements (chapter 6) and financial arrangements (chapter 7). The document ends with an assessment of the key risks of the Fund (chapter 8) and some high-level implementation considerations (chapter 9).

¹ The inception workshop recommended that a managed fund, established as a separate legal entity (probably a trust) but closely linked to ORASECOM be explored further through the business case.

² Primarily arising from donor or investment income, but possibly also including user charges, PES and other sources of income in the future.

2 Motivation for the Fund

Significant interest has been expressed in the concept of a Conservation Fund for ORASECOM, through the project steering committee and the wider stakeholder consultations. This chapter outlines the motivation for the Fund, describing the conservation context and the need for funding at a basin-wide level merged into an assessment of ORASECOM institutional arrangement and international experience on Conservation Funds. The motivation forms the basis for an understanding of the purpose and associated functions of the Fund.

2.1 The conservation situation

A parallel study to this business case has demonstrated that viable conservation projects exist in the Orange-Senqu River Basin that require funding. Projects range from studies and monitoring, to implementation of interventions on priority transboundary conservation issues. Such projects may be implemented by the parties, or by ORASECOM. An outline of some of the key conservation challenges and the possible responses to such challenges is given below.

2.1.1 *The key conservation issues*

The extensive review of literature and consultations established five main conservation challenges in the Orange-Senqu River Basin. Of these five issues, some have localized impacts whilst others have transboundary implications. These main challenges identified in the basin are:

- Threat to water resource availability
- Decline in water quality
- Alteration of the flow regime/hydrology
- Soil erosion and wetland degradation
- Invasion of alien species

Of these, water resource availability, water quality and alteration of flow regime were identified as the highest priority challenges for the basin (Table 1).

Water resource availability

Water resource availability in the basin is greatly influenced by agricultural, municipal and industrial demands. Agriculture accounts for the most significant portion of current and projected demand (60%). Mining and industrial demands in the Orange River System (excluding the Vaal river system) are a relatively small component of the total demand, although these sectors are concerned about assurance of supply, owing to increasing demands on the system. Over 97% of total water use takes place within South Africa. A steady increase in consumptive water demand is anticipated in the basin – a total increase of 12.6% is projected by 2025.

The Vaal River system is facing the greatest challenges in reconciling future demand with, in particular, significant growth in the Rand Water supply area projected. Losses of around 25% are experienced in this area, suggesting that water conservation and demand

management could contribute significantly to meeting increased demand. RSA DWAF has set a target of 15% reduction in demand in the Vaal river system by 2015. In addition, a number of smaller towns (e.g. Kuruman, Mafikeng and Upington) have been identified for water conservation interventions to relieve water availability issues.

A number of interventions that address water resource availability issues and concerns stand out in the basin – all of which require financial support of some form. Examples of such interventions include (see Appendix A for details):

- Water conservation and demand management measures in towns such as Kuruman, Mafikeng and Upington
- Partnership in the Richtersveld COWEP programme and the extension of similar projects to Namibia and Botswana
- Conducting a study on the potential for increased efficiency of water use in agriculture, through reducing losses in conveyance and on-farm use (although it is accepted that agriculture in the region is already highly efficient)

Water quality

Surface water quality in the Upper and Middle Orange River areas is generally good. In the Vaal River high nutrient and salt loads are the result of mining and industrial discharges and untreated or poorly treated municipal effluent. High nitrate levels in the Lower Orange River suggest nutrient enrichment from agriculture. The Integrated Water Resources Management Plan conducted by GTZ also found an increase in salinity in the lower reaches of the river, resulting from irrigation return flows and evaporative losses along the river.

Thus the major water quality issues centre on mining and industrial activities (predominantly in the Vaal River basin), municipal discharges and irrigation (particularly between Vioolsdrift and the Vaal-Orange confluence). While existing mines are exploring a range of innovative options for managing mine water discharge, the challenge of abandoned mines remains high and one where significant funding will be required.

Small-scale mining along the banks of the Lower Orange River result in high sedimentation loads and, along with reduction in river flow, create conditions favourable for the proliferation of reeds. The proliferation of reeds has been exacerbated by high nutrient loads resulting from irrigation activities in the Lower Orange River. Reeds pose several additional problems in that they increase the surface area available for blackfly larval attachment and increase riverine transmission losses caused by evaporation and evapo-transpiration.

A number of interventions that address water quality issues and concerns stand out in the basin – all of which require financial support of some form. Examples of such interventions include (see Appendix A for details):

- Support of the rehabilitation of the Klip River wetlands;
- Support to the remediation of mine drainage from decommissioned mines; and
- Support the upgrading of various wastewater treatment works.

Altered flow regime

The main drivers resulting in a degraded hydrological regime are high water demand in the Vaal River basin, and reservoir operations which do not provide meaningful environmental releases.

The key reported impacts are:

- The proliferation of reeds due to lower flow velocities and high nutrient loads
- An increase in the prevalence of blackfly
- Changes in the hydraulics of the Orange River Mouth estuary

Key challenges in the estuary are also linked to physical changes associated with sand mining and road construction, rather than the flow regime per se. Co-ordination of rehabilitation of the estuary is weak.

A number of interventions that address issues and concerns relating to altered flow regime stand out in the basin – all of which require financial support of some form. Examples of such interventions include (see Appendix A for details):

- Coordination of the rehabilitation and management of the Orange River Mouth estuary;
- Support to the Black Fly control programme; and
- Support to Lower Orange Transfrontier Conservation Area (LOTCA) Invasive Alien Plant Management Programme.

Table 1: summary of example priority conservation issues in the Orange-Senqu River Basin

ISSUE	CAUSE	IMPACT	COUNTRIES IMPACTED
Water availability	High demands and abstractions, particularly in agriculture	Availability concerns for downstream countries	RSA and Namibia
		Low flow in estuary	RSA and Namibia
Water quality	Poorly managed waste water treatment works, industrial effluent and agricultural run-off	High nutrient levels resulting in eutrophication	RSA and Namibia
	Pollution from mining and industry	High levels of salinity and heavy metal pollution	RSA and Namibia
Altered flow regime	Reservoir operations, high rates of abstraction	Flow regime inappropriate to ecological requirements; low flow in estuary	RSA and Namibia
	Black fly infestation	High costs in cattle losses	RSA and Namibia
	Reed invasion	Increased black fly population, altered habitat, flow and siltation patterns, and fire hazard.	RSA and Namibia
	Poor control of water hyacinth	De-oxygenation, interference with recreational use and dam operation	RSA and Namibia

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2.1.2 Need and opportunities for basin conservation

It is clear that there are a number of conservation challenges in the Orange-Senqu River Basin, of differing orders of magnitude, and with differing funding requirements. Addressing these conservation challenges is critical in ensuring the sustainable management of the basin, particularly given both increasing demand and the impacts of climate change.

It is equally clear, from the studies conducted in this project, that there are a number of interventions that could result in significant improvements in the status of the basin. Some of these interventions can also bring significant benefits to water users and local communities. Two challenges arise in relation to a number of these challenges:

- How best to fund them; and
- How best to co-ordinate cross-border activities (where these are required).

International best practice has pointed to the management of water at the basin level, rather than according to administrative and political boundaries. The establishment of ORASECOM has proved the commitment of the riparian states of the Orange-Senqu River Basin to this approach. This institutional arrangement enables the identification, at the basin level, of the key conservation challenges in the basin, and the adoption, at the basin level, of an appropriate funding strategy to address these challenges. Such an approach moves well beyond the rhetoric of integrated basin management, to its implementation, and reflects a maturity of vision by riparian states in relation to the management of shared water resources, and the shared benefits to be derived from such cooperation.

The tables in Appendix A provide examples of the range of conservation-related interventions required in the basin. Such interventions range from the relatively low cost, to the extremely expensive. A number of these interventions will also require substantial multi-year funding in order to take on the magnitude of the challenge.

The key challenge with respect to conservation priorities and priority interventions is financial and institutional in nature, given that the technical understanding of these issues and the required interventions has largely been gained. The challenges can therefore be articulated as:

- Where and how to access the necessary financial resources for the priority conservation issues, particularly where these issues span international borders; and
- What institutional arrangements are required to source, manage and disburse these financial resources, ensuring the best principles of governance, financial oversight and control, accountability and transparency are maintained.

The establishment of a specific, basin-wide, funding mechanism to support the implementation of these interventions will facilitate the sustainable management of the basin to the benefit of all parties.

2.2 Response to the opportunity: the ORASECOM Conservation Fund

The development of fund, to support the financial management of resources to achieve particular conservation outcomes, is well established internationally. These funds vary greatly in nature – legally, institutionally, geographically, purpose and financially. A detailed

review of conservation funds was undertaken during the inception phase of this project and can be found in the inception report. A summary of the review is attached in Appendix B. The review provided some important lessons on best practice that have been incorporated into this business case.

Arising from that review and from a review of the ORASECOM institutional arrangements (Appendix C), it is clear that a Fund provides the most appropriate financial vehicle to support the priority conservation issues identified through the basin-wide assessment and planning process. This conclusion was supported by the Project Steering Committee, the ORASECOM Technical Task Team and the ORASECOM Legal Task Team. This endorsement forms a critical point of departure for the business case.

2.2.1 Purpose

It is clear that the Orange-Senqu River Basin faces some significant conservation challenges and that one of the key responsibilities of ORASECOM will be to implement conservation measures / programmes (where this responsibility has been delegated by the parties) or to make recommendation to the parties on appropriate conservation measures or programme and provide sources of funding. Whether ORASECOM implements interventions or provides recommendations, it will need to secure funding for the identified, priority conservation issues (and responses). In this regard, a mechanism is required to ensure that funds are mobilised on a continuous basis from a wide variety of sources.

The purpose of the ORASECOM Conservation Fund can therefore be stated as:

“To source, manage and disburse funding for priority conservation issues in the Orange-Senqu River Basin through the establishment of a dedicated, independent financial vehicle”

Key objectives arise from the purpose:

- To identify priority conservation issues for funding, from the list of priority conservation issues identified in the ORASECOM strategy (Basin Wide Plan);
- To develop a funding strategy for the priority conservation issues;
- To develop projects to address the priority conservation issues, including feasibility and bankability;
- To source and manage funding for the priority conservation issues, including contract management and disbursement for projects;
- To monitor success of projects and funding, and to report on achievements

2.2.2 Functions

A summary of high-level functions is included:

- Strategy
 - based on the framework provided by the ORASECOM Strategy, to develop a Fund strategy outlining the priority conservation measures that the Fund will finance (sub-strategy of the ORASECOM strategy)
 - implement the strategy through a business plan
 - monitor the achievement of strategy through a series of indicators and accounting (review)
 - link implementation of the strategy to performance management systems in the Fund

- Source funding
 - Develop a marketing strategy for the Fund and the priority conservation issues
 - Source finance from key donors (new and existing donors), including the development of bankable projects and proposals
 - Consider and develop mechanisms for ongoing financial support through reliable income streams, including investment, user charges and member state contributions
- Fund management
 - Protection of income
 - Investment of capital and the generation of investment income (endowment income)
 - Management of the outsourcing of Fund investment
 - Regular reporting on Fund performance
- Project development and disbursement
 - Identification of interventions / programmes against strategy (criteria)
 - Project feasibility assessment
 - Project development, including determining financial requirements
 - Develop disbursement arrangements, including contracts with implementing agents
 - Monitoring of projects and disbursements
 - Project and expenditure reporting
- Contracts management
 - Develop, implement and manage contracts
 - Monitor contracts with implementing agents / parties
 - Report on implementation of contracts
- Monitor and report on conservation projects
 - Monitor priority conservation issues selected for funding, as part of a broader monitoring of conservation issues in the basin by ORASECOM
 - Report on conservation expenditure and progress with priority conservation issues
- Institutional relationships
 - Develop relationships with key partners and stakeholders
 - Articulate a partner / key stakeholder strategy as part of the ORASECOM strategy and the business plan
- Governance
 - Strategic direction
 - Oversight and control
 - Appropriate design and structure of the organisation
 - Financial reporting and accounting
 - Systems of risk management and mitigation
 - Measure and maintain organisational performance
- Administrative functions
 - HR management, including management of individual performance
 - Administration

3 Legal form

3.1 Available legal forms

There are broadly 5 different legal forms that can be considered for the Fund. These are:

- A trust, established under common law, in one of the member countries or an independent country.
- A charitable foundation, established under company law (or specific charities legislation), in one of the member countries or an independent country.
- An international body, established by decree of an international grouping such as SADC.
- A special entity created by custom legislation in one of the member countries.
- An entity created by agreement between the member countries.

The above legal forms are briefly described (Table 2).

Table 2: available legal forms

LEGAL FORM	DESCRIPTION
<i>A trust, established under common law, in one of the member countries or an independent country.</i>	<p>South Africa has an extensive body of common law supporting the establishment and operation of trusts. It is based on English common law, modified by subsequent court findings and some specific legislation – such as the Trust Property Control Act.</p> <p>A trust is not a juristic person, but it tends to act like one to all intents and purposes. A trust is created when a donor asks a trustee to manage its assets on behalf of a beneficiary. The trustee takes ownership of the asset, but does not benefit from the fruits of the asset – they are only the custodian. Trusts are extensively used for charitable foundations, where a donor wishes to place a large pool of funds in the hands of trustees, to be used for the benefit of a particular cause.</p> <p>The ORASECOM Conservation Fund could consider establishing itself as a trust within one of the member states, or in an independent country if this is seen to be advantageous.</p> <p><u>Example:</u> Table Mountain Trust, Mandela Rhodes Trust</p>
<i>A charitable foundation, established under company law (or specific charities legislation), in one of the member countries or an independent country.</i>	<p>While foundations can also take the form of a trust, this legal form is used here to describe the establishment of a legal entity that is established under company law, or other relevant legislation. For example, the South African Companies Act 61 of 1973 makes provision (section 21) for the establishment of 'Associations not for Gain'. These are not for profit companies that are established as public companies. As such they must abide by the relevant Companies Act legislation and disclosure requirements, and are governed by a Board of Directors, appointed by the members (shareholders). Members do not receive dividends or any other form of profit share in the company, but are only responsible for establishing the company, and then voting for directors at the AGM.</p>

	<p>Countries such as the UK have specific charities legislation (the UK Charities Act) which provides for the establishment of a legal entity incorporated in the name of this Act. The governance and disclosure requirements tend to be more aligned to the needs of non-profit organisations with less of the onerous requirements stipulated in companies legislation.</p> <p><u>Example:</u> various NGOs (WWF, TNC, etc.)</p>
<i>An international body, established by decree of an international grouping such as SADC.</i>	<p>Organisations such as the UN and SADC have the power to create international bodies. These bodies have legal status if recognised as such by the member states.</p> <p><u>Example:</u> SADC Secretariat, SADC Tribunal</p>
<i>A special entity created by custom legislation in one of the member countries.</i>	<p>One of the member states may choose to pass specific legislation which brings the ORASECOM Conservation Fund into being. The powers and functions of the Fund will then be specified in the legislation, along with other relevant legislation governing public entities of this nature.</p> <p><u>Example:</u> Gautrain Management Agency, South African National Roads Agency, TCTA</p>
<i>An entity created by agreement between the member countries.</i>	<p>The member countries may agree to establish the Fund, along similar lines to the establishment of ORASECOM itself. This calls for agreement between the parties on issues such as powers and functions and governance arrangements.</p> <p><u>Example:</u> ORASECOM, ZAMCOM</p>

3.2 Assessment of legal form

The legal form of the OCF is based on the functions that the Fund will have to perform. The adage of “form follows function” applies to enable the best suited form for the required set of functions to achieve the desired outcome to be selected.

3.2.1 Assessment criteria

In assessing the most appropriate legal form for the OCF, a number of important criteria should be applied to a design-tree (Figure 1). The following criteria emerge from international lessons and good-practice:

- *Governance criteria*
 - *Independence and accountability to build credibility:* it is critical that the Fund be regarded as credible to enable support from the key sources of funding, namely donors (multinational, government, corporate, private and civil society organisations) to be forthcoming. As in the medium to long-term the Fund may be receiving income from beneficiaries of conservation activities, these sources of revenue will also require credibility and accountability; and
 - *Protection of income and tight financial control:* the Fund’s primary purpose is to source finance against and defined expenditure framework (strategy), and to manage the funds, including management of disbursement and associated

- contracts. Accordingly, the Fund primary risk is related to finance and the management of funds, and accordingly it requires good systems of financial control and accountability. This is both to reduce internal risks (failure of systems) and to build investor / donor confidence. Governance systems that enable and support such management and control will be required.
- *Ability to ring-fence risk*: as the Fund is going to manage significant financial resources, it will be important that the Fund's risk is ring-fenced and that this risk is not transferred to a hosting or parent institution. This also improves accountability, as risk cannot be transferred.
- Legal regime and legal status
 - *Stable and recognised legal regime*: the legal regime upon which the institution is built (i.e. the laws that govern the entity) must be stable and recognised, and must incorporate or underpin principles of good governance and tight control. Weak legal regimes, or legal regimes that are likely to change do not engender investor / donor confidence and do not provide a stable platform for the establishment and management of the organisation; and
 - *Legal regime that enables management flexibility and portability*: the OCF will cover a basin composed of four member states, As such; the institution requires some flexibility in requirements for location and management of the institution (meetings, board representation, residency, etc.). In addition, it may be necessary to move the institution to another legal regime (portability). The regime under which the institution is established should enable as much flexibility as possible, whilst providing clear framework for good governance and control.
 - *Legal status*: the OCF will need to enter into contracts with staff, contractors and others. It is therefore necessary that the Fund has the legal capacity to do so. Its legal form should also be such as to limit the liability of directors/trustees and staff – except to the extent to which they are negligent in the performance of their fiduciary and other duties.
 - Human resources, skills and capacity
 - *Clear and simple systems that enable attraction of skills and support hosting / service sharing arrangements*: the OCF will require certain skills in the sourcing and management of funding. In addition, it is possible that the Fund will share some functions and services with a hosting institution. Accordingly, the form of the Fund must enable it to attract and retain scarce skills, and to easily enter into HR arrangements with potential hosting institutions. Finally, an established and tested HR regime should be utilised, to reduce internal risk associated with poor HR policy and management.
 - Establishment and management complexity
 - *Simple arrangements for management*: the OCF will be entering into a range of contractual, funding, management and hosting arrangements. It will be important that the Fund be established in such a manner (i.e. legal regime, institutional and governance arrangements, organisational arrangements) that these arrangements with the “outside” world are simplified. Such simplification reduces risk, increases efficiency and reduces cost.

3.2.2 Applying the assessment criteria

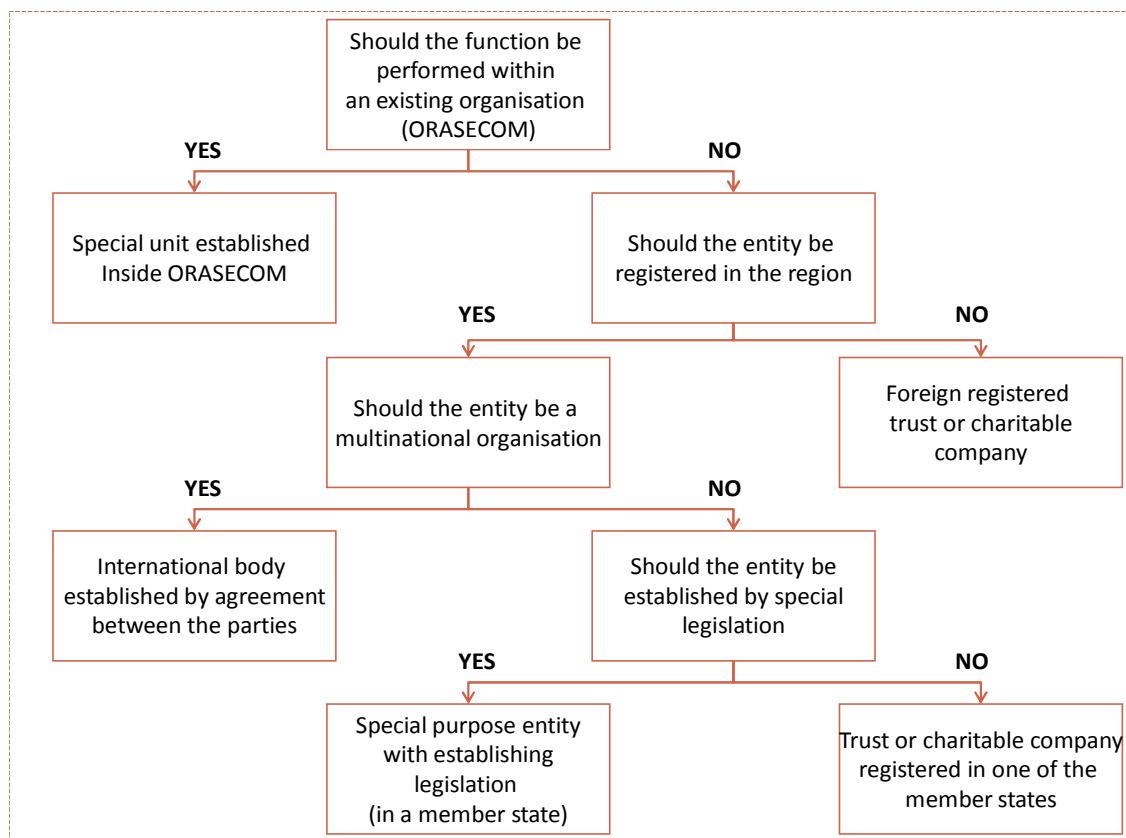


Figure 1: Decision-tree for the legal form of the OCF

Applying the criteria to the decision-tree:

- Should the function be performed within an existing organisation (ORASECOM)?*
Assessing this question against the criteria highlights the key issues for consideration as governance, independence and risk. It is widely recognised that an independent Fund, separate from any institutional influence and in a position to make its own decisions, is the central element of building credibility of the institution with prospective funders and financiers. An independent entity will be better equipped to establish the appropriate systems of governance and financial control, reflecting the financial management and financial risk nature of the institution. Finally, an independent entity is required to ring-fence risk – where the Fund is part of an existing entity, the financial risk of the Fund is transferred to the parent entity. This suggests that a separate, legal entity is required for the OCF.
- Should the entity be registered in the region?*
Although both a foreign-registered entity and an entity registered in one of the basin states achieve³ the required criteria⁴, it is possible to express a preference, based on

³ Assuming foreign registration in the UK, Europe or the USA.

the local context and prerogatives of the Basin. A comparison of the two options is included (Table 3).

