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EXECUTIVE COMMITTEE OF  
THE MULTILATERAL FUND FOR THE  
IMPLEMENTATION OF THE MONTREAL PROTOCOL  
Forty-third Meeting  
Geneva, 5-9 July 2004

**Addendum**

**TREATMENT/ENCASHMENT OF PROMISSORY NOTES (FOLLOW-UP TO  
DECISIONS 41/4 AND 42/44)  
(REPORT FROM THE TREASURER)**

**Rules and/Or Systems for the Transparent and Equitable Encashment of Promissory Notes  
Used In Other Forums**

**INTRODUCTION**

1. At the Forty-first Meeting of the Executive committee in December 2003, the Executive Committee requested the Treasurer to report on rules and/or systems for the transparent and equitable encashment of promissory notes used in other forums. This is to enable the Executive Committee to determine the advisability of establishing more standardized rules for the use of promissory notes, and in an effort to ensure that the notes, as well as the contribution in cash of all donors were treated equitably and exchange rate loss minimized.

2. In response to the Executive Committee's decision, the Treasurer circulated a survey/questionnaire to the three implementing agencies and twelve other institutions. The agencies are as follows:

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1. The African Development Bank
2. The Asian Development Bank
3. The European Bank for Recon. & Development
4. The Inter-American Development Bank Group
5. The European Commission
6. The International Fund for Agricultural Development (IFAD)
7. The Islamic Development Bank
8. The Nordic Development Fund
9. The OPEC Fund for Int. Development
10. Corporation Andina de Fomento (CAF)
11. Caribbean Development Bank
12. East African Development Bank
13. The World Bank (which is the Trustee of the (GEF Trust Fund)
14. UNDP
15. UNIDO

3. Out of fifteen surveys sent and one mission undertaken, seven replies were received. Of the replies received four of the agencies namely: The World Bank, The International Fund for Agricultural Development (IFAD), Caribbean Development Bank and UNIDO confirmed that they had exposure to the use of promissory notes and their responses form the basis of this report.

4. The agencies circularized were selected on the basis of our understanding of their activities and possible involvement in the use of promissory notes.

## **RESULTS OF THE SURVEY (Reflects the majority of respondent observations)**

### **Standardized Formats**

5. The use of a standardized form of promissory note was predominant. There was an instance however, where Member States requested slight modifications to suit their particular needs and these required agreement with the Treasurer.

### **Place of Custody of Notes**

6. Promissory notes are generally held in the Central Banks of Member States. Each bank has an account opened in the name of the Treasurer. Only the representatives of the Treasurer are signatories to these accounts.

7. In one instance, promissory notes are sent directly to the Treasurer by the Member States for his/her custodial care.

### **Currency of Promissory Notes**

8. The notes are denominated and encashed in the currency or currencies as set out in the applicable governing rules of the particular Fund. They are encashed in the same original currency. In this respect, no exchange difference arises. If the encashed funds are in national currencies and they are transferred to the Treasurer's bank account, which is in US dollars, then it is very likely that exchange rate differences will occur.

### **System for Encashing Promissory Notes**

9. Notes are payable on demand. However, Member States are allowed in some instances to enter into separate arrangements with the Treasurer in order to draw up encashment schedules, provided that such schedules do not affect the operational needs of the Fund.

10. Encashment typically takes place twice a year, but there were provision in some funds for the notes to be encashed up to three times per year.

11. Notification of note encashment or draw downs are made to designated representatives of Member States. They in turn, instruct the designated banks to effect the necessary action. However, in some cases, the Treasurer had the authorization from the Member States to send their encashment requests directly to the designated banks. Such requests are usually in the form of authenticated faxes or SWIFT messages.

12. In an effort to ensure a fair, transparent and equitable encashment of the notes, the Treasurer generally attempts to encash notes on a pro rata basis among Member States at the agreed intervals as needed for disbursements.

13. At the request of a Member State, the Treasurer may agree to encash promissory notes on a basis other than pro rata. In all such cases, agreement for such notes must not be less favourable to the Fund.

14. When a payment of only a portion of a note is demanded, a notation of such partial payment is typically endorsed on the reverse of the note, or at the option of the Treasurer, a new note for the new balance is executed.

15. Transfers of notes to third parties are not undertaken.

### **Other Modes of Paying for Contributions**

16. Letters of credit were used by one Member State as the mode of payment. These letters are held by the Member State and encashed in a similar manner as Promissory Notes.

### **Advantages of using Promissory Notes as a Mode of Payment**

17. Promissory notes provide Member States with the opportunity to efficiently manage their cash outlay as a form of deferred payment since the notes are encashed only as agreed.

18. Implementing agencies are able to make commitments on their projects against future cash flows by use of the notes. Without the notes, such commitments would not be possible.

### **Disadvantages of using Promissory Notes as a Mode of Payment**

19. Failure or delays by the issuing country to honour the commitment as per the agreed encashment schedule.

20. Since notes are non-interest bearing, the Fund loses interest income. This loss leads to a reduction in the availability of resources.

21. With the denomination of some notes in national currencies, there is an exchange rate risk when the notes are encashed. The longer it takes to encash the notes, the more likely it is that the rate at the time of the encashment would be different from the rate at the time the notes were made.

### **RECOMMENDATIONS FOR CONSIDERATION**

22. In order to reduce wide fluctuations arising from exchange differences, all notes denoted for a particular year should be encashed at the end of the year to which they relate.

23. Member States should provide the Treasurer, in a timely manner, copies of all promissory notes.

24. Member States should ensure that the Treasurer is provided with quarterly bank account statements for all the promissory held with their banks.

25. The practice of assigning and/or passing of promissory notes to agencies should cease and the Treasurer should encash all the notes when due, but no later than the end of the relevant year. The proceeds should then be made available to the implementing agencies in the form of cash. This would eliminate exchange differences between the amounts passed on to the implementing agencies and the Treasurer's records. The Treasurer would have recognized any exchange differences arising between the original amount and the encashed value before sending the funds to the agencies.

26. Member States should make their notes in a standard format, which can be readily encashed by the Treasurer for disbursements.

27. The system of establishing encashment schedules should be regularized and made applicable to all Member States. With the approval of the encashment schedule, the dates should be strictly followed to the extent that the replenishment of the Fund is ensured.

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