In testing this with the Project Steering Committee and key stakeholders, preference for a regional fund emerged. This was motivated on four grounds: (1) Funding is likely to be local, as the initial reliance on donor funding reduces. Thus regional registration supports tax benefits to regional funders. In addition, the issue of foreign exchange regulations and the movement of money is facilitated by a regional fund, with money moving with SADC or SACU. (2) A regional fund facilitates hosting arrangements with ORASECOM, with consistent legal regimes supporting contract arrangements and human resource regimes. (3) A fund registered in the region reflects the regional flavour of the institution and grounds the initiative in the Basin. (4) Regional registration reduces the transaction and management costs (overheads) associated with the Fund.

⁴ Spergel and Taieb, in their 2008 review of conservation trust funds [Ref], identify 4 multi-country funds, none of whom are established in one of the member countries. The following quote from their review gives their reasons for establishing the Funds 'off-shore':

"In the cases of the first three of these multi-country funds, the countries for whose benefit the CTFs were established were considered (at the time that the CTFs were established) not to have legal systems in which most people had confidence, or which would protect the CTF from taxation and attachment, and which would not impose any legal barriers to the CTF's effective operation. In addition, since each of these three CTFs were established for the benefit of three different countries, it was felt by people in all of the countries involved that legally establishing the CTF in a "neutral" and mutually acceptable foreign country would allay fears that the CTF might otherwise end up being dominated by the particular one of the three countries under whose laws it might otherwise be established."

The fourth Fund (based in Central America) chose to establish itself in the USA to make it easier for US donors to contribute directly to the fund.

The Sangha Trinational Foundation (covering Cameroon, CAR and the Republic of Congo) is a trust established in the UK. The MD, Dr Timothee Fomete, gives the following reasons for why the trust was established in the UK:

1. The member countries are all francophone countries with no established trust law. One of the countries would have had to create the foundation through specific legislation and then get the other countries to recognise this foreign legislation – a process that is fraught with difficulty.
2. They wanted a stable legal environment that would not be subject to change.
3. They wanted a secure environment for investors.
4. They chose the UK because a UK trust does not require a local office, local directors or local board meetings. The UK also has an arrangement with the US whereby UK charities are allowed to apply for registration of a sister-charity in the US (section 501(3) (c) status of the US Internal Revenue Code).
5. Registering the Trust in a neutral country was politically more acceptable than choosing one of the member states.

Table 3: Comparison of regionally- and foreign-registration for the Fund entity

	REGIONALLY REGISTERED	FOREIGN REGISTERED
Governance		
<i>Independence</i>	Independence can be demonstrated, although more closely linked to member states (parties) owing to legal association. Basin registration however introduces a regional "flavour" to the institution.	Greater independence, as established under the legal regime of a country not in the basin. This however undermines basin "flavour" of the institution.
<i>Financial control & ring-fence risk</i>	Can be equally achieved in a foreign or a regionally registered entity	
<i>Financial matters (tax)</i>	Tax benefits for donors based in the region, requires separate establishment of fund-raising vehicle in other countries (e.g. UK and USA) for international donors	Tax benefits for donors in the country where the Fund is legally established
Legal regime		
<i>Recognised legal regime</i>	Both have well recognised legal regimes, although the foreign regime is possibly marginally better recognised (more credible) owing to significant precedence regarding such institutions and the governance thereof	
<i>Flexibility and portability</i>	Consistent legal regimes for hosting institution More easily portable	Flexible regime, but different legal system from regional host institutions (requires legal alignment)
HR regime		
<i>Human resources and skills</i>	Easily access tried and tested human resource systems that attract and retain staff, and are consistent with host institution	Good system, but consistency with host institution will have to be tested
Establishment		
<i>Establishment and management complexity</i>	Can be simple (depending on approach)	Simple, but may be more expensive because of the different legal and human resource regimes

- *Should the entity be a multinational organisation?*

This option requires special agreement between the parties to establish the entity as an international organisation, and recognition as such by the host country, similar to the process used for ORASECOM.

Assessing this option against the criteria demonstrates the key concerns as the legal regime (and related governance and confidence) and establishment complexity. The legal regime of this institution would have to be established through the international

agreement, and the regime of one of the parties will probably have to be adopted. Accordingly, the body of law supporting this entity is more limited than other options. This issue is key in considering good governance and funder confidence in the institution. A further (and perhaps more significant) consideration is the establishment complexity associated with creating a new international entity through agreement between parties. This process is lengthy, costly and complex, and undermines the short-term viability of the institution.

- *Should the entity be established by special legislation?*

This option assumes registration of the entity by one of the parties, through special legislation established in that country.

Assessment of this option against the criteria demonstrates its unsuitability on the basis of legal regime (and related governance and confidence) and establishment complexity. The legal regime for this entity would have to be created through the establishing legislation, with reference to other law for additional governance and control (such as company law). Such a process introduces legal complexity that may undermine the process or subsequent entity governance. A further key legal issue is the portability of the institution – as it is established by special legislation in one of the riparian states, the entity cannot be moved from that legal regime. Hosting may be established in another country, but legal issues between the hosting country requirements and the establishing regime remain. Finally, the establishment complexity introduced by the need for special legislation is extensive, requiring a lengthy, costly and complex process that undermines the short-term viability of the institution.

3.2.3 Conclusion of the assessment

Based on the analysis outlined above, it is clear that two legal forms are the most appropriate based on the purpose and functions of the proposed entity: a charitable company or a trust established in one of the member states. This conclusion is consistent with international experience, with similar funds internationally typically established as one of the above legal forms (charitable company or trust).

3.3 Comparing trusts and charitable companies

There are two proposed legal forms available to ORASECOM: a trust or a company (Table 5).

3.3.1 Legal regimes in the member states

These forms exist in all four member states. Trust law is well established in South Africa and Namibia, whilst in Botswana and Lesotho trust are recognised under company legislation. Each member state has dedicated company's legislation that recognises charitable companies and recognises various taxation benefits for these entities. Given the similarity between member states' legislation with respect to trusts and charitable companies, the remainder of this analysis will focus on the interpretations provided by South African law. These interpretations are however largely transferrable to the other member states (Table 4).

Table 4: comparison of the legal regime for trusts and charitable companies in the four ORASECOM member states

RELEVANT QUESTIONS	SOUTH AFRICA	NAMIBIA	BOTSWANA	LESOTHO
Is the form (both charitable company and trusts) enabled in law?	YES NGOs: Companies Act 1963 (s 21) Trusts: Trust Property Control Act (1988)	YES NGOs: Companies Act (2004) (s21) Trusts: Trust Monies Protection Act (1934)	YES NGOs: must be registered with the Registrar of Societies and the Dept of Civil and National Registration (Ministry of Labour and Home Affairs) Trusts : two pieces of legislation • Admin of Estate Trusts • And Deeds Registry Act 3302 The latter outlines the legal, governance and financial requirements	YES NGOs: supported under the Constitution, the judiciary (civil society). Must be registered. Not recognised as a company (i.e. not governed by company legislation) Trusts are regulated by the Deeds Registry Act 1967
Is the law the same/ different from SA? If yes, how so?	-	Companies Act is similar Trust Monies Protection Act does not exclusively deal with Trusts as encompassing, only with monies. In Namibia trusts are dealt with under common law: this implies that the legal requirements are similar to RSA law, however two differences exist: 1. trusts in Nam are recognized as legal persons 2. Can exist as 'oral' trusts (limited ability to ensure good governance)	NGOs: registration as set out above. Different in that it places more emphasis on the management of NGOs. This is evident in the establishment of a council for NGOs called BOCONGO Trusts: very similar legal structure to RSA	NGOs: the source of law is different, not typically from legislation, but constitution and other (tbc). Trusts: similar legal characteristics (tbc)
Is the form well supported in law (and legal history?)	YES	YES	YES	YES
Is any particular legal regime preferable, or are they all equally suitable? Why?	Trusts in SA are not juristic person NGOs: Section 21 Companies are juristic persons with well established legal regimes	Trusts are not exclusively recognized in legislation, but are established in common law. Trusts are recognized as legal persons Can conclude oral trust deeds, need not register with the Master NGOs: in legislation tax implications are dealt with well, however, in case the practice has been less successful.	Both legal regimes are similar in structure to RSA. Trusts are not recognised as juristic person	Trusts: The Income Tax Act shows that both trustees and trusts are chargeable (s11 and 15). Trusts take on a charitable organization form for tax exemption. NGOs: Charitable organizations are exempt from tax (s25).

3.3.2 Trusts

The legal establishment of the first legal form, the Trust, will provide ORASECOM flexibility as trusts can be used to serve a variety of purposes. Trusts are not recognised as a legal person, and the Trustees become the owners of the property - although in a legal and not a personal sense. However it is generally accepted that trusts are able to enter into valid contracts, with the representatives of the trust not being held personally liable as long as they have entered into the agreement with the express or delegated permission of the trustees. Trusts are ordinarily formed in four ways namely, by agreement, by means of a will, a court order or by statute. The parties to a Trust are the Founder, the Trustees and the Beneficiaries. ORASECOM is free to appoint any number of Trustees as there is no limit to the amount of Trustees appointed.

For a Trust to be created it must be legal and contain the following *essentialia*. There must be a clear intention; an obligation, property (including money) and an object (purpose), ORASECOM can set out the terms of Trust Deed and make general and specific rules regarding the general principles of the Trust administration. The administration of a Trust revolves primarily around the Trustee and the relationship between the trustee and the beneficiary. ORASECOM can furthermore set out the duties and obligations of trustees. If it chooses not to, then these duties and obligations will be determined by common law and by statute. They require, amongst others, that trustees always act in good faith, jointly and in an impartial manner.

3.3.3 Company

The second proposed legal form available to ORASECOM is a company. If established in South Africa this would be called a Section 21 Company, or 'Association not for Gain'. Typically, a company exists in law as a separate entity, distinct from its members. There must be at least seven members in the Company (equivalent to the Founder of a trust). All the assets and liabilities are its own and do not belong to the members. A Section 21 company has a two-tier structure, the lower tier comprising of seven or more natural or juristic persons called the members and the other comprising of two or more directors. Hence in theory, the ORASECOM Fund would be controlled by its members / shareholders, who have the right to exercise all the powers of the company. In practice, however, the strategic direction of the Fund is determined by the directors, who are elected by the members.

As a company the ORASECOM Fund will have wide powers to carry out its main object and purposes. These powers include the power to purchase movable and immovable property, to invest company funds in any way, to borrow money, to open and operate banking accounts, to employ staff etc. In order to be incorporated, and once incorporated, the ORASECOM Fund must comply with the extensive provisions of and formalities provided for in the Companies Act.

3.3.4 Summary: trust vs. company

The legal establishment of both these legal form processes provide the ORASECOM Fund sufficient legitimacy, accountability, transparency, protection and control. There are the apparent similarities which are shared by both legal forms namely, the establishment of the terms which outlines the appointment, powers and fiduciary duties, followed by the registration process and the Regulator under which both forms are protected. Clear nuances

are that Trusts are not recognised as a juristic person, whereas a company operates as a separate legal entity. Further, there is no minimum number of Trustees to be appointed, whereas a company (Section 21) requires no less than seven members to be appointed and no less than two directors.

Accordingly, there is little to choose between trusts and charitable companies in terms of the ideal legal form for the OCF. However, the juristic status of the Section 21 Company and the stringent requirements of the Company's Act probably make this the preferred form.

Table 5: Table of key attributes of trusts and charitable companies

ATTRIBUTE	TRUST	SECTION 21 COMPANY (or similar incorporated charity)
Legal status		
<i>Is it a legal entity?</i>	Not a legal entity except for tax purposes (South Africa)	Is a juristic person
<i>Through which legal instruments is it governed?</i>	Governed by extensive common law in countries such as the UK and South Africa. Legislation covers specific aspects; for example the Trust Property Control Act dictates the relationship of a Trust to the property under its control.	Section 21 companies are governed by the Companies Act and extensive common law. In countries such as the UK there are additional legislative requirements placed on charities through the Charities Act and SORP 2000 (also relevant to UK Trusts).
<i>Can it enter into contracts?</i>	Enters into contracts, etc. as if it is a juristic person and given some legal status by the Trust Property Control Act (South Africa). Requires evidence that the signatories to the agreement are acting under the express or implied approval of the trustees, as per trust deed requirements.	Enters into contracts (i.e. has all the powers of a legal person). Authority for signing on behalf of the company is normally delegated by the Board to the executive management.
Governance		
<i>Who has ultimate control?</i>	Trustees, or the Curator/Protector (depending on wording of Trust Deed)	Members, at the AGM, through their power to appoint the Board of Directors.
<i>Who has effective control?</i>	Trustees make decisions, or may delegate powers to management.	Board of Directors make decisions, with operations delegated to management.
<i>Who appoints the Board?</i>	The original trustees are appointed by the originator of the trust. The trust deed may then make provision for the replacement of trustees after a certain tenure. In the absence of any arrangement, the trustees themselves will determine when new appointments should be made and will make the election. The trust deed may also stipulate that decisions regarding new trustees will be made by the curator, or 'protector'.	The Board of Directors is appointed by the members of the company at the AGM. Normally the articles of association (similar to a constitution) will provide for the regular replacement of directors after a specified term. New directors are then appointed at the next AGM.
<i>Who appoints management?</i>	The Trustees	The Board of Directors
<i>Who is accountable?</i>	The Trustees each have a fiduciary responsibility to act in the best interests of the Trust.	The Board of Directors have a fiduciary responsibility to act in good faith.
Finance		

ATTRIBUTE	TRUST	SECTION 21 COMPANY (or similar incorporated charity)
Legal status		
<i>What level of financial autonomy is there?</i>	Trustees have discretion to manage the capital and income of the Trust, within the limitations set by the Trust Deed.	The Board of Directors have full control over the assets and income of the company.
<i>What level of transparency is there?</i>	Trusts do not have to disclose their financial affairs to the public, nor submit to an external audit. They are required to submit financial statements to the Master of the Court upon request. In practice, most trusts receiving donor money will subject themselves to audits and make their financial statements available to donors.	Companies are required to undergo an annual audit. Section 21 companies are public companies and are therefore required to make their annual financial statements publicly available.
<i>How are surpluses and reserves treated?</i>	A Fund is likely to be set up as a discretionary trust, which means that all surpluses are to be utilised in the interests of the trust deed, at the discretion of the trustees. The trust deed will normally provide that, upon dissolution, any reserves should be donated to an organisation with similar objectives.	A charitable company is not allowed to distribute surpluses to its members. Any surplus or reserve should be used to further the objects of the company. Upon dissolution, the Act requires any surplus to be distributed to a company or body with similar charitable objectives.
HR regime		
<i>What human resource requires exist?</i>	A Trust is subject to normal HR rules as prescribed by the host country's legislation and is not restricted in its ability to attract appropriate staff.	A company is subject to normal HR rules as prescribed by the host country's legislation and is not restricted in its ability to attract appropriate staff.
Risk management		
<i>Exposure of decision-makers to claims of non-performance.</i>	Trustees have a fiduciary responsibility to act in the best interests of the Trust. If it can be proved that they have failed to do so, then there is a risk that they could be held personally liable for a loss suffered by the Trust or a third party. <i>Bona fide</i> duty	The new Companies Act places a fiduciary responsibility on directors, making them personally liable if they act in bad faith, or if they continue to manage a business that is technically insolvent for more than 6 months. However the level of protection afforded to directors is slightly higher than that afforded to trustees.
<i>Risk of expropriation or other claim against the Fund's assets</i>	The assets of a trust are registered in the names of the trustees. Recent case law has confirmed that these assets should not be included in the trustee's estate in the event of claims made against the trustee. The assets of the trust are therefore protected.	The assets of a company are generally protected from claims made against the members and directors of the company. For example, if a director or member of a company is declared insolvent, his/her creditors may not attach the assets of the company.
<i>Ability to satisfy donors that their donations will be spent as intended.</i>	A trust may have the power to alter its objectives without consulting donors, and may have the right to withhold financial statements from non-trustees. However this is unlikely to happen and major donors will inevitably sign contracts that commit the trustees to conform to	A company must comply with fairly rigorous internal control, reporting and disclosure requirements, as prescribed in the Companies Act. Donors will therefore not need to stipulate these conditions in their own agreements.

ATTRIBUTE	TRUST	SECTION 21 COMPANY (or similar incorporated charity)
Legal status		
	certain reporting and internal control requirements.	

3.4 Legal location of the Fund

The analysis against criteria above recommended registration of the Fund within the Basin. Selection of one of the member states is accordingly required.

From a legal perspective, the Fund can be established in any of the member states, as each state has appropriate legislation enabling the Fund and each state has a legal history (precedent) regarding the legal administration of such entities. Accordingly, there is no legal preference for the location of the Fund within one or other member state (Table 4).

However, from a practical perspective, it is evident that the Fund should be located in the same country as the host institution. Subsequent sections of this business case will motivate the appropriate institutional and organisational arrangement for the Fund, closely associated with the ORASECOM (a hosting arrangement based on a management contract). Accordingly, it is recommended that the Fund be registered in South Africa, for four reasons: (1) Registration in the same country as ORASECOM supports ease of contract administration between the Fund and ORASECOM (management contract). (2) The Fund will be managed by a Fund Manager employed and located within ORASECOM – such management will be complex if the Fund is located in another country (foreign account, transactions management, contracts management, etc). (3) Of the four member states, South Africa has the longest and most extensive legal history of trusts and charitable companies, with significant precedence supporting confidence in the legal regime and associated fund governance. (4) Many partners and funding institutions (private sector and non-governmental) for the Fund are situated in South Africa, given that the majority of the water use within the Basin is in South Africa. Accordingly, registering the Fund in South Africa reduces transaction costs and provides taxation benefits to potential funders.

3.5 Conclusion of the legal form analysis

An extensive analysis of the most appropriate legal form and legal location of the Fund has been described above. This analysis, combined with stated preferences of key stakeholders within the Basin suggest that the ORASECOM Conservation Fund should:

- Be registered as a charitable company
- Be registered in South Africa,
 - according to Section 21 of the Company's Act

4 Institutional Arrangements

4.1 Institutional linkages with ORASECOM

A key consideration is the institutional-organisational form of the Fund and its relationship with ORASECOM. The legal form analysis above demonstrated that the Fund should be established as a separate entity (rather than established within ORASECOM).

4.1.1 *Institutional models for the Fund*

Three institutional-organisational arrangement options are available (Figure 2):

1. A separate entity is established for the Fund, with its own Governing Board, its own executive management and its own staff and systems. This model is appropriate where the Fund will be assuming a significant amount of risk (through financial management, project and contracts management, etc) and where that risk both needs to be ring-fenced within a separate entity (i.e. risk should not be transferred to ORASECOM) and that entity is able to control its risks by retaining control of its functions (i.e. does not outsource any functions that are central to managing the risk).
2. The Fund establishes its own, independent Board and appoints a Fund Manager (CEO), but makes use of some of the staff, services and systems of ORASECOM (for non-core functions). This model is appropriate where the Fund needs to retain some core functions in order to manage risk, but can outsource various (non-core) functions to ORASECOM to achieve economies of scale, implement cost savings and access established ORASECOM systems.
3. The Fund has a management contract with ORASECOM, with the Fund Board outsourcing all functions except strategy and corporate reporting (i.e. the Board retains control over strategic direction and Fund strategy and for reporting on the Fund). This model is appropriate where the Fund functions and Fund risks are intricately associated with those of ORASECOM, and where overlapping mandates suggest that other institutional models would result in duplication of functions resulting in increased cost and reduced efficiency (and possibly efficacy). The Fund Board has only limited control over implementation of the Fund strategy, including the management of investments, disbursement and contracts (the Fund Board however is ultimately accountable for these functions). Accordingly, to ensure that the Fund Board is not exposed to unacceptable risk, shared responsibility with the ORASECOM council and confidence in the outsourced functions will be required.

A comparison of these institutional models (Table 6) enables an assessment of the most suitable model for the specific circumstances of the OCF.

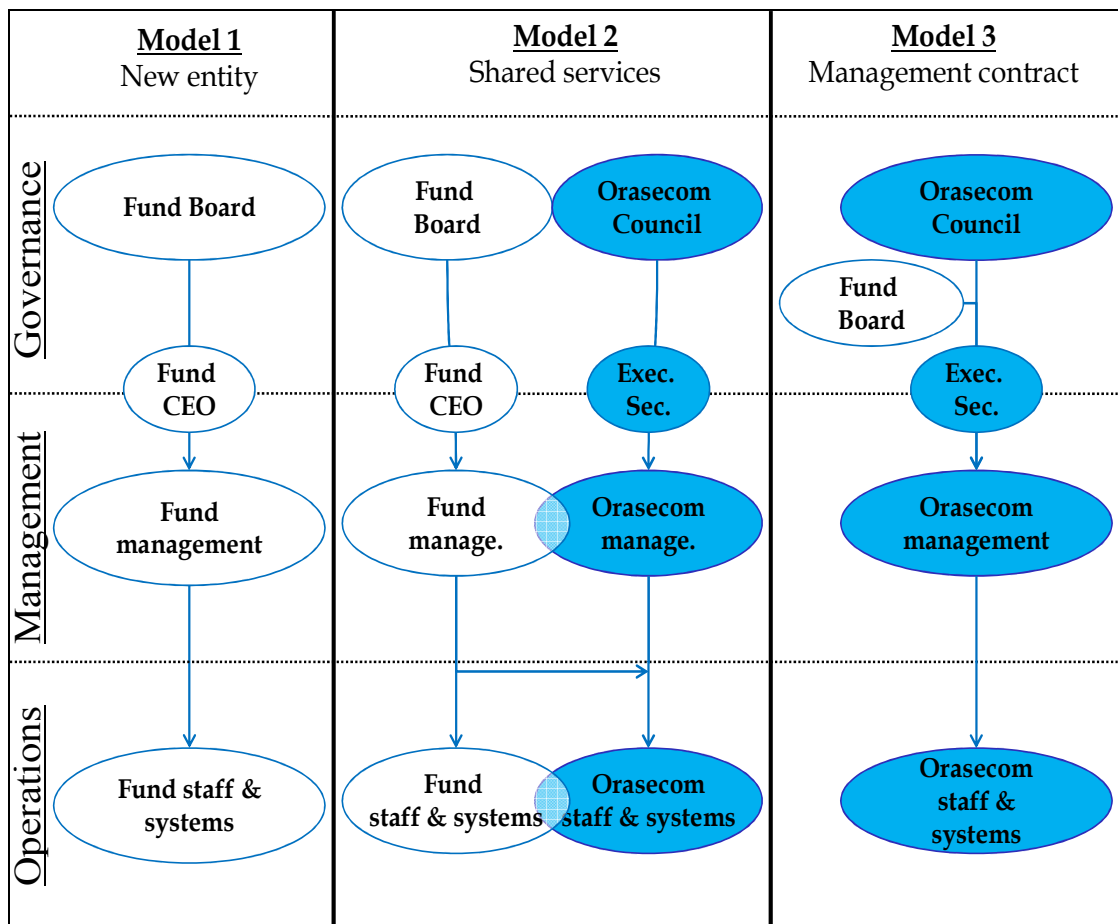


Figure 2: institutional / business model options for the Fund

Table 6: comparison of institutional models for the Fund

MODEL 1: SEPARATE ENTITY	MODEL 2: SHARED SERVICES	MODEL 3: MANAGEMENT CONTRACT
Linkage to ORASECOM strategy and activities		
Linkage would have to be established through MOU or similar legal mechanism.	Linkage would have to be established through MOU or similar legal mechanism, although sharing of services implies closer relation than model 1.	Close relationship – Fund strategy closely linked to ORASECOM strategy through joint strategy formulation and implementation
Perception of independence		
Can be perceived as most independent, as no association with any other institution. However, may be difficult to brand and market the Fund, as a new institution has no track record.	Mixed perceptions of independence, as sharing of services align the Fund with ORASECOM. This can be positive, as the Fund can associate with the track record (brand) and credibility of ORASECOM.	Most closely aligned of the three models, and therefore sense of full independence can be undermined. However, because the mandate of the Fund is closely linked to that of ORASECOM, this institutional linkage can be of benefit and the Fund can associate with the brand and credibility of the ORASECOM.
Ring-fence risk		

MODEL 1: SEPARATE ENTITY	MODEL 2: SHARED SERVICES	MODEL 3: MANAGEMENT CONTRACT
<i>Linkage to ORASECOM strategy and activities</i>		
Fully able to ring-fence and control risk.	Slightly less control of risk, as sharing of services implies some sharing of risk with ORASECOM. Control over functions and operation of the Fund reduced through service sharing arrangements.	Least ring-fencing of risk of the three options. Board exerts control through the management contract, with day-to-day operational management through ORASECOM. Failure of the host institution may induce failure of the Fund, and <i>visa versa</i> .
<i>Establishment simplicity</i>		
Complex to establish, as a new entity must be established, complete with new staff, systems and structures.	Intermediate complexity, as a new entity is established, although some existing staff and systems of ORASECOM are utilised.	Simple to establish – requires appointment of the board, development of the management contract and recruitment of the Fund manager. Systems and Structure of ORASECOM are fully utilised.
<i>Cost of entity</i>		
Most expensive model, as a full institution must be established, including full administrative and compliance functions.	Intermediate cost – some cost savings through shared services, but some cost duplication.	Cheapest model – management contract utilises the full administrative and compliance capacity of ORASECOM.
<i>Circumstances under which model is most suitable</i>		
When a large, complex Fund is established, that requires a separate, independent identity, the ability to ring-fence risk and to exert tight control over financial risk and governance.	A fund of mixed size – too large to be run by one or two managers, but too small to warrant a fully separate institution. Close association with a “shared services” institution for cost reasons and for strategic alignment reasons.	Small fund with fund management functions implemented by one or two managers. Close strategic alignment with a mandated “sister” institution is required. Cost savings a significant consideration.

4.1.2 Conclusion of the institutional model analysis

The analysis of institutional models, combined with the understanding of the OCF gained through the preceding chapters, suggests that a phased approach (institutional evolution) should be considered, starting with Model 3. In the first instance, it is appropriate that a management contract arrangement with ORASECOM be concluded, given (1) the close alignment of the OCF and ORASECOM, (2) the need to manage costs, (3) the anticipated small size of the OCF initially, and (4) the advantages of linking the Fund into the ORASECOM brand.

As the Fund grows and its functions expand, so moving the institutional model to Model 2, and ultimately to Model 1 may be appropriate. Importantly, starting at Model 3 does not preclude this evolution, but creates a stable “incubator” environment for the development of the OCF.

4.2 Institutional arrangement with other institutions

Figure 3 illustrates the main institutional relationships that will impact on the strategic and operational life of the Fund.

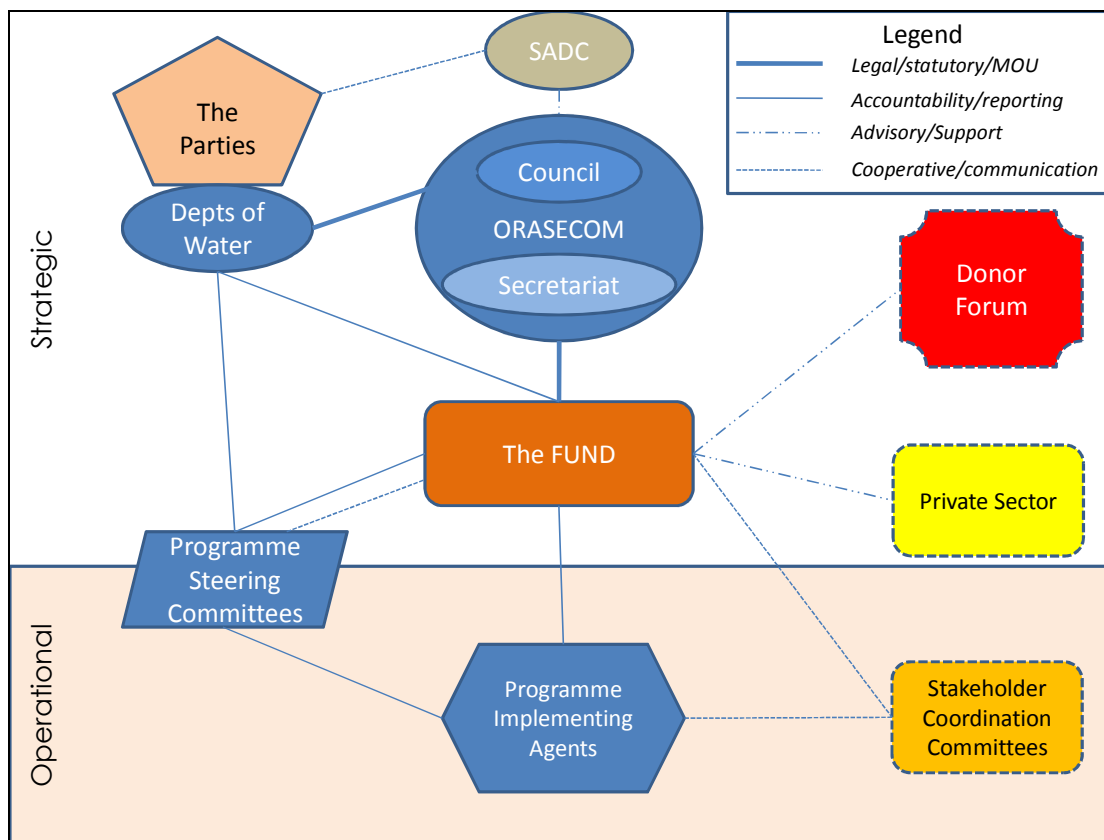


Figure 3: institutional Arrangements for the Fund

It is proposed that the Fund will be a separate legal entity that is run by a Board of Trustees or Directors. These Directors/Trustees will represent, at the very least, the interests of ORASECOM and the parties to the ORASECOM agreement (via each country's Department of Water).

The thick lines above represent legal or statutory relationships – as in those resulting from an MOU or contract between the parties. ORASECOM is governed by the parties, and exists by virtue of their agreement. The Fund will be controlled by its Board, and not by ORASECOM. However it will be necessary for the Fund to enter into a formal MOU with ORASECOM, to ensure that the Fund's strategy is nested in the broader ORASECOM strategy.

Higher up in the diagram one can see the relationship with SADC. The parties are expected to communicate with SADC regarding developments in ORASECOM, and SADC may advise ORASECOM on appropriate strategy. However there is no requirement for ORASECOM to conform to SADC policy.

The Fund will be accountable to its Board. Apart from representatives from the parties and ORASECOM, there may also be board representation from donors, the private sector, and NGO's operating in the basin. At the very least, there should be some advisory relationship with these parties to ensure that the Fund is cognisant of issues important to these entities.

It is proposed that donors should form a 'forum' of some kind to represent their interests in the Fund, rather than the Fund having to deal with donors separately.

A number of different management arrangements are proposed below. A broad picture sees the parties or the Fund appoint a project implementing agent (PIA) to oversee projects. This PIA will report to a Project Steering Committee (PSC) that is normally made up of the parties affected by the project, along with the Fund's representative/s. In some cases, where the parties have not assigned responsibilities to the Fund, the PSC will report to the parties directly. In others they may report to the Fund.

Provision is made for Stakeholder Communication Committees. These may be forums provided for local stakeholders to coordinate their engagement with the Fund around particular projects in the Fund's stable.

5 Fund Governance

5.1 Good governance

The King Committee proposed seven key characteristics of good corporate governance:

1. *Fairness*: all the decisions taken in the operation of Fund should be impartial and every attempt should be made to ensure that all the stakeholders receive fair treatment from the organisation.
2. *Transparency*: is essential for the Fund, since one of its main objectives is to ensure funder confidence. Therefore the information presented to the relevant stakeholders must be accurate and timely, while being sensitive to information that may come under public scrutiny.
3. *Accountability*: the Fund is accountable to shareholders through the Governing Board. Management of the entity is accountable to the Board. Governance mechanisms and procedures must be established to enable assessment of management and the Governing Board of the Fund, built on appropriate performance assessment frameworks and reporting.
4. *Responsibility*: the Governing Board and management of the Fund will have clearly stated roles and responsibilities, which will be reflected in the memorandum of association and board charter (company) / trust deeds (trust) and the terms and requirements of employment. This will ensure that the entity's objectives and mandate are achieved as effectively and efficiently as possible.
5. *Discipline*: the parties that will manage and operate the Fund should be committed to adhering to proper conduct and corporate governance principles.
6. *Independence*: the Fund board and management should be independent in their decision-making and act with integrity, in the best interest of the entity and its key stakeholders. There should be no undue political interference, or any other form of interference, in the entity's decision-making or execution of its mandate.
7. *Social responsibility*: the Fund should be aware of broader social and environmental issues facing the Basin, and the impact that poverty has had on the basin's socio-economic context. The entity should contribute to social upliftment and broader economic development for all the basin's citizens.

5.2 Governing body

5.2.1 Purpose

Regardless of whether a trust or a charitable company is formed, they will both be governed by a Board (of Trustees or Directors). The purpose of this governing body is to ensure that the trust/company is steered in the direction intended by the Founder of the trust (or founding members of the company).

The Board is the accountable authority of the Fund. As such, the Board is ultimately responsible for good governance in the Fund, is the custodian of the strategic plan, and is responsible for the affairs, the governance and management of the Fund, including

performance and service delivery. As the accountable authority, the Board has fiduciary and governance responsibilities.

The fiduciary duties of the Board require that the Board assumes custodianship of the assets and records of the Fund, and that the Board acts in the best interests of the Fund in managing the financial affairs of the OCF. The Board is required to maintain fiduciary oversight, to ensure effective, efficient and transparent systems of financial and risk management, and to keep full and proper financial records to facilitate the internal and external audit of the OCF.

The Board must provide leadership and must retain full and effective control over the direction and performance of the Fund. A key element of control is the management of risk. The Board must ensure that risk is adequately understood and that all necessary measures to manage risk are implemented.

In line with the principles of leadership and good governance, the Board must provide strategic direction to the Fund, develop the business strategies and policies, ensure good governance through appropriate systems and controls, provide guidance and advice to the executive management, monitor and review the performance and service-delivery of the OCF, and ensure compliance with all relevant laws, regulations and codes of business practice.

The Board is accountable to shareholders through a chairperson, who leads the Board and facilitates communication with the shareholders.

5.2.2 Code of conduct

Trustees or directors may not act beyond the objects of the trust or company (as set out in the memorandum of association or Trust Deed), or beyond the limitations placed on their powers by legislation or by common law. Trustees or directors stand in a 'fiduciary' relationship to the company: trustees or directors must use their position and exercise their powers in a *bona fide* manner in the interests of the trust or company and not place themselves in a position in which their personal interests conflict with their duties.

Trustees or directors may not act arbitrarily, capriciously or for an improper purpose. Trustees or directors must exercise an independent discretion and may not fetter their discretion. Further, if a trustee or director fails to exhibit in the performance of his or her duties that degree of skill which may reasonably be expected from a person of his or her knowledge and experience, the trustee or director may be liable to the trust or company for any loss it may suffer.

5.2.3 Composition

Board composition should be a mix of governmental and non-governmental representatives, and board size should be a compromise between adequate representation and efficiency in decision-making. Board composition should be in the majority non-government, with some key government *ex officio* positions to represent government interests. Civil society should be represented, as the Board should be responsive to the needs and concerns of NGOs and community groups. However, representation should be such that the Board is not pulled in too many directions by a wide range of constituencies with conflicting interests. Similarly, representation should be of such a nature that it makes provision for representation that is beneficial to the OCF. Representation of the private sector is useful, as the private sector

often have experience serving on boards, bringing a high level of financial expertise, and as the private sector may be an important donor to the Fund.

As a Section 21 Company, OCF must have at least seven members. As a Trust, OCF has no limit to the amount of trustees selected. These members may be natural or juristic persons, representatives, nominees, foreign citizens or other institutions, such as government departments.

Based on this purpose and functions of the institution, and the governance requirements, it is recommended that the OCF's Board consists of between 5 and 11 trustees or directors, comprise of representatives of:

- Departments of Water Affairs of the Member States;
- The ORASECOM Executive Secretary;
- Donors, selected through the donor forum;
- Private sector, selected through the stakeholder committees; and
- Civil society; selected through the stakeholder committees.
- The fund manager (Fund CEO where applicable) should attend board meetings, but in a non-voting capacity.

Based on the purpose and nature of the institution, the following competencies must be represented on the board:

- Understanding of water related conservation issues in the basin and beyond;
- Understanding of mitigation measures – technical and non-technical;
- Understanding of the donor environment, accountability and credibility to donors;
- Legal and compliance competency;
- Financial competency and some knowledge of fund management; and
- Human resource competency.

5.2.4 Nomination

Board selection should be through a participatory approach, with good representation by the Fund's beneficiaries, government, donors, and private sector, to ensure that stakeholders have confidence in the OCF board. As these groupings are represented on the OCF board, it is recommended that the board chairperson convenes an *ad hoc* board nominations committee that will provide oversight of the nominations process and will make recommendations to the board regarding short-listed nominees. The nominations committee is supported in the nominations process by the Fund Manager and ORASECOM management. Invitation to the board should be through a collective board process.

5.2.5 Tenure

Board tenure should be considered to enable sufficient time for implementation of strategy, but also adequate turn-over to enable the introduction of new ideas. Consistency between one board and the next should be ensured by retaining a critical mass of board members and through good induction processes.

It is recommended that the OCF implement a tenure of three years, renewable twice, and that at least one quarter (3 members) of the board be changed each term.

5.2.6 Management of the institution

The board should establish its own proceedings, in line with the requirements of the trust deeds / memorandum of association. These proceedings will include quorum, adjournment,

voting, board delegation, recording of minutes, resolutions, and the appointment of committees and committee chairs.

5.3 Strategy development

The purpose of the Fund is clearly located within the broader purpose and mandate of ORASECOM and of the member states. Accordingly, the Fund's strategy is a nested strategy, reflecting the strategic direction provided by the overarching ORASECOM strategy (the Basin Wide Plan) and the respective strategies of the member states. It is recommended that the OCF strategy be based on priority conservation issues and basin interventions identified through the ORASECOM Basin Wide Plan (which necessarily must take cognisance of the national strategies of the member states). The OCF strategy builds on these priority issues and develops the funding and implementation strategy, including project and contract management.

A strategic planning process that is closely aligned with that of ORASECOM and reflects the strategic objectives of ORASECOM, the member states and mandated national institutions is required. The strategic plan of the Fund must reflect that of ORASECOM, which in turn reflects the strategic intent and objectives of the member state. Accordingly, a step-wise planning process is required.

Strategic planning is a critical area for stakeholder involvement, and structures to ensure that the strategy reflects stakeholder perspectives are required.

5.4 Fund management

5.4.1 Management arrangements

In essence, four management arrangements for the identification, funding, disbursement and management of priority conservation projects can be identified (Figure 4). The management arrangements are driven by two key considerations: (1) the source of funding and (2) assignment of the functions and, therefore, the responsible authority. Any one (of these arrangements is appropriate for the Fund, and it is likely that across its projects, the OCF involvement will follow all four options (i.e. all four management arrangements taking place concurrently). This has significant implications for organisational design, skills requirements and financial management of the Fund.

- *External funding with function not assigned (A)*
The ORASECOM makes a recommendation to the party(ies) regarding a priority conservation project, with a recommendation on finance (funders). However, the party(ies) do not assign the function to the ORASECOM, but rather retain the function. The Fund manages funding for the project on behalf of the parties, who in turn conclude contracts with the implementing agents (PIA) for execution of the project. ORASECOM / OCF may be represented on the project steering committee (PSC), but this structure is convened by the client on the project, namely the party(ies). Financial accountability, contract management and monitoring / reporting follows the financial flows described above.
- *External funding, with function assigned (B)*
In this case, ORASECOM makes a recommendation and the party(ies) assign the implementation function to the ORASECOM and the OCF. The OCF therefore source the funding from donors and concludes arrangements with PIAs. The Fund convenes the PSC, although the party(ies) must be represented on the PSC. As with (A),

financial accountability, contract management and monitoring / reporting follow the financial flows.

- Party funding, with function assigned (C)**
As with (B), ORASECOM's recommendation is followed by assignment from the party(ies), but in this case the party(ies) provide funding along with the assignment. Funding flows from the party(ies) through ORASECOM to the OCF. The OCF concludes arrangements with PIAs and manages contracts, disbursement, and project monitoring and reporting. The PSC has representation from both ORASECOM / OCF and the party(ies). As with (A), financial accountability, contract management and monitoring / reporting follow the financial flows.
- Party funding, with function not assigned (D)**
This arrangement is similar to (A) above, in that ORASECOM makes a recommendation to party(ies), with the parties implementing the recommendation. In this case, however, the ORASECOM / OCF recommends that the party(ies) finance the initiative. The party(ies) manage the contract with PIAs and convene the PSC. The ORASECOM may have representation on this structure. As with (A), financial accountability, contract management and monitoring / reporting follows the financial flows.

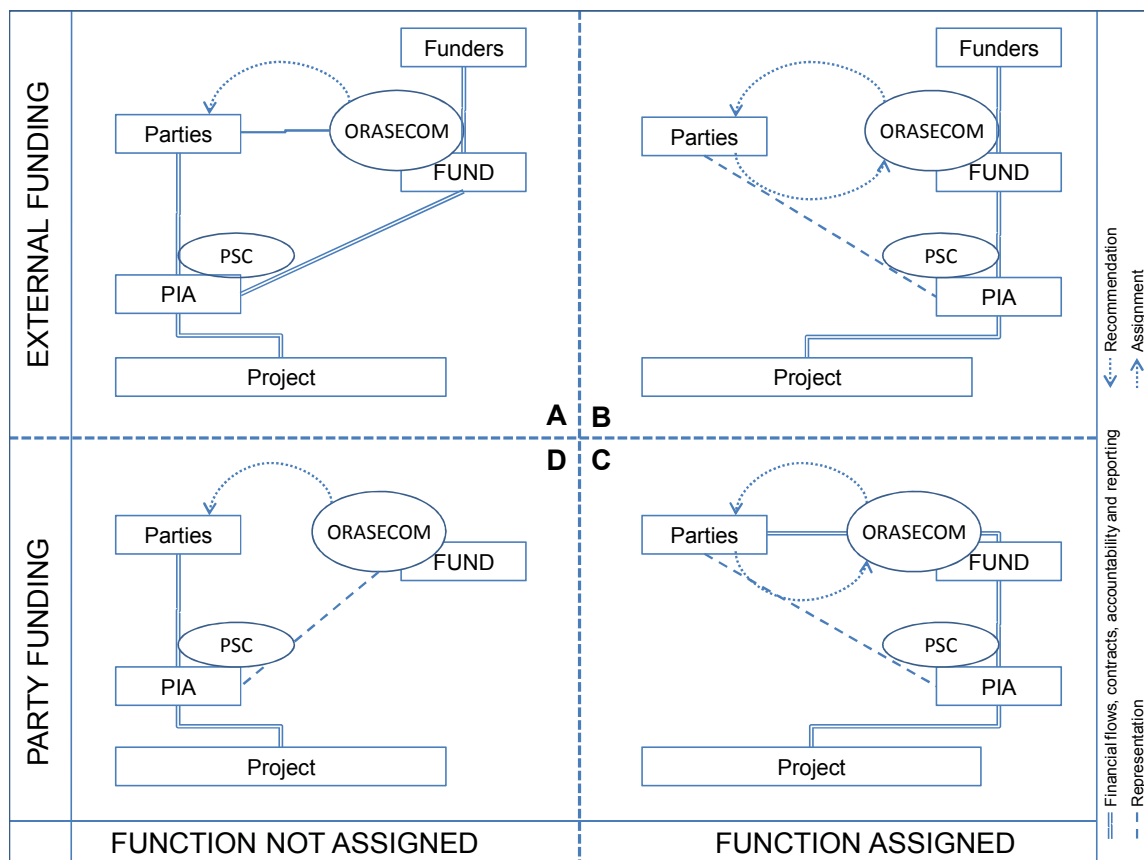


Figure 4: management arrangements for the ORASECOM fund

5.4.2 Fund manager

The Board is responsible for appointing the Fund manager, although if a management contract is concluded with ORASECOM, this responsibility rests with the Executive Secretary. The Fund manager must enter into a performance agreement with the Fund on acceptance of his or her appointment.

The Fund Manager is responsible for the implementation of the strategic goals and objectives of the Fund, and for its governance and fiduciary functions. The Fund Manager is responsible for the day-to-day management of the Fund and for the leadership and direction of the OCF management team. The Fund Manager is accountable to the Board (or the Executive Secretary where a management contract is used).

During the establishment of the Fund, the Fund Manager will drive the organisational design and development of the new entity, and strategically manage and coordinate the activities of the evolving Fund.

Specific responsibilities may include:

- Strategic management of the organisation
 - Provides the strategic vision and operational leadership
 - Leads the OCF management team
 - Responsible for structuring programmes and delegating authority
 - Represents OCF executive on the Board
- Establishment of financial management systems and oversight of financial management
- Oversight of infrastructure, facilities and equipment, moveable assets, and development and maintenance of information systems
- Ensure organisational systems and human resources management
 - Initially establish and organisationally develop the SADIS.
 - Ensure and monitor organisation policies and systems
 - Manage the SADIS staff and performance
- Ensure high level of service

The Fund Manager is the public face of the OCF and is responsible for public awareness and public confidence in the deposit insurance scheme.

Significant human resource capacity is required for the Fund, given the significant challenge posed by basin conservation finance initiative, with the various complex institutional, strategic, financial, political and organisational elements to the Fund. In this regard, outstanding Fund leadership will be required, not only to ensure effectiveness and efficiency of Fund administration, but also to ensure ongoing strategic re-alignment, as the strategic direction of ORASECOM, parties stakeholders, beneficiaries, funders and other players changes. A carefully designed job description, recruitment, evaluation and performance management system will be required to ensure access to and retention of the required Fund Manager.

5.5 Governance systems and control

The OCF needs to put governance systems and controls in place to ensure that the King principles of good governance are embedded into the operations of the Fund. Standard systems include the strategic plan, business plan and budget, management appraisal and performance management, the internal audit, and quarterly and annual reporting.

5.5.1 Planning systems

There are 3 main planning tools that are used to ensure good governance – such as accountability, discipline and transparency. These are the Strategic Plan, the Business Plan and the detailed budget.

The Strategic Plan

It has already been emphasised above that the OCF's strategy must be closely aligned with that of ORASECOM. ORASECOM's strategy, in turn, should reflect the strategic objectives of the Parties and their mandated national institutions. Accordingly, a step-wise planning process is required.

The Strategic Plan is normally produced (or updated) annually, covering a rolling three or five year period. It is the responsibility of the Board and is meant to provide the Executive with high level direction and with Key Performance Areas or Indicators. Given the need for alignment with ORASECOM, the planning process should commence once ORASECOM's annual planning process is near completion. An alternative may be to run the two planning processes in parallel.

Strategic planning is also a critical area for stakeholder involvement (in line with the governance principles of transparency and responsibility), and structures to ensure that the strategy reflects stakeholder perspectives are required. These normally take the form of workshops and other forums where stakeholders are able to comment on current strategy and provide input on their desires.

Once the Strategic Plan has been completed and adopted by the Board, it is passed on to the Executive where it forms the basis of the Business Planning process.

The Business Plan

The Business Plan is similar to the Strategic Plan, in that it is normally updated on an annual basis and covers a period of 3 to 5 years. However it is more operational than the Strategic Plan, in that it provides the detailed programme information required to implement the Board's strategies.

The Business Plan will also contain another level of detail with regards to budgets and sources of funds.

Annual budgets

Both the Strategic and Business Plans will contain budget information. The CFO will need to take this information and break it down into the detailed cost and revenue centres. The managers of each cost and revenue centre should then be given the responsibility to monitor these budgets against actual costs on a monthly basis.

Rules should be put in place regarding budget variations and the need to identify the causes of these variations, as well as the impact of these variations on the expected annual surplus/deficit. Significant variations from the budget will need to be escalated up to senior management and the Board if adjustments are going to be required to programmes and/or strategy.

5.5.2 Management appraisal and performance management

The Balanced Scorecard is an example of management appraisal and performance management. It is meant to provide a relevant way for assessing achievements by linking performance measurements to four key business perspectives: internal, customers, innovation and learning, and the financial perspective. The focus is on a few key measures to evaluate performance and cascade the overall strategies through the organisation. The scorecard links intangible with tangible assessment factors and is an important element of an acceptable review and appraisal system.

Executive rewards should be determined in relation to the performance contracts signed between them and the OCF. These contracts take into account the Key Performance Indicators of the OCF's business plan. To ensure that individuals put maximum effort into their roles the following should be in place:

- Executives should sign performance agreements with annual targets and review periods,
- There should be clear definition of objectives, responsibility and expectations,
- Effective measurement and monitoring systems should be put in place,
- Performance-linked remuneration would ensure improved individual and entity performance, and
- Sanctions for sub-standard performance should be spelled out.

5.5.3 External and internal audit

The Companies Act requires all companies to be externally audited on an annual basis. Trusts are not required to be audited, however good corporate governance recommends that companies (and trusts) subject themselves to regular internal and external audits.

External audit

The Fund should subject itself to an annual external audit – even if it is a trust. External audits focus on the presentation of financial information – usually the annual financial statements. Generally Accepted Auditing Standards require that the auditors perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. It also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

Internal audit

The internal audit process is often on-going – as opposed to the annual external audit. Its purpose is to assess the internal controls of the organisation and to ensure that they are operational and effective. There is therefore a strong emphasis on measuring compliance with the entity's policies and procedures.

Internal auditors either produce an annual report, or meet with management and the Board on a regular basis to advise on changes required to internal controls and systems.

5.5.4 Reporting

An important governance control is to ensure regular reporting of management and financial information.

Annual report

The primary source of information for the public is the Annual Report. It contains the annual financial statements, produced in accordance with Generally Accepted Accounting Practice, as well as supplementary information such as narrative reports from the Board Chairperson and the CEO.

It is often used as a promotional document, but also serves the purpose of keeping stakeholders informed of the organisation's financial position, performance and future direction.

Quarterly report

While the annual report generally has an external focus, there is a need for more regular reports to be submitted to the Board and to management. The CEO and other senior management must receive financial and management accounts on a monthly basis. The Board, which should be meeting at least on a quarterly basis, should receive unaudited quarterly reports that detail the financial performance and position of the Fund, as well as performance against budget. The quarterly report should be accompanied by a narrative report from the CFO, detailing any variances and other relevant information.

The Board may delegate queries relating to the quarterly reports to a Board committee such as the Audit committee; however the whole Board should take responsibility for examining the quarterly reports.

6 Organisational and HR considerations

Organisational design for the OCF is heavily dependent on the institutional-business model adopted (Figure 2), the extent of project implementation by the Fund (Figure 4) and the resources that the Fund will be able to generate. Accordingly, this section of the business case will assume a simple structure for the Fund, with possible evolution into a more complex structure as the Fund matures and workload increases.

6.1 Functional description

The first step in the organisational design process is understanding the functional requirements of the Fund. These functions do not equate to organisational positions (HR requirements), with several (all) functions performed under one position initially. Over time, as the Fund grows and its project load increases, organisational structuring based on functional distinction may be required.

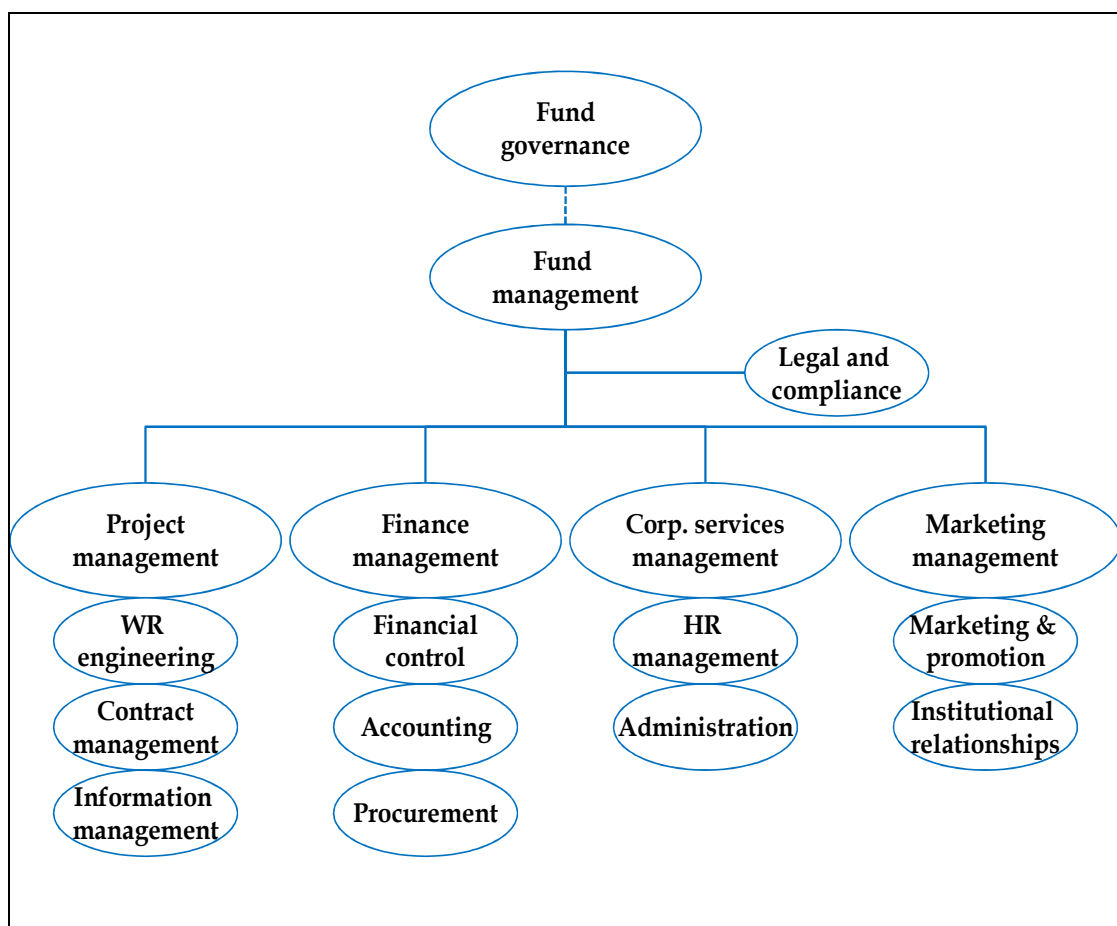


Figure 5: high-level functional description for the Fund, assuming some implementation of conservation projects

The high-level functional structure is built on the following elements (Figure 5):

- *Fund management*: functions related to implementing the strategic direction of the Board, and day-to-day management of the institution
- *Legal and compliance*: functions related to governance and legal issues for the Fund, management of risk and strategic support to the Fund Manager
- *Project management*: functions related to the identification, development and implementation of priority projects
 - *Water resources engineering*: identification of priority conservation projects, assessment of appropriate mitigation responses / initiatives
 - *Contracts management*: initiation and management of contracts with implementing agents, including tendering and evaluation
 - *Information management*: management of all information related to priority projects, link into information management in ORASECOM and member states
- *Finance management*: functions related to financial management, investment and income, accounting, budgeting, reporting and management of financial risk
 - *Financial control*: daily management of financial affairs of the Fund, including investment and income, disbursements, etc.
 - *Accounting*: daily bookkeeping and accounting, budgeting financial reporting
 - *Procurement*: all procurement functions for the Fund, except project procurement
- *Corporate services management*: functions related to the full range of corporate services for the OCF
 - *HR management*: human resources recruitment, human resources management (HRM) and human resources development (HRD)
 - *Administration*: full range of administration functions for the Fund, including document administration, support services, etc.
- *Marketing management*: a key function for the Fund, particularly whilst fund-raising from donors remains an important income stream – responsible for all elements of marketing and fund-raising
 - *Marketing and promotion*: fund-raising through development of appropriate marketing and promotion material, scoping opportunities and packaging proposals
 - *Institutional relationships*: management of relationships with shareholders and key stakeholders, and development of partnerships with allied and complementary institutions

This functional description assumes that the Fund will be implementing some project (B or C in Figure 4), while it will be sourcing funding for others (D) and routing funding for yet others (A). It is important to recognise that if this assumption is true, then the functions described here will be required, irrespective of the institutional-business model of the Fund (Figure 2).

6.2 Organisational structure

Based on an understanding of the early Fund as a small entity, with relatively limited resources and small project load, an early Fund structure can be developed (Figure 6). This structure is built on the assumption that the early Fund will conclude a management contract with ORASECOM, and that ORASECOM will employ a Fund Manager to implement that contract, accountable to the ORASECOM Executive Secretary, but also reporting to the OCF

Board (together with the Executive secretary). The Fund Manager will be responsible for all of the functions described above.

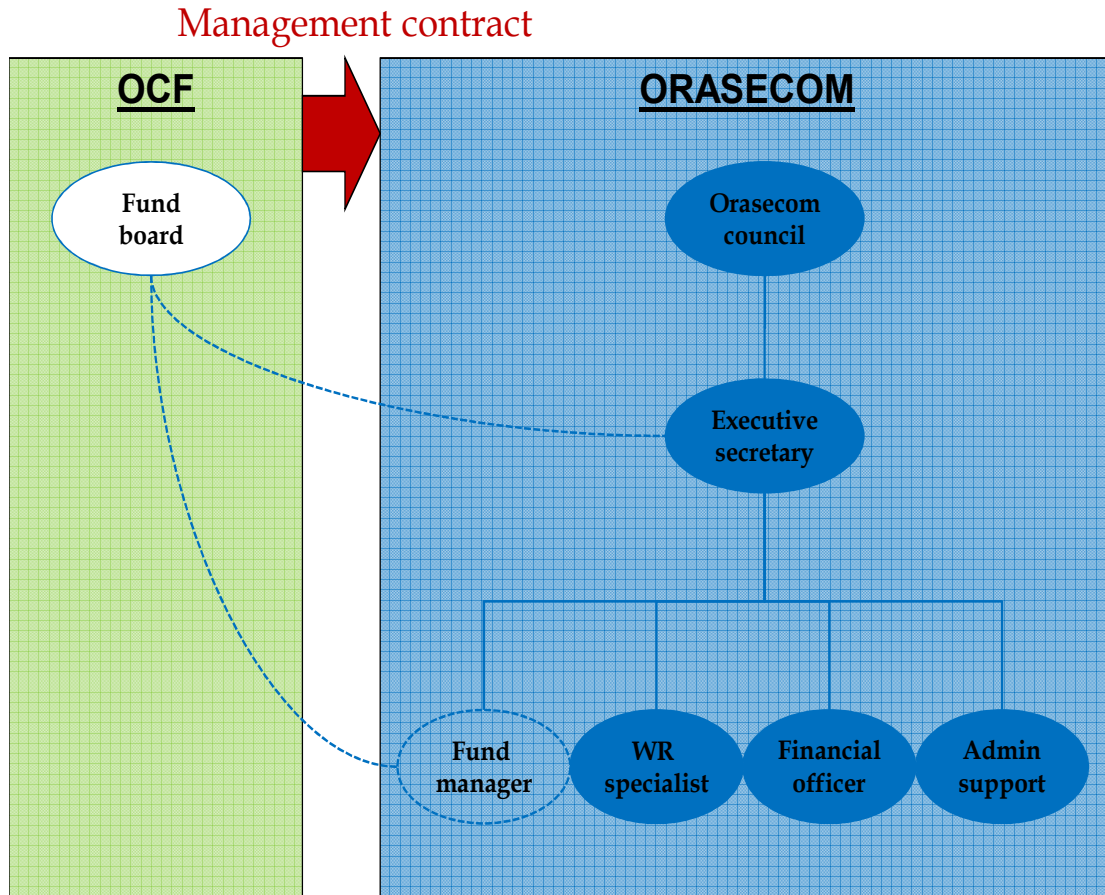


Figure 6: initial organisational structure for the OCF, based on a management contract between the Fund and ORASECOM

As the workload in the functional areas expands, linked to increasing access to resources and increasing assignment, so more staff may be required and the institutional-business model for the Fund may change.

7 Financial considerations

7.1 Financial arrangements

Financial arrangements describe the flow of funds through the OCF (Figure 7).

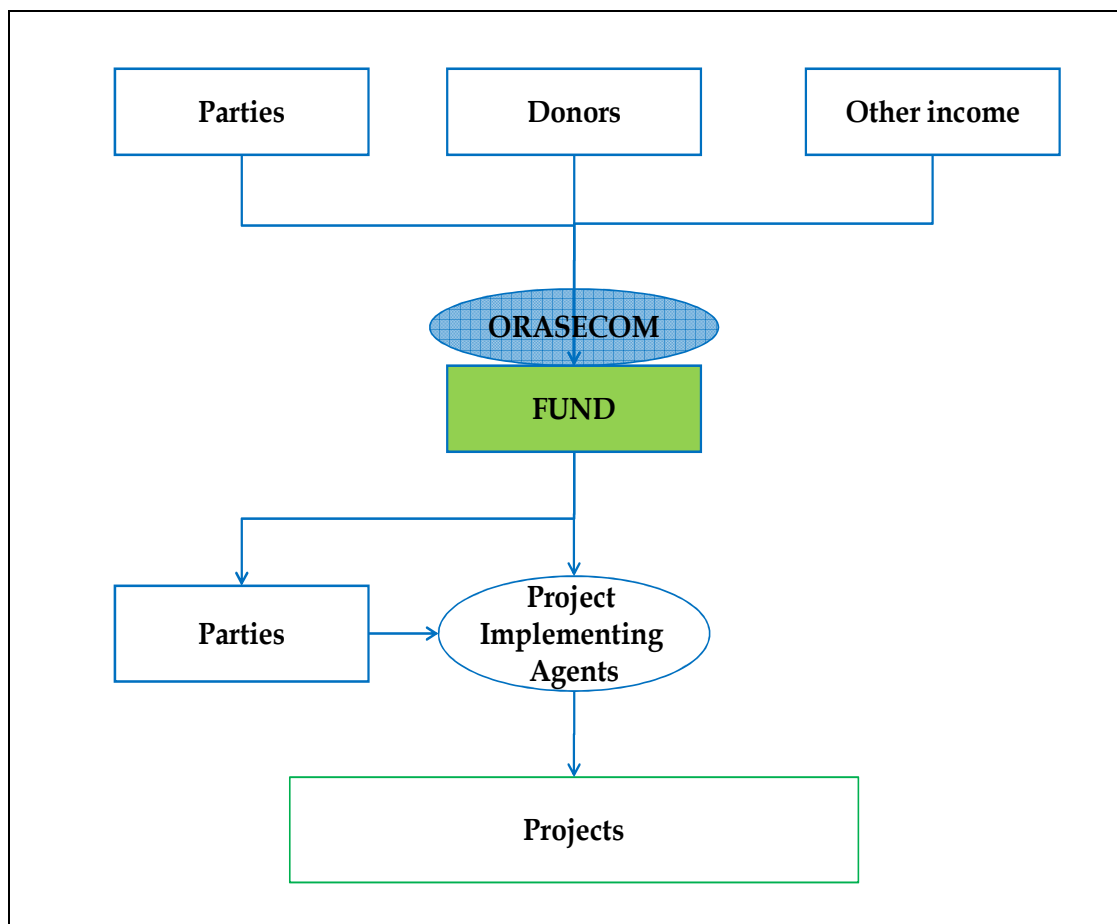


Figure 7: financial arrangements for the Fund

Sources of finance may include a combination of party contributions, donor funds and other sources such as investment income and user charges.

The Fund, apart from holding some of the funds back to cover its overhead costs, then has two alternatives for distributions, reflecting the management arrangements described in Figure 4. The first is to distribute to the Parties, for them to spend on projects (via disbursement to Programme Implementing Agents). This is likely to be the case where the Parties have not assigned responsibility to the Fund, and instead prefer to retain control over the projects. Contractual arrangements between the Fund and the parties governing this transfer of funds will be required. The second alternative sees the Fund disburse funds to the PIA's, reflecting a contractual arrangement between the Fund and the PIA.

7.2 Financial requirements of the Fund

See Mitigation Measures Assessment Report for details of the costs of selected mitigation measures.

7.3 Cost of the OCF

The cost of the Fund is largely going to be determined by the role the Parties require it to play. The most cost-intensive model is where the Parties assign responsibilities to the Fund, and the Fund implements the projects through contracts with Programme Implementing Agents. Staffing is then required to manage the projects, as well as manage the pool of funds received from Parties, donors and other sources. On the other end of the scale, a limited number of staff (and overheads) are required if the Fund is only going to play a financial facilitation role, where it links projects to Parties to donors, without the funds flowing through the Fund. The Parties retain control over the projects and over the related financing thereof. The Fund's role is then limited to facilitating the project initiation, ensuring that projects are coordinated, and playing an advisory role on the project steering committees.

As described in the previous chapter, the OCF will initially only consist of a Fund Manager, with all support functions performed by ORASECOM. All four management arrangements for the Fund (Figure 4) can be implemented through this organisational structure, with the Fund manager assuming the range of functions outlined in Figure 5.

7.3.1 Cost-model assumptions

The OCF will initially consist of a Fund Manager, with all support functions performed by ORASECOM. It is assumed that ORASECOM will need to scale up its capacity for its own purposes and should therefore be able to cope with the demands of the Fund as and when needed.

7.3.2 Establishment costs

Establishment costs are estimated to be in the region of R210, 000. These are primarily the recruitment costs of employing the Fund Manager (R180, 000 – being 20% of the annual salary cost plus the cost of drawing up the employment contract). Another R40, 000 may be required for setting up the workstation (furniture, computer, networking, stationery, etc.)

7.3.3 Operating budget

The operating costs of the OCF cover the salary and related overhead costs of the Fund Manager. These are estimated to be in the region of R1.6m per year. Any project related costs will be on a 'variable cost' basis in that they will only be incurred where they are covered by specific funding.

No budget is provided for outsourcing costs. It is expected that ORASECOM will provide management services related to finance and administration on a no-fee basis.

7.3.4 Cost summary

Table 7 provides a summary of the costs expected in the first few years of operation.

Table 7: summary of costs for the OCF

Budget	2010/11	2011/12	2012/13
Board Costs	R 464,584	R 330,673	R 347,206
Staff Costs	R 651,667	R 848,925	R 891,371
Overheads	R 169,597	R 484,120	R 508,326
Outsourcing	R -	R -	R -
Establishment	R 217,785	R -	R -
TOTAL COSTS	R 1,503,632	R 1,663,718	R 1,746,903

7.4 Sources of finance

There are four broad sources of finance open to the Fund. These are discussed in more detail below.

7.4.1 Contributions from the Parties

These may be from the Parties' general tax revenue, or could be from specific taxes collected. Party finance may be ongoing finance as part of an annual allocation to mandated government institutions, or may be once-off programme finance for specific conservation initiatives that support party objectives.

The Parties have fiscal resource limitations and this may constrain the amount of money that can be allocated to transboundary conservation initiatives, except where these are aligned with national strategic priorities. Where these objectives are aligned, countries may be resistant to allocating money to the OCF for implementation at a transboundary level, rather than implementing the intervention at a national or catchment level. The exception to this is where joint intervention between countries is imperative for effective implementation or it is viewed as a transboundary flagship project.

In summary, government (party) financing can be expected to cover:

- institutional operating costs,
- transboundary flagship projects and
- catchment initiatives recommended by the OCF but implemented under the auspices of a national or catchment institution.

7.4.2 Donor Funds

The second source is donor funds. This includes all money provided by external institutions, including cooperating partners (donors), private sector and non-governmental groups. This may be directly into the OCF or to an implementing agent on behalf of the OCF. The important element is that these grants need to support activities that are consistent with the transboundary priorities and objectives. Cooperating partners are already providing significant funding to ORASECOM projects, but this may be translated into some level of basket funding under the direct control of the OCF. Private sector and civil society organisations provide a potentially untapped source of donations that may be relevant with the increasing public and corporate recognition of the importance and vulnerability of water resources.

In summary, grants and donations are likely to be the largest source of funding (initially from cooperating partners, but then potentially from private sector and nongovernmental organisations), at least in the next few years as the OCF establishes itself within the basin.

7.4.3 Investment income

Funds often generate passive income by virtue of sitting on a large pool of capital. Returns from investments will be significant in the case of an endowment fund, and may still be significant – especially in the early years – for a sinking fund and a capital fund. Large endowments allow funding to be made from interest (or other investment) income on the capital. However gaining this level of endowment initially is unlikely, particularly in the current financial climate.

The Fund could contain a revolving element, which would see cash flows generated from interest income on the loans as well as repayment of the loans themselves. This would suit specific interventions that have relatively quick payback periods (such as water loss control in urban areas), with savings or local tariff income covering debt repayment, which then becomes available for further loans. However these types of projects should be supported by PPPs and other government or private financing. They should only be considered by the Fund if they contain a transboundary element which makes government or private finance too complex or unattractive for private finance.

7.4.4 Charges or taxes

Non-investment income may include tariffs, user charges, levies, earmarked taxes (applied to water users or property), payment for environmental services schemes, carbon and biodiversity finance, patents, and sale of goods and services. These options are not likely to feature as a source of finance in the short to medium term. Typically, these charges must be legislated (empowered) at a national level and require fairly sophisticated financial management systems to ensure payment, which restricts the likelihood of direct charging and collection at a transboundary (OCF) level. Dedicated basin-wide management or pollution charges would require aligned legislative processes to enable them, which is logistically and politically unlikely. Joint infrastructure charges have and can be applied to cover the costs of infrastructure development and operation, but are unlikely for more localised infrastructure. It is also clear from the review of financial requirements that the Fund should not be servicing projects that are eligible for private sector or government finance. Infrastructure projects that generate returns via user charges would fit the category of projects that do not need to be funded by the OCF.

Pollution charges have not been implemented in the riparian states, although South Africa has developed the possibility for a waste discharge charge, which currently does not cater for cross-border impacts. Economic charging (taxes to reflect the value rather than the cost of managing water) has not been developed by the riparian states (although South Africa is exploring this). Users are politically resistant to this type of tax and national treasuries are usually unwilling to earmark this for specific purposes.

Including costs for transboundary conservation initiatives into existing user charges may be considered, but currently payment levels are low and are dedicated to managing local priorities.

Payment for environmental services (PES) may be considered in quite targeted local situations, where beneficiaries pay another group to maintain environmental functioning, but this must be locally negotiated. Alien vegetation removal may be partially funded by beneficiaries of the water (such as South Africa's Working for Water programme), but this currently does not have a cross-border element and has evolved a PES and government financing focus.

In summary, while user charges and taxes may be implemented at a catchment level, they are unlikely to be allocated to transboundary initiatives, except where these align with the local priorities against which the money was collected, while PES systems may be negotiated between local groups even in a cross-border context.

7.4.5 Summary

Given the options discussed above, it seems evident that the OCF can expect to have its institutional costs funded by the Parties, with project costs being funded by donors. The Parties are also expected to contribute to projects, but probably only where these are flagship projects for ORASECOM, or where the funds are channelled directly to institutions in the Party's own country.

Income generated from investments, charges and taxes are expected to be inconsequential or non-existent in the short-term.

7.5 Financial systems

The Fund will initially utilise the financial systems of ORASECOM and will therefore have no need for a separate financial system. ORASECOM will need to maintain separate financial records to allow the OCF to report separately.

The future financial systems of the Fund will depend on the extent of financial intermediation and project management required. At most the Fund's CFO will be responsible for: Fund management, Project management, and administration costs. Fund management is likely to be fairly straightforward, with the Fund likely to adopt a conservative investment strategy. The financial systems will therefore be straightforward, although the governance systems will need to be strong to avoid mismanagement and the risk of fraud.

The financial systems required for project management, if this is undertaken by the Fund, will require the capacity to deal with multi-currency accounting and multi-year work-in-progress accounts. Most standard small business accounting packages now have the ability to deal with this level of complexity. The Fund should therefore not have to invest in a customised financial system.

8 Risk analysis

There are several risks facing the conservation fund, some that are internal to the Fund itself, and which relate to the standard business and governance risks facing any institution, and some which are external to the Fund and are driving by the specific context within which the Fund operates.

8.1 Identification of key risks

- **Insufficient funding:** In the current context of a global financial crisis and the slow-down of economies both internationally and in the basin states, the potential exists that less money may be available for basin management activities than may have been expected. This is compounded by the competition for funding for other purposes in the riparian states, all of which still have some way to go to meet, for example, the Millennium Development Goals.
- **Poor financial management:** In any body managing substantial funds, the potential for poor financial management poses a significant risk. In this case, the Fund will be managing funds obtained from a number of sources, and will need to be able to account to such sources for the effective and productive use of those funds.
- **Poor governance:** Closely linked to the risk of poor financial management is the more general risk of poor governance of the institution. It is envisaged that the Conservation Fund will have a Governing Board, with full fiduciary responsibility. It is important that the members of the Board have, between them, the appropriate capabilities to exercise their full fiduciary and legal responsibilities to ensure good governance of the Fund.
- **Lack of agreement and co-operation between member states:** The Fund will serve, in essence, the four member states of ORASECOM. The potential exists for disagreement between the states on the allocation of funds to projects, particularly where certain projects are seen to benefit specific states and not others. This potential may be exacerbated if the establishment of the Fund is seen to divert funding possibilities away from the individual states to a common pool from which they may not benefit to the same extent.
- **Lack of implementation capacity:** There is limited capacity (in the private sector, NGOs and the state) in the four member states to implement some of the work that needs to be done in the basin. While the potential exists to buy in capacity from outside the member states, this must be done within an approach that ensures sustainability in the long term. It is critical that projects that are envisaged are aligned with sustainable and available capacity.
- **Lack of credibility:** The sustainability of the Fund will depend on the credibility not only of the Fund, but of ORASECOM, both within the basin and within the broader donor community. Sustainable, long-term funding will depend on the Fund being seen as credible, and offering good value for money. Lack of credibility will impact negatively on the willingness of donors, stakeholders and states to provide resources to the Fund.

8.2 Risk quantification and management

RISK	IMPACT	LIKELIHOOD	MANAGEMENT
Insufficient funding	High	Medium	Development of a realistic financing strategy; diversification of financial sources; matching of finances to projects
Poor financial management	High	Low	Appropriate determination of required staff capacity; appointment of skilled and experienced staff; development and implementation of good financial management systems; effective monitoring and oversight;
Poor governance	High	Low	Appointment of appropriately qualified/ experienced people to Board; training for Board members; appointment of effective Audit committee; Board performance assessments conducted;
Lack of agreement between member states	Medium	Low	Development of agreed principles and criteria for selection of projects; transparent and inclusive process of selecting projects; dispute mechanism in place; identification of new sources of funding rather than competition with existing sources of funding for member states;
Lack of implementation capacity	Medium	Medium	Tailor projects to existing capacity (state, NGO and private) for implementation; buy in capacity where appropriate and where sustainability can be ensured;
Lack of credibility	High	Medium	Ensure Fund is responsive to the needs of the basin states and stakeholder groups; identify "quick wins" to establish ORASECOM and the Conservation Fund as effective and important players in basin management

9 Implementation considerations

The following key steps are required in taking this process forward:

- Political support for the ORASECOM Conservation Fund from ORASECOM Council, including a mandate to move towards legal and functional establishment
- Initiate the legal and functional establishment process, through a OCF Establishment Project
- Legal establishment of the OCF
 - Select appropriate legal form and location
 - Select appropriate institutional model
 - Draft require legal documentation, including institutional agreements
 - Leading to a legally established entity with clear institutional and management arrangements
- Functional establishment of the OCF
 - Organisational design, including job evaluation and description
 - Organisational policies and systems
 - Financial policies and systems
 - Recruitment of key staff
 - First business plan for the OCF
- Financial strategy for the OCF
 - Sources of funding, focussing on sustainability of the OCF
 - Secure funding
 - Investment strategy developed
 - OCF funding strategy
- Contract development and implementation of first conservation measures

Appendix A

Examples of interventions to priority conservation issues

CONSERVATION ISSUE	POSSIBLE MITIGATION INTERVENTION OR PROJECT	INSTITUTIONAL RESPONSIBILITY	COST IMPLICATIONS
High water demands in municipal centres compounded by poor asset management.	Water Conservation and Demand Management in the town of Kuruman covering: A survey of the current status water services infrastructure. In order to improve asset management, water audits and determination of the water balance, leak repair/ retrofitting programme, pressure logging and possible pressure reduction and consumer awareness	Kuruman municipality supported by RSA DWAF	>R10 million
	Water Conservation and Demand Management in the town of Mafikeng covering: Leak repair/retrofitting programme, pressure logging and possible pressure reduction, consumer awareness and verification of existing irrigation water use.	Mafikeng municipality supported by RSA DWAF	>R10 million
	Water Conservation and Demand Management in the town of Upington around implementation of the existing leak reduction strategy.	RSA Local government	>R10 million
	Support of the Richtersveld COWEP programme which will require partnership with the local community, RSA DWAF, SANPARKS and the local municipality.	SANPARKS, RSA DWAF, RSA local government	<R1 million

CONSERVATION ISSUE	POSSIBLE MITIGATION INTERVENTION OR PROJECT	INSTITUTIONAL RESPONSIBILITY	COST IMPLICATIONS
Repeated releases of non-compliant wastewater effluent across the Orange-Senqu river basin	Support the upgrading of various wastewater treatment works	RSA Local government, RSA DWAF	>R100million
Extensive mining in Witwatersrand mining basin resulting in decant of contaminated mine water from Vaal River system	Collection and treatment of mining decant currently threatening the Cradle of Humankind World Heritage Site, water users, and the Krugersdorp Game Reserve.	RSA DWAF, RSA DME, Mining companies.	>R100million
High return flows (containing high levels of untreated effluent) in Klip river catchment as well as (low pH) mining water pollution	Support of the (on-site) physical rehabilitation of the Klip River wetlands which includes the construction of additional gabions and earth structures to prevent river bank erosion.	Working for Wetlands, RSA Local government	<R1million
	Support of the rehabilitation of the Klip River wetlands by addressing the upstream contamination of wastewater and mining effluent.	Working for Wetlands, RSA Local government, RSA DWAF, RSA DME, Mining companies.	R10million- R100million
	Possible mitigation intervention or project	Institutional responsibility	Cost implications
	Addressing sand mining and removal of spoil dumped in and around estuary	Local mining companies, RSA DWAF, Northern Cape Department of Environment & Conservation, Orange River Interim Management Committee	<R1million
	Support to Lower Orange Transfrontier Conservation Area (LOTCA) Invasive Alien Plant Management Programme for: Establishing joint technical working group for invasive alien plant management. Quantification of extent of invasive alien plants in the LOTCA. Carrying out livelihoods and socio-economic assessment Developing invasive alien plant management plan for LOTCA. Developing and transferring technical capacity for management of invasive alien plant control programmes in	RSA DWAF, Working for Water, Namibian Ministry of Agriculture, Water & Forestry, Namibian Ministry of Environment & Tourism and Namibian Ministry of Lands & Resettlement.	<R1million per annum

	Namibia		
	Coordination of management of the Orange River Mouth estuary with involvement from the Northern Cape provincial Department of Environment & Conservation, the Orange River Interim Management Committee and Richtersveld community.	Local mining companies, RSA DWAF, Northern Cape provincial Department of Environment & Conservation, the Orange River Interim Management Committee	<R1million per annum
	Support to Black Fly Control programme for: Funding and research support to pilot control programme upstream towards Vaal-Orange River confluence. Funding for surveys and monitoring, hiring of helicopters for applications, and purchase of larvicide. Installation of additional flow measurement stations along the length of the river.	RSA DWAF, WRC, RSA Department of Agriculture, RSA Agricultural Research Council	<R1million Per annum

CONSERVATION ISSUE	POSSIBLE MITIGATION INTERVENTION OR PROJECT	INSTITUTIONAL RESPONSIBILITY	COST IMPLICATIONS
Degradation of the Orange River Mouth estuary and Lower Orange River area	Addressing sand mining and removal of spoil dumped in and around estuary	Local mining companies, RSA DWAF, Northern Cape Department of Environment & Conservation, Orange River Interim Management Committee	<R1million
Flow reductions which have created conditions favourable for the proliferation of reeds and other invasive alien species.	Support to Lower Orange Transfrontier Conservation Area (LOTCA) Invasive Alien Plant Management Programme for: Establishing joint technical working group for invasive alien plant management. Quantification of extent of invasive alien plants in the LOTCA. Carrying out livelihoods and socio-economic assessment Developing invasive alien plant management plan for LOTCA. Developing and transferring technical capacity for management of invasive alien plant control programmes in Namibia	RSA DWAF, Working for Water, Namibian Ministry of Agriculture, Water & Forestry, Namibian Ministry of Environment & Tourism and Namibian Ministry of Lands & Resettlement.	<R1million per annum
Collapse of Orange River estuary due to absence of natural seasonal flow patterns and local mining activities	Coordination of management of the Orange River Mouth estuary with involvement from the Northern Cape provincial Department of Environment & Conservation, the Orange River Interim Management Committee and Richtersveld community.	Local mining companies, RSA DWAF, Northern Cape provincial Department of Environment & Conservation, the Orange River Interim Management Committee	<R1million per annum
Blackfly prevalence due to low flow conditions, absence of natural seasonal flow patterns and reed encroachment.	Support to Black Fly Control programme for: Funding and research support to pilot control programme upstream towards Vaal-Orange River confluence. Funding for surveys and monitoring, hiring of helicopters for applications, and purchase of larvicide. Installation of additional flow measurement stations along the length of the river.	RSA DWAF, WRC, RSA Department of Agriculture, RSA Agricultural Research Council	<R1million Per annum

Appendix B

Review of Conservation Funds

Introduction

A key element of the inception phase is a review to inform the feasibility assessment (business case) of a basin-wide fund to support conservation measures. A specific element of this review is to identify and describe conservation type funds successfully implemented elsewhere in the region and globally that may provide ideas and lessons applicable to the Orange-Senqu basin. The terms of reference indicate a number of questions, all of which are necessary for the business case:

1. *What will the fund be used for?*
2. *Who will administer the fund?*
3. *How will the funds be collected?*
4. *How can financial sustainability in the immediate, short, medium and long term be assured?*
5. *How can we be sure that the fund is achieving the objective of ensuring the conservation of the basin's water and natural resources? What sort of indicators can be developed in this respect?*

This chapter provides the review of international funds comparable to the proposed ORASECOM water and environmental conservation fund. This task involved the review of 20 international funds, spanning the full range of possible objectives for the proposed ORASECOM conservation fund and including funds in the region and beyond, in developed and developing countries.

Table: List of funds reviewed

No.	FUND	COUNTRY / REGION
1	Arizona Water Protection Fund	USA
2	Clean Water State Revolving Fund	USA
3	Drinking Water State Revolving Fund	USA
4	Cooperation Fund for the Water Sector	ASIA
5	Environmental Funds of the Ukraine	UKRAINE
6	Environmental Pollution Prevention Fund	KOREA
7	Fund for the Protection of Water (FONAG)	ECUADOR
8	Great Lakes Protection Fund	USA
9	Land and Water Conservation Fund	USA
10	National Environmental Protection Fund	BULGARIA
11	National Fund for Environmental Protection and Water Management	POLAND
12	National Trust EcoFund,	BULGARIA
13	Nile Basin Trust Fund	NILE BASIN
14	Pan-African Infrastructure Development Fund	AFRICA
15	Provincial Water Protection Fund	CANADA
16	Sangha Tri-National Foundation	CAMEROON, CAR, CONGO
17	SADC Regional Development Fund	SADC
18	Shanghai Water Resource Protection Fund	CHINA
19	Table Mountain Fund	RSA
20	Water Infrastructure Fund	USA

This review presents a synthesis of this analysis, and rather than only providing a summary of the funds, it provides an analysis of the funds against a set framework. This framework considers:

- The purpose
- The institutional models
- The institutional relationships and arrangements (including trust funds)
- The financial arrangements

The framework then provides an analysis of this information distilling key lessons and issues for consideration in the design of the proposed ORASECOM conservation fund.

One particular fund that was reviewed - the Nile Basin Trust Fund – is described in some detail, given potential similarity with the proposed ORASECOM conservation fund.

Purpose of the Funds

Water quality maintenance

The first category of funds seek to maintain water quality, to maintain drinking water quality, support productive use of the resource or to protect aquatic ecosystem goods, services and functions.

Such funds vary widely in their size and application, but many of the developed world funds focus on infrastructure development to support wastewater treatment. These funds usually provide resources to local authorities (municipal service providers) to support a range of wastewater infrastructure capital costs, including maintenance, refurbishment, betterment (upgrading) and replacement. Examples include the Drinking Water State Revolving Fund (USA), the Clean Water State Revolving Fund (USA), the Provincial Water Protection Fund (Canada – Ontario) and the Shanghai Water Resource Protection Fund (China).

Another group of funds support a wider range of environmental quality / pollution control objectives, including:

- Rehabilitation of contaminated land
- Removal and disposal of toxic waste
- Accident and emergency response to pollution incidents
- Prevention of pollution
- Research and technology development

While these funds do not relate specifically to the water resource, they clearly support prevention of water pollution through activities that prevent pollution or manage pollution impact on land, in water and in the atmosphere generally. Examples of such funds include the USEPA Superfund (USA) and the Environmental Protection Fund (Zambia).

Infrastructure development

A large number of funds exist for the development of infrastructure in the water sector. Besides the water quality related infrastructure funds discussed above, these funds can broadly be classed into two categories:

1. Funds for the development of new water resources infrastructure, such as dams, pipelines, irrigation systems (e.g. the Pan African Infrastructure Development Fund); and
2. Funds that support water conservation through rehabilitation, refurbishment, maintenance and betterment of existing infrastructure (e.g. the Water Infrastructure

Fund, the Clean Water State Revolving Fund and the Drinking Water State Revolving Fund of the USA).

Aquatic ecosystem protection

A number of funds focus on the protection of aquatic ecosystems as their primary purpose. Such protection serves environmental quality objectives and seeks to create or maintain an environment that resembles the natural state. Specific activities that such funds finance include:

- Environmental engineering and construction activities, such as the creation of artificial wetlands, restoration of channels, and the removal of man-made structures (e.g. weirs);
- Biological interventions, such as riparian re-vegetation, the re-introduction of certain aquatic species, and the restoration of wetlands and uplands;
- Agricultural management activities, such as fencing and grazing improvement, improved agro-chemical use; and erosion control;
- Strategies and management plans;
- Environmental awareness and education; and
- Applied research.

Examples include the Arizona Water Protection Fund (USA), Great Lakes Protection Fund (USA) and the National Fund for Environmental Protection and Water Management (Poland).

Land and conservation

A further large group of funds exist that support land conservation initiatives. Here one can distinguish the following broad groupings:

- Acquisition of land for conservation purposes (e.g. Land and Water Conservation Fund, USA);
- Payment for environmental services (e.g. FONAG, Equador);
- Funding of particular biodiversity conservation activities, often within a particular geographic area (e.g. Table Mountain Fund, Sangha Tri-National Foundation);
- Awareness, advocacy and education; and
- Conservation related research.

Whilst these funds do not pertain exclusively to the aquatic environment, conservation of land and water are closely related and many of these funds focus on protection of the aquatic (including marine) environment.

Institutional development and support

This final category of funds within the water sector focus on developing the water sector management institutions, through:

- institutional establishment support, including development of institutional infrastructure;
- institutional capacity building, and co-finance for human resource recruitment and retention;
- funding of particular institutional programmes or processes (e.g. strategy development); and
- to provide resources for funding regional water sector initiatives of a regional development institution.

Examples of these funds include the Nile Basin Trust Fund, the SADC Development Fund and the ADB's Cooperation Fund for the Water Sector (CFWS). The Funds can either serve as a means to pool resources (often provided by member states) or as a conduit for grant funding (often from donors).

Table: Purpose of the funds reviewed

FUND	COUNTRY / REGION
<u>WATER AND ENVIRONMENTAL QUALITY MAINTENANCE</u>	
National Fund for Environmental Protection and Water Management	POLAND
Clean Water State Revolving Fund	USA
Drinking Water State Revolving Fund	USA
Environmental Funds of the Ukraine	UKRAINE
Environmental Pollution Prevention Fund	KOREA
Shanghai Water Resource Protection Fund	CHINA
National Environmental Protection Fund	BULGARIA
<u>INFRASTRUCTURE DEVELOPMENT</u>	
Water Infrastructure Fund	USA
Pan-African Infrastructure Development Fund	AFRICA
Cooperation Fund for the Water Sector	ASIA
<u>AQUATIC ECOSYSTEM PROTECTION</u>	
Arizona Water Protection Fund	USA
Fund for the Protection of Water (FONAG)	ECUADOR
Great Lakes Protection Fund	USA
<u>LAND AND BIODIVERSITY CONSERVATION</u>	
Provincial Water Protection Fund	CANADA
Sangha Tri-National Foundation	CAMEROON, CAR, CONGO
Table Mountain Fund	RSA
National Trust EcoFund,	BULGARIA
Land and Water Conservation Fund	USA
<u>INSTITUTIONAL DEVELOPMENT AND SUPPORT</u>	
Nile Basin Trust Fund	NILE BASIN
SADC Regional Development Fund	SADC

Fund Institutional Arrangements

The institutional arrangements describe how the fund is constructed in relation to other institutions. The term Fund refers to the process of Funding or to a collective investment scheme or vehicle. The distinction is significant:

- the former definition refers to a financial arrangement through which finance is received, administered and disbursed
- the latter refers to an institutional arrangement that has strategic, governance and accountability implications.

These arrangements are described diagrammatically below (Figure 3.1Figure) through three possible institutional models:

- Institutional Fund

The Fund may be an institution in its own right, established as a legal entity with a governing board structure and management capacity. In this case, the fund develops strategy for the institution, including sources and disbursement of funding, and is accountable for the implementation of that strategy (and the expenditure against the strategy). Whilst the fund may outsource some of its peripheral functions (including investment), the Fund retains the core Fund functions of strategy, revenue management, financial management and disbursement.

- **Managed Fund**

In this mixed model, the Fund is established as an independent entity (may or may not be a legal entity) with stakeholder representation through an advisory committee, steering committee, board of trustees or governing board. However, much of the administrative and technical functions of the Fund are transferred to an allied institution, which is responsible for the financial management including disbursement. Strategy may be set by the board, or may be informed by the stakeholder grouping (steering committee or advisory committee).

- **Fund Account**

On the other extreme, the fund may simply be a financial vehicle for the collection, management and disbursement of finances, and to support fund accounting. In this simplest form, the fund is a bank account or a ring-fenced line item within an existing account. A separate institution is responsible for the account, and develops a strategy according to which funding and disbursement is undertaken. This separate institution is accountable for the fund, assumes the risk associated with the fund and performs all the management and administrative functions associated with the fund.

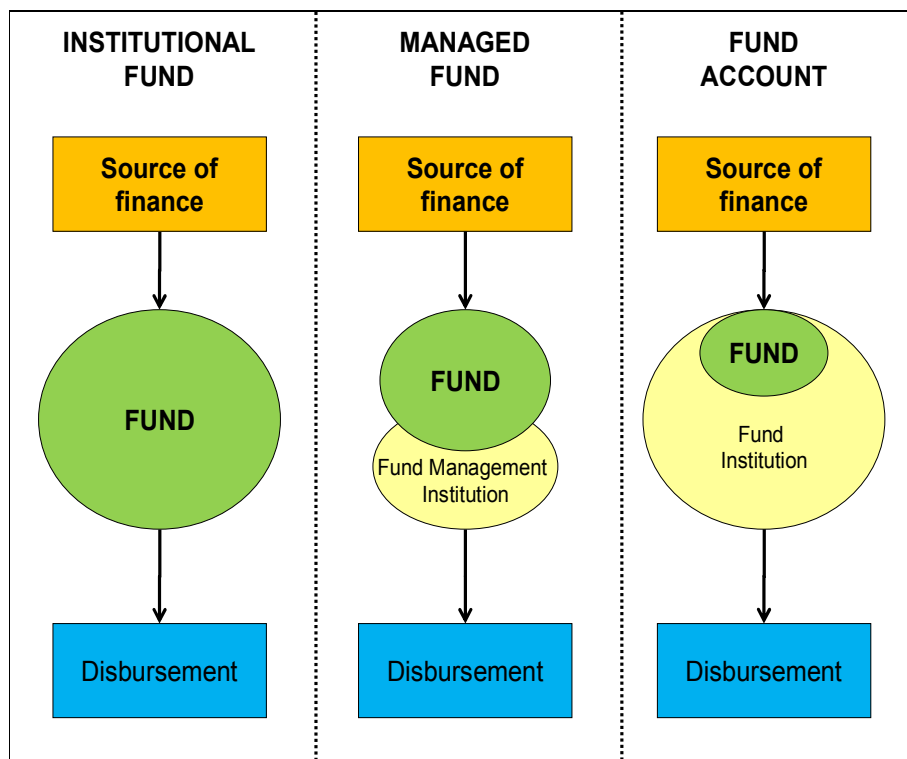


Figure: Institutional models for a Fund

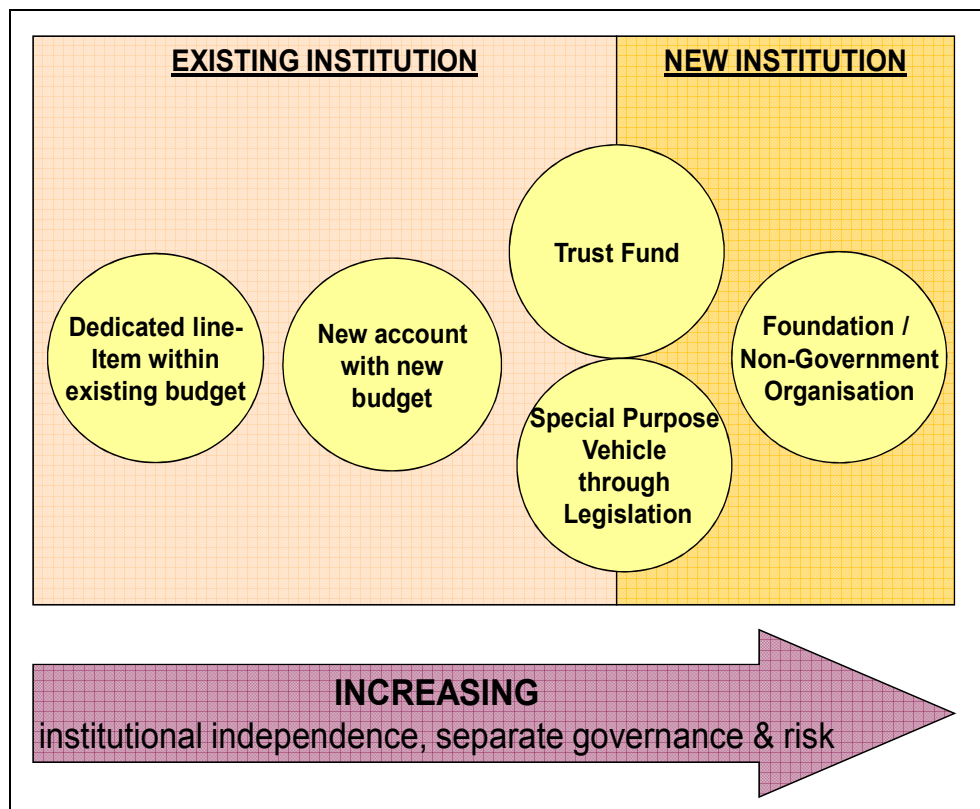


Figure: Institutional / legal vehicles for the Fund

Table: Examples of Funds fitting the institutional models

INSTITUTIONAL FUND	MANAGED FUND	FUND ACCOUNT
FONAG, ECUADOR	Nile Basin Trust Fund, NILE BASIN	Water Infrastructure Fund, USA
Sangha Tri-National Foundation, CAMEROON, CAR, CONGO	Shanghai Water Resource Protection Fund, CHINA	Drinking Water State Revolving Fund, USA
Great Lakes Protection Fund, USA	Table Mountain Fund, RSA	Clean Water State Revolving Fund, USA
National Fund for Environmental Protection and Water Management, POLAND	Arizona Water Protection Fund, USA	Provincial Water Protection Fund, CANADA
Pan-African Infrastructure Development Fund, AFRICA	Environmental Pollution Prevention Fund, KOREA	Environmental Funds of the Ukraine, UKRAINE
National Trust EcoFund, BULGARIA		Land and Water Conservation Fund, USA
		National Environmental Protection Fund, BULGARIA
		Cooperation Fund for the Water Sector, ASIA
		SADC Regional Development Fund, SADC

Functional areas

In understanding the distinction between the models, it is useful to unpack the functional areas typically associated with funds and funding. The functional areas are allocated to

different institutions and imply differing institutional relationships between the three broad institutional models described above.

- Funding strategic framework
This is the broad framework according to which the fund operates and described the sources of funding, what funding will be used for (the purpose of the fund) and the rules for allocation
- Funding allocation and monitoring
This pertains to the determination of funding allocation, based on the framework and an assessment of applications / priority areas. This functional area develops the rules for allocation into a set of practical guidelines and procedures, and involves the administrative process of identifying and evaluating projects / initiatives for funding. In addition, this functional area evaluates the effectiveness and efficiency of the fund against the defined objectives / purpose through ongoing monitoring and evaluation of funded initiatives.
- Financial administration and control
This refers to the financial and administrative management of the fund, including disbursement, loan repayment and investments, and accounting.
- Reporting
This refers to the accountability function with various reporting on fund allocation and disbursement, fund investment and debt management, and financial management.
- Information and marketing
Is the provision of information regarding the fund and funding to wider stakeholders, including prospective fund beneficiaries.

These functional areas are distributed differently in the three institutional models described above:

- The Institutional Fund model assumes all strategic and core functional areas within the Fund – it develops the strategic framework, does the fund allocation and monitoring, is responsible for reporting and for information management and communication functions. This model usually also internalises funding administration, but may make use of professional services for fund investments or debt management.
- The Managed Fund model sets the strategic framework and may assume some of the core functional area of funding allocation and monitoring. However, often this model utilises the close institutional relationship with the fund management institution to delegate the allocation and monitoring, administration, reporting and information functions. Accountability against the strategic framework is maintained through reporting arrangements between the Fund and the management institution.
- In the Fund Account model a separate institutional structure for the fund does not exist, and its functional areas are part of the larger functional areas and strategy of the host institution (fund institution). This institution's mandates and functions are significantly greater than those of the fund, and the fund constitutes a part (often small) of the activities and strategy of the host institution.

Institutional relationships

The fund has particular relationships with the accountable authority; partners and mandated institution/s, the funders and financiers, projects and initiatives, and the public (Figure 3.2Figure). Broadly, relationships centre on:

- Responsibility for strategy and governance;
- Input to strategic direction and accountability against the direction;
- Financial accountability;

- Project (funding) application and evaluation, financial support, oversight and monitoring; and
- Information.

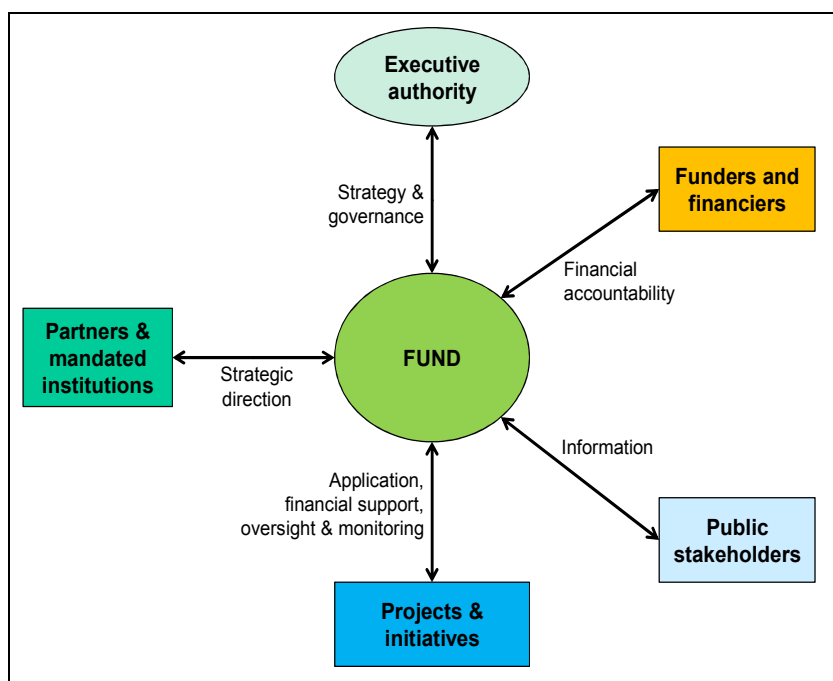


Figure: Relationships for the fund

The extent to which these relationship manifest as institutional arrangements depends on the institutional model and the distribution of functional areas.

- Relationships for the Institutional Fund centre closely follow the institutional arrangements depicted in Figure 3.2Figure, except that the accountable authority is internal to the Fund (governing board, trustees, etc.). This is the most complex institutional form of the Fund and therefore has the most complex institutional arrangements associated with the fund.
- Relationships for the Managed Fund centre on the institutional arrangements with funders and financiers, and with partners and mandated institutions. As with the Institutional Fund, the accountable authority is internal to the Fund (governing board, trustees, etc). Relationships with projects and with the wider public stakeholders (information) are often delegated to the fund management institution.
- Relationships for the Fund Account are simple, with all the relationships undertaken through the separate institution that houses the fund. Because that institution has a wider mandate than the fund, the institutional arrangements for the fund often form part of existing institutional arrangements that emerge as part of the host institution's broader mandate and functions.

Strategy development, risk and stakeholder participation

The development of strategy for the fund and the associated accountability for the fund and risk varies greatly between the different forms of funds described above. However, ultimately the institution that assumes accountability for the fund must have responsibility for strategy formulation. Where the fund has a designated governing board or trustee structure, which

assumes responsibility for governance and risk management, this structure sets the strategy.

However, where the purpose of the fund has overlapping mandates with other institutions, stakeholder input to strategy development is often required to ensure alignment of fund objectives with the strategic framework (policy and objectives) of the other mandated institutions. This is particularly the case where the fund assumes a regional mandate that requires alignment with national objectives. In addition, significant funders (and founders) often require representation for strategy development, to ensure alignment with the funders objectives. Such representation can be achieved through designated positions on the governing board (trustees), but for governance reasons it may require the establishment of a joint strategy development forum. Where this parallel structure for input to the strategy is required, custodianship of the strategy (and associated risk) still rests with the accountable authority (i.e. board), but with a requirement that the strategic input from the forum be taken into consideration.

Where the fund is effectively a designated item or ring-fenced account within a larger institution, the fund strategy is part of the broader strategy of the institution, which is developed outside the ambit of the fund through the institution's governing structure.

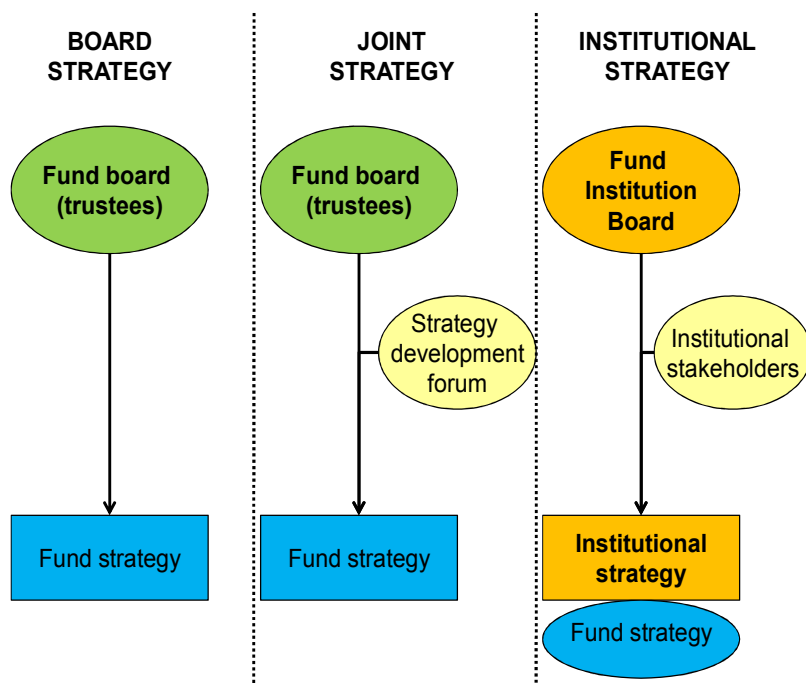


Figure: Strategy development and stakeholder participation

Nature of the institution: organisational and cost implications

Depending on the institutional model, functional areas, institutional arrangements, the responsibility for strategy and risk management, the fund assumes significantly different organisational and cost implications.

The Institutional Fund, with only limited outsourcing (perhaps of the fund administration functions), is the most complex organisationally, as it must build capacity for the full range of functional areas (perhaps with the exception of some of the technical financial capacity). Accordingly, this institutional form is the most costly and utilises few economies of scale or shared services.

The Managed Fund is an intermediate form, with some capacity required for the strategy, allocation and monitoring functions, but with significant cost and skills efficiency introduced through the sharing of services and outsourcing of functions.

The Fund Account is the simplest organisational form of the fund, requiring very few staff and limited skills as most of the fund functions are performed within the greater functional areas of the host institution.

Trust Funds

A relatively recent development is the emergence of trust funds – so called Conservation Trust Funds (CTF) or Environmental Trust Funds (ETF) – as financial instruments for the collection, management and disbursement of grant funding for conservation activities. Broadly, trust funds are a pool of financial resources that are collected for a specified purpose, that are kept and administered separately from other finance (e.g. government revenue) within a designated account and that are managed by a professional entity including an independent governing body.

These CTFs have a number of common features:

- They are independent legal persons, with all the related juristic powers;
- They are governed by an independent, professional board that is typically composed of individuals from a mix of private and public institutions;
- Political representation is limited, to ensure the institutions are apolitical / non-aligned;
- They make grants to government, civil society and private sector institutions – accordingly, they are financing mechanisms rather than implementing agencies;
- CTFs typically provide finance in four broad areas: (i) conservation projects; (ii) institutional strengthening; (iii) sustainable livelihoods; and (iv) private sector partnerships for conservation.
- They often finance part of the long-term management costs of a country's protected area (PA) system;
- Administrative costs (overheads) are typically 10-20% of the annual budget, while investment returns are typically around 10%;
- Because they are professional, accountable and non-align institutions, they serve as an effective means for mobilizing funding from the public and private sector.

Four key conditions or prerequisites for successful CTFs have been described in the literature:

1. The funding requirements are long-term and sustained – CTFs do not cover short-term, emergency funding requirements;
2. They support conservation systems including a number of protected areas or conservation initiatives, rather than individual protected areas;
3. There is political and financial commitment to support the fund and participate in its work; and
4. There are appropriate legal and financial practices and institutions that support the fund, to provide the confidence for raising capital.

A number of different kinds of CTF can be described:

- Grants Fund
Channels resources to target groups, typically civil society, for a broad range of conservation and sustainable development projects, not limited to PAs

- Green Fund
Primarily finances activities related to biodiversity conservation
- Brown Fund
Finances activities such as pollution control and waste treatment, and are financed by pollution charges or fines
- Parks Fund
Finances the management costs and sometimes the establishment costs of specific protected areas, or of a country's entire protected area system, including financing livelihoods or sustainable development activities in protected area buffer zone communities

Fund Financial Arrangements

Sources of conservation finance

Water conservation finance refers to the provision of financial resources for the development, implementation and management of water conservation programmes or initiatives. As such, water conservation finance is a wide and diverse field, covering all manner of financing arrangements from individual projects and initiatives to government funding for national (state) conservation mandates. Increasingly, governments, multilateral donor agencies and civil society are recognizing the need to develop sustainable water conservation finance mechanisms, and are pioneered innovative and successful economic instruments that dedicate long-term funding for water conservation.

Another element of conservation finance is funding for environmental conservation and the protection of natural capital within the context of sustainable utilisation. Finance for this type of conservation is developing rapidly, but it is widely held that the efforts to date have not achieved the scale of impact required to meet the global conservation funding challenge. New initiatives, like debt-for-nature-swaps (debt redirection) have helped to close the gap, but significant challenges remain to find sustainable mechanisms that are institutionally and financially responsive to the conservation funding challenge.

Conservation finance can be distinguished according to the source of funding, which also typically informs the purpose of funding:

- Government finance in the form of fiscal allocations from general tax revenue (including debt-for-nature swaps), earmarked government (tax) revenue or allocations from government grants or loans. Government finance may be ongoing finance as part of annual allocation to mandated government institutions, or may be once-off programme finance for specific conservation initiatives that support government's objectives;
- Income through user charge and levies, earmarked taxes, payment for environmental services schemes, carbon and biodiversity finance, sale of goods and services, patents, amongst others. Such income is often relatively stable and forms the basis for operational cost recovery; and
- Grants and donations from cooperating partners, private sector and/or nongovernmental organisations.

Types of funds

While the preceding section has described various differing institutional forms of funds, funds can also be distinguished based on the source of their finance and the sustainability of funding. Broadly, four types of funds are described in the literature:

- **Endowment Fund**
Capital is invested in perpetuity, and only the resulting investment income is used to finance grants and activities – the capital base is maintained or grown over time. Disbursement capacity of the fund is maintained or grows over time. Large initial funds (seed funding / endowment) are required to ensure a reasonable investment return after costs and inflation are covered.
- **Sinking Fund**
The entire principal and investment income is disbursed over a fairly long period (typically 10 to 20 years) – the capital base is eroded over time until the fund is depleted. Disbursement capacity of the fund reduces with time. Moderate initial investment is required, depending on the nature of the funding to be undertaken.
- **Revolving Fund**
Loan repayments and / or income from taxes, charges, fines, or PES schemes regularly go into the fund and therefore the asset base of the fund is maintained or grows over time. Disbursement capacity increases with time and moderate initial funding (seed funding) is required to initiate the loan cycle.
- **Mixed Fund**
That has both a capital portion and an investment portion, often operated through separate accounts. The investment portion may be based on endowments, income or may be built on a loan arrangement. These funds are often the most popular, as they allow different arrangements for different funders – i.e. donors can contribute capital to specified programmes on a sinking fund basis, other funders can provide endowments aligned with the general fund strategy, while financiers can enter into loan-type revolving fund arrangements.

Accounting and financial reporting

Fund accounting serves any non-profit organization or the public sector where the main purpose is stewardship of financial resources received and expended in compliance with legal or other requirements, rather than profit. Accordingly, such organizations have a need for special reporting to financial statements users that show how money is spent, rather than how much profit was earned. Fund accounting follows the principles of GAAP (Generally Accepted Accounting Principles) developed for the Public Sector.

Implications for ORASECOM

Purpose of the fund

The first key consideration for a Fund is the purpose. This purpose may be focussed or broad – however, where a broad purpose is pursued, the fund should have sufficient resources to enable effective execution of a wide mandate. Similarly, the fund should be institutionally aligned to enable it to deliver its broad mandate without institutional complexity and inefficiency arising owing to overlapping mandates. As such, most funds with broad mandates are government supported funds located within key government institutions (Treasury, Environmental Regulator, etc.).

Funds for other institutions are, therefore, often more focussed in mandate. This reflects the lower resources typically available and the reduced mandate. A distinctly focussed mandate with clear objectives and success indicators is a key success factor in these funds.

Applying this rule-of-thumb to a possible ORASECOM conservation fund suggests that a focussed purpose for the fund should be established, with the fund responding to the key issues that reflect the mandate of ORASECOM, are within the funding capabilities of the

organisation (or its donors) and are sufficiently significant to solicit support (both financial and political).

Legal establishment and corporate form

Following clarification on the purpose of the fund, the legal and corporate form of the fund should be carefully considered. A number of legal forms are available where the fund is established as a separate institutional structure:

- Common law trust fund;
- Civil or common law foundations;
- Civil or common law not-for-profit corporation;
- Created by special legislation as a public entity or public-private partnership; or
- Created by international agreement between donor and beneficiary countries.

In addition to these independent entities, a fund may be established within an existing institution (separate bank account or ring-fenced line item), with or without an advisory committee established to provide strategic input, enable stakeholder participation and to ensure an element of governance and oversight.

Where a separate legal entity is required, the chosen legal form may be either in-country or offshore (i.e. either in one of the beneficiary countries or in a third-party country). Important considerations in selecting the appropriate legal form include the legal and institutional strength of the host country, taxation issues for the fund, taxation issues for donors and issues of perception linked to the host country. The final form listed here – by international agreement between participating countries – may be particularly relevant to the proposed fund, given the international nature of funding and disbursement.

Ultimately, the nature of the fund, where it should be established, various legal and taxation considerations, its statutory governance structures and its reporting requirements depends significantly on considerations of risk and credibility, stakeholder acceptability, economy and cost minimisation and administrative efficiency. This requires a detailed analysis of what is most suitable, combined with extensive consultation with stakeholders on stakeholder preferences.

A further consideration will be the institutional-organisational form of the Fund, with distinction between a separate entity to house the Fund or the use of an existing entity to share services and reduce overhead costs.

Political support

Political support for the fund concept, the specific fund purpose and the selected fund institutional and organisational models is of critical importance to ensure that buy-in to the fund is achieved. Such support is central to ensuring a streamlined mandate, efficient and effective execution of functions, and ongoing financial support. This is particularly important for regional funds that cross administrative and political boundaries, as the institutional arrangements for such funds are particularly complex and require widespread political support to ensure effective fund implementation.

Gaining and maintaining this support implies particular governance structures and systems that keep the key stakeholders – member states and national mandated institutions – closely involved in the process and confers a degree of ownership of the process to those stakeholders. Such structures and systems involve both the nominations process for representation on the governing board of the Fund, and the establishment of additional governance structures such as advisory councils or stakeholder committees that input to the fund strategy and performance review.

Governing board and structures for representation

Where a separate institutional structure is deployed, and hence a governing board is required, board composition should be a mix of governmental and non-governmental representatives, and board size should be a compromise between adequate representation and efficiency in decision-making. Board composition should be in the majority non-government, with some key government *ex officio* positions to represent government interests. Civil society should be represented, as the Board should be responsive to the needs and concerns of NGOs and community groups. However, representation should be such that the Board is not pulled in too many directions by a wide range of constituencies with conflicting interests. Representation of the private sector is also useful, as the private sector often have experience serving on boards, and often bringing a level of financial expertise not usually found in either government or the NGOs.

Board selection should be through a participatory approach, with good representation by the Fund's beneficiaries, government, donors, and private sector, so that stakeholders have confidence in decisions that are taken. The roles and responsibilities of Board members must be very clear, and board procedures should be clearly articulated. Board tenure should be considered to enable sufficient time for implementation of strategy, but also adequate turn-over to enable the introduction of new ideas. Consistency between one board and the next should be ensured by retaining a critical mass of board members and through good induction processes.

Strategic planning

A strategic planning process that is closely aligned with that of the support organisation and reflects the strategic objectives of ORASECOM, the member states and mandated national institutions is required. The strategic plan of the fund must reflect that of ORASECOM, which in turn reflects the strategic intent and objectives of the member state. Accordingly, a step-wise planning process is required.

Strategic planning is a critical area for stakeholder involvement, and structures to ensure that ensure that the strategy reflects stakeholder perspectives, is widely supported and enables alignment between the fund and partner institutions are required.

Risk management

Significant financial and risk management capacity is required within the fund, to ensure good governance and appropriate execution of fiduciary responsibilities, and to ensuring ongoing financial (and technical) support from donors and funding institutions associated with perceptions of credibility, accountability, professionalism, transparency, efficiency and effectiveness. This implies governance structures and systems within the organisation that ensure that the highest standards of governance and risk management are maintained, and that relationships with key stakeholders and funders are nurtured. It also implies the need for specific and specialised skills at board and executive level within the organisation.

Consultation and stakeholder participation

The need for extensive stakeholder engagement and for dedicated stakeholder representation structures has been outlined under the need for political will and for strategic planning above. In summary, consultative structures must be established that reflect the need for political will, that understand and internalise the strategic objectives and imperatives of key stakeholders, and that maintain good relationships and efficient institutional arrangements with key stakeholders and funders.

Such consultative structures may go beyond governance structures to imply an organisational design that reflects the importance of ongoing consultation and collaboration with stakeholders, partners, beneficiaries and allied initiatives.

Human resources and capacity

Human resource capacity must reflect the significant challenge posed by a regional conservation finance initiative, with the various complex institutional, strategic, financial, political and organisational elements to the proposed fund. Outstanding fund leadership will be required, not only to ensure effectiveness and efficiency of fund administration, but also to ensure ongoing strategic re-alignment, as the strategic direction of stakeholders, beneficiaries, funders and other players changes. A carefully designed description, recruitment, evaluation and performance management system will be required to ensure access to and retention of the requisite management skills.

Organisational performance

A clearly defined and quantifiable purpose and objectives, linked to measurable and reportable criteria that enable constant and careful assessment of the performance of the organisation against a set of commonly accepted key performance indicators, to ensure that the organisation remains true to its mandate and the expectations of its stakeholders, funders and beneficiaries. A balanced score-card type approach may be appropriate for such an organisational assessment.

Summary: best-practice in fund assessment and establishment

Based on the international experiences in the establishment of functional and efficient conservation funds, the following process can be outlined:

1. Defining specific, priority conservation objectives
 - a. Undertake a careful assessment of the need for public expenditures to achieve these objectives;
 - b. Assess the institutional arrangements for achieving the objectives to determine existing mandates and initiatives; and
 - c. Define the conservation finance gap to enable the development of a focussed mandate for the fund.
2. Determine the financial requirements
3. Identify possible sources of funding and assess viability of sources meeting required funding
4. Develop the main elements of an expenditure program
 - a. such as specific objectives, cost estimates, description of eligible project types and beneficiaries, terms of financing, procedures, principles and criteria of project appraisal and selection, procurement rules, time frame, indicators of performance
5. Conduct an institutional assessment to select the best institutional arrangement for managing the expenditure program
6. Develop a business case describing the institutional arrangements, governance requirements, organisational implications and financial arrangements for the institution
7. Develop the legal instruments for the establishment of the institution
8. Commence functional establishment of the institution through recruitment of senior (executive) staff – CEO or similar – to drive the functional establishment, and strategic and business planning process.

Nile Basin Trust Fund

Given the apparent similarity of the fund considered by ORASECOM with the Nile Basin Trust Fund (NBTF), this fund is summarised here based on available information.

History

The Nile Basin Initiative is supported by contributions from the NBI countries themselves and through support from several multilateral and bilateral donors. The financial mechanisms in support of the NBI were designed with several objectives in mind: to maximize riparian ownership and control of the process; to meet donor requirements for fiduciary accountability; and to provide timely and efficient administration of funds. Given the nascent nature of the cooperative Nile institutions, the magnitude of financial resources involved, the imperative for early implementation of projects, a multi-donor trust fund was proposed by the Nile Council of Ministers as the preferred initial funding mechanism (requested in March 2001 and launched in January 2003). This was to allow funds to be transferred according to established disbursement and procurement procedures. The objective is the eventual transfer of the trust fund to a Nile Basin institution as program implementation progresses and a permanent institutional framework established.

Purpose

The NBTF is a funding mechanism that helps administer and harmonize donor partner support pledged to the Nile Basin Initiative (NBI). The NBTF has an institutional purpose (as defined above) and specifically supports the preparation and implementation of NBI programs. The majority of funds supporting NBI programs and projects are administered through the NBTF, and it has proven to be a very effective mechanism for harmonizing donor support to the NBI and ensuring a unified and coherent approach to managing funds.

At the basin-wide level, the NBTF supports:

- Strategy (Shared Vision Program);
- Stakeholder engagement through the process of NBI dialogue and engagement; and
- Institutional capacity through strengthen the NBI institutions

At the sub-basin level, the NBTF supports:

- The development of investment programmes (ENSAP and NELSAP); and
- The preparation and implementation of joint investment projects.

Institutional form, arrangements and governance

The NBTF exists as a separate legal entity (a Trust Fund) and follows the institutional model described above as the Managed Fund.

The NBTF is governed by a committee (NBTF Committee) that is responsible for overseeing the operation of the trust fund and ensuring that resources used meet NBI program objectives. This Committee is comprised of representatives from contributing agencies, the NBI, and the World Bank. Formal NBTF Committee meetings are held once a year in one of the Basin countries.

The World Bank administers the NBTF on behalf of contributing donors, in accordance with the NBTF Agreement and the World Bank's Trust Fund Policy and Procedures. Accordingly, the World Bank is responsible for fiduciary management of pooled multi-donor resources

and for preparing and supervising NBTF-financed projects in accordance with the Bank's rules and procedures.

NBTF funds are transferred to the NBI, which has the primary responsibility for the implementation of project activities. Almost all (about 95 percent) NBTF-financed NBI projects are recipient-executed. This helps ensure ownership of NBI activities and contributes to building institutional capacity to implement regional projects.

As progress is made in program implementation and a permanent institutional framework for the NBI is agreed, the NBTF will be transferred to an NBI institution.

Financial arrangements

The contributors to the NBTF are Canada (CIDA), Denmark (DANIDA), European Commission (EC), Finland, France, Netherlands, Norway, Sweden (SIDA), United Kingdom (DFID), and the World Bank.

APPENDIX C

ORASECOM Institutional Review

Introduction

A possible conservation fund for ORASECOM will be situated within an institutional-legal environment at a regional (SADC), basin and country level. It is important to clarify the legal mandate of ORASECOM, its emerging institutional relationships with other institutions and the national policies that provide the context for conservation measures to be implemented. It is against this context that potential institutional models of funding can be identified and evaluated.

Institutional Arrangements for ORASECOM

Mandate and Role of ORASECOM

ORASECOM's activities are bound by the terms of the ORASECOM Agreement, signed on behalf of the Parties in Windhoek. ORASECOM is founded on the SADC principles of increased regional integration and cooperation of the use of shared water resources to address poverty and food security. Importantly, the ORASECOM Agreement recognizes the existing water sharing arrangements in the Basin (bilaterals) and that the rights and responsibilities of the Parties are not affected under these agreements.

The ORASECOM Agreement establishes the Council as the highest body of ORASECOM. It is the technical advisor to the Parties on matters relating to the development, utilization and conservation of the water resources in the River System. The Parties may also assign other functions, pertaining to the development and utilization of the water resources in the basin, to the Commission. However, mechanisms for the Parties to assign additional functions to ORASECOM have not been clarified or tested.

The objectives, functions and powers of the Council specified in the Agreement are instructive as to the role of ORASECOM. The Objectives are to “serve as technical advisor to the Parties relating to the development, utilisation and conservation of the water resources in the River System” and “other functions . . . as the Parties may agree to assign” [Article 4]. This is captured in the functions of Council “to make recommendations or to advise the Parties” [Article 5], many of which relate directly or indirectly to catchment conservation measures:

- *Measures and arrangements to determine long-term safe yield of the water resources in the River System*
- *equitable and reasonable utilisation of the water resources in the River System to support sustainable development on the territory of each Party*
- *the investigations and studies conducted separately or jointly by the Parties with regard to the development of the River System, including any project or the construction, operation and maintenance of any water works*
- *extent to which the inhabitants in the territory of each Party concerned shall participate in the planning, development, utilisation, protection and conservation of the River System, as well as the harmonisation of policies in that regard and the possible impact on the social, cultural, economic and natural environment*

- *the standardised form of collection. Processing and disseminating data or information with regard to all aspects of the River System*
- *the prevention of the pollution of water resources and the control over aquatic weeds in the River System*
- *contingency plans and measures for responding to emergency situations or harmful conditions resulting from natural causes such as droughts and floods, or human conduct such as industrial accidents*
- *the regular exchange of information and consultation on the possible effects of planned measures*
- *measures with a view to arriving at a settlement of a dispute between one or more of the Parties*

The Agreement also includes the catch-all provision, ‘*such other matters as may be determined by the Parties.*’ Hence, ORASECOM has a mandate to make recommendations to Parties on measures to conserve catchments. To do this the Council has the powers to establish “working groups or committees” and to “appoint technical experts to provide expert opinion and advice”.

Currently no additional functions or powers have been assigned to ORASECOM by the Parties. An important element of this is that ORASECOM is empowered to provide advice and make recommendations, but not to implement this unless requested to by the Parties. It is therefore an advisory rather than a water management body.

The underlying principle of ORASECOM is that the Parties must retain the discretion to implement the recommendations emerging from the Council. Hence, ORASECOM is not able to implement recommendations unless it is assigned this function by the Parties. The Parties and the relevant national and sub-national water institutions have a mandate and resources for delivery. These institutions are likely to resist assignment of implementation functions to ORASECOM, except where joint action between two or more countries is imperative and the focus of the intervention is of a flagship transboundary nature. Nevertheless, resources to implement catchment conservation measures are limited, and therefore financial assistance in the implementation of ORASECOM recommendations is likely to be well received.

Furthermore, recommendations provided by ORASECOM must also include estimates of the cost of implementing the recommendation and may suggest how these costs may be apportioned between the Parties. Recommendations to Parties must not only indicate what must be done, but also how it must be done. In a resource limited environment, it may not always be pragmatic to request the parties to provide resources, but rather to assist the Parties to obtain resources to assist implementation. Consequently, there is scope for ORASECOM to make funds available to Parties or to indicate the way in which funding may be sourced for conservation measures. Recommendations which are supported through a funding mechanism may be more likely to be implemented.

In terms of the typical planning cycle for conservation measures, there are three main stages, each of which ORASECOM has varying mandates to effect and each of which requires differing levels of financial resources:

- ORASECOM clearly has a mandate to **plan** in order to make recommendations to the Parties on issues of a transboundary nature, although as planning moves into design, there may be a need for the Parties to agree to the need for such an intervention.
- ORASECOM only has a mandate to **implement** a measure or initiative within an area of the basin on assignment from the relevant countries, and in the foreseeable future

it is likely that the Parties would require greater control over implementation of most conservation measures in their jurisdictions.

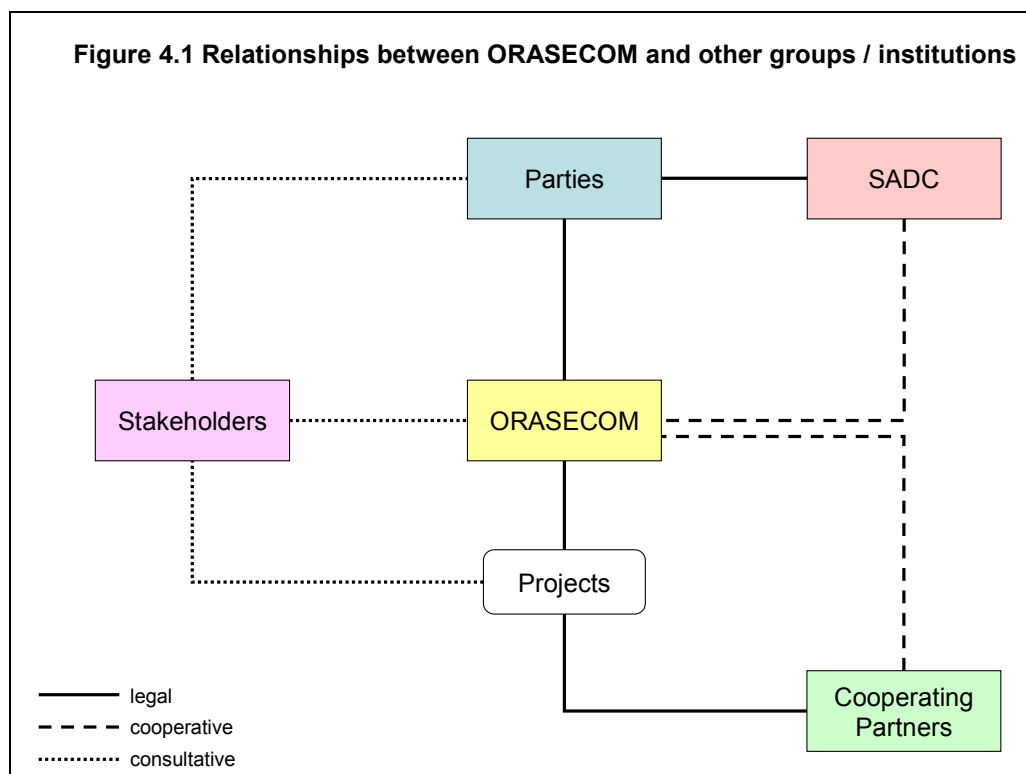
- ORASECOM has a need to **monitor** the status of water resources within the basin, in order to identify issues of transboundary significance and to plan effectively, but while ORASECOM has no direct mandate to monitor it does have the role of ensuring that monitoring is adequate, compatible and accessible.

It follows that any funding mechanism must enable either ORASECOM to plan, implement and monitor a conservation measure, or alternatively must enable the Parties to do so with coordination and support provided by ORASECOM at a basin level.

Since being established as an international body in South Africa, ORASECOM has the powers of a juristic person in South African law. This means that ORASECOM has considerable latitude in the legal establishment of any funding mechanism, including a separate trust or possibly even a legal corporate entity.

ORASECOM Institutional Relationships

This mandate and legal context provides the basis for the institutional arrangements of ORASECOM, particularly in the relationships between ORASECOM and other institutions relating to the planning, implementation, funding and monitoring of conservation measures in the basin. The following diagram outlines the key legal, cooperative or consultative relationships between ORASECOM and other institutions.



The important aspects of these relationships are:

- *Parties* are the principles of the ORASECOM Agreement and determine the mandate and involvement of ORASECOM in catchment conservation measures (through assignment) or endorse the recommendations that ORASECOM makes.

- SADC (represented by the Secretariat: Water Division) is responsible for cooperatively ensuring implementation of the SADC Protocol on Shared Watercourses, with monitoring and dispute resolution elements, while the Parties also represent ORASECOM in SADC in terms of the SADC Treaty.
- ORASECOM *projects* are the key vehicle for ORASECOM to achieve its advisory mandate (with limited permanent capacity) and are conducted by legally contracting implementing agents and/or consultants to provide services – these projects may be studies to generate recommendations or where assigned the projects may involve implementation in one or more of the four countries.
- *Cooperating Partners* provide important sources of funding and technical support, but this is primarily through projects, that are cooperatively agreed between ORASECOM and the group of cooperating partners.
- *Stakeholders* (private sector, civil society and local government) within the basin may be consulted at a project level, or more broadly by ORASECOM at a basin level or by the Parties (governments) at a national/sub-national level.

All four states are signatories to the SADC Revised Protocol on Shared Watercourse Systems (2000), which was initially adopted in 1995 and then revised in 2000, in order that its provisions were brought in line with those of the United Nations Convention on the law of the non-navigational uses of international watercourses (1998). The Protocol makes provision for management institutions for shared watercourses, and sets out five components that guide the development, use and protection of international watercourses. They are as follows:

- Balancing development with conservation
- Inter-state co-operation
- Equitable sharing of water courses
- Developing compatible national systems
- Notification of emergencies

The Protocol provides for the guiding principles for equitable and sustainable allocation of international waters in the SADC region. As the four Parties are signatories to the Protocol, it provides the overarching framework for the management of international waters in the Orange-Senqu basin. This framework should provide for the ‘harmonized legal regime’ for the Orange River in which the revised SADC Protocol, the ORASECOM agreement and the national legislative arrangements for the four countries are consistent and aligned.

Each basin state has its own legal, policy and institutional framework governing the use of both national and international waters, adding to the significant layers of complexity to water management at basin level. Furthermore, the four states vary considerably in both economic power and levels of development, with highly divergent needs in terms of the use of the waters of the Orange Senqu basin. And so it is essential that the existing institutional framework be mapped nationally and internationally in order to understand the levels of complexity better.

Review of National Policy and Legislation

While the Protocol on Shared Watercourses and the Agreement provides SADC legislative framework for ORASECOM, each of the Parties has a national water policy, legislation and strategy that provide the framework for water management within that part of the basin, including conservation measures and potential funding mechanisms. While there are moves towards harmonization of policy, legislation and strategy between countries in SADC and particularly those that share transboundary river basins, these are not entirely aligned. This

is a result of the different pathways in developing national water policy and legislation, as well as the institutional arrangements and capacity in each country.

Therefore, it becomes important to understand the mandate and function of the national water (and related) policy and legislation. Importantly, Member States can only perform or assign what they are empowered to do through policy and legislation, and as such the Parties' national policy and legislation forms an integral part of the institutional arrangements within which ORASECOM operates.

An important nuance of this is the way in which water related conservation measures are defined at a national level, as well as the distinction between those conservation issues having a transboundary nature and those with local or sub-national characteristics. The former are clearly ORASECOM's domain, while the latter are typically of national interest. However, this distinction is not always clear, so the legislative framework for the key conservation issue areas is unpacked in this section.

The tables in Appendix B outline the legal and institutional framework within which water resources management occurs in the four counties. Of particular interest is the level of alignment in a number of areas, namely:

- Water use authorisation, control and enforcement of both abstraction and discharge related water use:
 - All four countries have an established licensing system, while South African and Namibia have national registers of water use and South Africa has the ability to require re-licensing under compulsory licensing.
- Water resources protection and environmental flows, including wetlands.
 - South Africa has Reserve requirements in law, while Namibia is developing policy around environmental flows and Lesotho has established environmental flow requirements associated with the Lesotho Highlands Water Project.
- Environmental and agricultural management, including soil conservation / erosion management.
 - These functions are typically fragmented between water, agriculture and environmental ministries in all four countries, with some policy misalignment even within the counties.

Currently, the institutional and legal frameworks vary between the four basin States, but their development and implementation are currently in a state of transition. Interestingly, from the institutional perspective:

- Institutional arrangements for water resources management.
 - South Africa and Namibia are in the process of establishing basin level institutions for water resources management, while Botswana and Lesotho maintain management at a national level.
- Raw water pricing and funding, distinguishing between water management, water infrastructure and pollution charges.
 - South Africa and Namibia have implemented comprehensive water resources management and infrastructure charges, as well as policy scope for waste discharge / pollution charges that are not yet implemented.

Possible Institutional Models for Conservation Funding

Sources of Funding for Transboundary Conservation Measures

As indicated in the funding review, there are four broad sources of funding for conservations measures in the transboundary context, namely transfers from Parties' government finance, income streams through user charges or levies, income from financial activities, and receipts from grants or donations. The opportunities and applicability of each of these sources and their specifics depends entirely upon the political and legal context of the basin and countries. It is therefore important to understand these sources in the context of ORASECOM.

Government Financing:

This represents fiscal allocations through the annual budget vote by one or more of the countries, either as recurring allocations or for specific conservation initiatives that support the governments' objectives. The original source of this finance may be the general revenue base, earmarked revenue or even government loans, but in each case the finance is transferred from government funds.

- This is a possible form of funding for ORASECOM and is the basis for the operating costs of the institution.
- The Parties have fiscal resource limitations and this may constrain the amount of money that can be allocated to transboundary conservation initiatives, except where this is aligned with national strategic priorities.
- Where these objectives are aligned, countries may be resistant to allocating money to ORASECOM for implementation at a transboundary level, rather than implementing the intervention at a national or catchment level.
- The exception to this is where joint intervention between countries is imperative for effective implementation or it is viewed as a transboundary flagship project.
 - ⇒ In summary, government financing is likely for institutional operating costs, possibly funding of transboundary flagship projects and catchment initiatives from ORASECOM recommendations implemented under the auspices of a national or catchment institution.

Income from charges and levies

This includes a range of tariffs, charges, levies or taxes applied to water users (or potentially other property, such as land). In this category, it is important to distinguish between user charges related to cost recovery for services rendered and levies-taxes that do not relate to benefit received. Other possibilities are targeted payments for environmental services and even carbon finance.

- Typically, these charges must be legislated (empowered) at a national level and require fairly sophisticated financial management systems to ensure payment, which restricts the likelihood of direct charging and collection at a transboundary (ORASECOM) level.
- Dedicated basin-wide management or pollution charges would require aligned legislative processes to enable them, which is logistically and politically unlikely.
- Joint infrastructure charges have and can be applied to cover the costs of infrastructure development and operation, but are unlikely for more localised infrastructure.
- Currently pollution charges have not been implemented in the riparian states, although South Africa has developed the possibility for a waste discharge charge, which currently does not cater for cross-border impacts.
- Currently economic charging (taxes to reflect the value rather than the cost of managing water) has not been developed by the riparian states (although South Africa is exploring

this), users are politically resistant to this type of tax and national treasuries are usually unwilling to earmark this for specific purposes.

- Including costs for transboundary conservation initiatives into existing user charges may be considered, but currently payment levels are low and are dedicated to managing local priorities.
- Payment for environmental services (PES) may be considered in quite targeted local situations, where beneficiaries pay another group to maintain environmental functioning, but this must be locally negotiated.
- Alien vegetation removal may be partially funded by beneficiaries of the water (such as South Africa's working for a water programme), but this currently does not have a cross-border element and has evolved a PES and government financing focus.
 - ⇒ In summary, while user charges and levies may be implemented at a catchment level, they are unlikely to be allocated to transboundary initiatives, except where these align with the local priorities against which the money was collected, while PES systems may be negotiated between local groups even in a cross-border context.

Income from financial activities

This specifically refers to investment income on endowment capital in a fund or other mechanism, as well as debt repayments on possible loans for conservation measures implemented by local agencies (government or other).

- Large endowments allow funding to be made from interest (or other investment) income on the capital, but gaining this level of endowment initially is unlikely, particularly in the current financial climate.
- For specific interventions that have relatively quick payback periods (such as water loss control in urban areas), soft or commercially-based loans may be provided to fund the capital costs of a conservation measure, with savings or local tariff income covering operating costs and debt repayment, which then becomes available for further loans.
 - ⇒ In summary, financial activity income may be considered, depending upon the available capital and disbursement mechanism.

Income from grants and donations

This includes all money provided by external institutions, including cooperating partners (donors), private sector and non-governmental groups. This may be directly into a fund or to an implementing agent on behalf of ORASECOM. The important element is that these grants need to support activities that are consistent with the transboundary priorities and objectives.

- Cooperating partners are already providing significant funding to ORASECOM projects, but this may be translated into some level of basket funding under the direct control of ORASECOM.
- Private sector and civil society organisations provide a potentially untapped source of donations that may be relevant with the increasing public and corporate recognition of the importance and vulnerability of water resources.
 - ⇒ In summary, grants and donations are likely to be the largest source of funding (initially from cooperating partners, but then potentially from private sector and nongovernmental organisations), at least in the next few years as ORASECOM establishes itself within the basin.

Institutional Models for Funding and Implementation

From the preceding discussion, it is apparent that conservation financing mechanisms within the basin may either be established at a transboundary level (i.e. funding under the control of ORASECOM) or may be located at a national level (i.e. funding under the control of institutions within one or more countries that are party to the agreement). The former are most likely to be funded by donations or government contributions into a basin fund, while

the latter may be government financed or user charge income through national or catchment institutions.

The purpose of this project conservation funding is only of interest in so far as it relates to transboundary conservation issues and measures, which would reflect issues or recommendations addressed by ORASECOM. This introduces a second key distinction around the responsibility for implementation of a measure, once endorsed by the Parties. This may either be assigned to ORASECOM acting at the basin level or be conducted by the relevant national, catchment or local institution within a country.

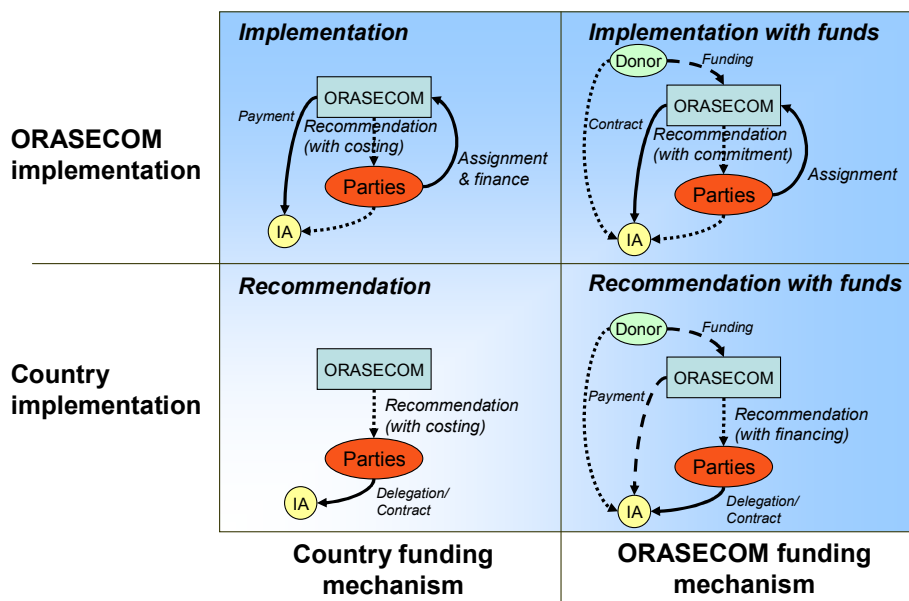
These two distinctions may be reflected as a two-by-two matrix presented in Figure 4.2 below. It is important to note that these models relate to the implementation of conservation measures on the ground, not to their planning which ORASECOM is mandated to perform and fund in its advisory capacity. On the other hand, the performance and financing of basin monitoring activities may be interpreted as a special sub-set of this implementation framework.

Option 1: Recommendation

The option in the bottom left square relates to ORASECOM making recommendations to the Parties to implement, together with an estimate of the costing and source of funding from the Parties' own resources. The Parties either separately or even jointly delegate or contract an implementing agent (IA) to perform the work (which in some cases may be the national Department/Ministry of Water). This would most likely be funded through government fiscal allocations or user charges, for activities that are aligned with national and/or catchment strategic priorities and objectives. This approach may be suitable where it is necessary to ensure basin level alignment of activities that are already being performed and financed to some degree within one or more of the countries. This may be particularly relevant for many basin monitoring activities.

- ✚ The important issue for ORASECOM to make effective recommendations of this nature is for the organisation to have an understanding of the institutional arrangements within countries, the strategic priorities at a catchment level within the basin and the potential sources of water conservation finance at a national and catchment level.

Figure 4.2. Institutional models related to conservation funding

**Option 2: Recommendation with financing**

The option in the bottom right relates to ORASECOM making recommendations to the Parties to implement, but also supported by the costing and the availability of external sources of finance. The Parties would delegate or contract an implementing agent that would most likely receive funds directly from ORASECOM sources (in the case of a fund) or from specific cooperating partners. It may be most appropriate for ORASECOM to establish a dedicated fund to manage these finances in a strategic and transparent manner. There are various management arrangements that may achieve this outcome, depending upon the level of operational and financial control required by the different institutions. It may be that this is the most common arrangement for ORASECOM in the short to medium term, as the Parties require operational control over intervention activities that occur in their countries. It may also be an appropriate model for additional monitoring activities required in the basin.

- ✚ The important issue for ORASECOM is to mobilise external sources of finance to support the strategic priorities at a basin level, and to ensure that recommendations are aligned to national and catchment priorities within a clear basin level strategic framework.

Option 3: Implementation by ORASECOM with Parties' funding

The option in the top left relates to ORASECOM making recommendations to the Parties (with the costing and proposed allocation of funding between the Parties), and that once endorsed are assigned back to ORASECOM to implement, together with the required funding (most likely from government sources or collected user charges). ORASECOM would delegate or contract an implementing agent that may be paid directly from ORASECOM sources (in the case of a fund) or from specific cooperating partners (as is currently the situation with planning projects), and would establish a steering committee consisting of the Parties' nominated representatives. Again, there are various management arrangements that may achieve this outcome, depending upon the level of strategic, operational and financial control required by the different institutions. It is important to consider that the management requirements of these types of projects may be significant

and must be met by the internal capacity of ORASECOM. Given the current resource limitations of the Parties, this option is only likely for “flagship” transboundary conservation issues with high political support, and that absolutely require joint basin level intervention (rather than coordinated implementation at a national level), such as initiatives on the estuary. It is important to note though that this is the way in which ORASECOM costs are financed, and so may provide the basis for basin initiatives of an institutional nature.

- ✚ The important issue for ORASECOM is to focus this approach on potential “flagship” basin initiatives that are affordable by the Parties and that will be politically supported by the Parties.

Option 4: Implementation by ORASECOM with funding

The option in the top right square relates to ORASECOM making recommendations to the Parties (with the costing and availability of finance), and that once endorsed are assigned back to ORASECOM to implement with its own funds. The intervention and project management would be similar to Option 3, except that it would be appropriate for ORASECOM to establish a dedicated fund to manage these finances in a strategic and transparent manner. This provides an important approach to basin level interventions that require coordination and consistency of implementation across countries, particularly where these activities are not being performed adequately within the countries. Again, because assignment to ORASECOM would be required, this would be most appropriate for “flagship” transboundary conservation issues that achieve the basin strategic objectives and that ORASECOM has mobilised funds for. This type of approach will be most successful if implemented through a dedicated ORASECOM funding mechanism, rather than piece-meal through individual projects.

- ✚ The important issue for ORASECOM is to mobilise adequate finance to support the basin level strategic objectives and to make clear recommendations around “flagship” basin initiatives that align with the national and catchment objectives of the Parties.

All four approaches are possible and may be implemented over the next few years. Each of them requires slightly different institutional arrangements and implementation considerations.