Chapter 25: Private Sector Development

This document is intended to provide an overview of the way MCC conducts due diligence on private sector development activities.

Introduction

The due diligence process entails a rigorous analysis of the compact proposal received from an eligible country for the purpose of determining whether that proposal meets MCC criteria for funding. This document describes how that analysis is expected to be executed for Private Sector Development (PSD) components within compact proposals. It also provides best practice guidelines for due diligence of initiatives involving access to credit (specifically, on-lending) and legal and regulatory reform.

The first section (Objective and Approach) provides a brief overview of the objective of due diligence and the approach used by MCC. The second section (Due Diligence Requirements) contains questions which should guide the due diligence process for all PSD proposals. The third section (PSD Best Practice Guidelines) contains: (i) a set of general guidelines which PSD will use in assessing proposals, and (ii) standards and best practices to be used in assessing specific PSD initiatives such as access- to-credit and legal and regulatory reform. The objective of the PSD methodology is to ensure that the final compact proposals incorporating PSD will be as well-designed as possible.

Objective and Approach

The purpose of the due diligence process is to allow MCC to make an informed decision as to whether the proposed initiative is compliant with MCC guidelines, is likely to achieve the intended outcomes, and is designed in a manner which will achieve maximum results.

The PSD group undertakes due diligence through a three step process:

1. Assessing whether the proposed initiative is compliant with MCC requirements.
2. Assessing the initiative as proposed in regard to the likelihood of its accomplishing the stated developmental challenge.
3. Assessing whether the initiative is compliant with best practice guidelines.

PSD considers due diligence to be a critical part of the compact development process. Due diligence provides an opportunity for collaboration with core team counterparts to identify and reduce risks, strengthen proposed initiatives, ensure integration and linkages with other compact initiatives, and refine budgets and timelines. Due diligence also provides the basis for establishing any conditions precedent to be included in the legal agreements.

The due diligence process will culminate in a recommendation to either: (i) approve the initiative as-is; (ii) approve the initiative on a conditional basis (assuming certain changes); or (iii) disapprove the initiative.

MCC Due Diligence Requirements

Due diligence will commence when MCC has received a complete proposal from the core team. A complete proposal is one which includes an outline of the development challenge, the proposed initiatives which address the development challenge, the proposed budget for those initiatives, and an economic rate of return analysis.

Due diligence will be complete when PSD has reached a conclusion as to whether the initiative as finally proposed (following assessment of the proposal as-is and full exploration of how the proposal can be strengthened) is complaint with MCC requirements, is likely to achieve its objectives, and comports with PSD best practice guidelines.

In order to make this determination, PSD will assess the proposal according to the following two sets of questions (which incorporate and expand upon MCC's Due Diligence Checklist).

Does the initiative comply with MCC requirements?

Economic Growth and Poverty Reduction
- ★ Does the initiative show a clear and compelling link between economic growth and poverty alleviation?
- ★ Does the projected economic rate of return meet MCC requirements?
- ★ Is the projected economic rate of return based on logical and defensible logic?

Sustainability
- ★ Will the proposed initiative be sustainable (capable of continuation without third party support) following compact close?
- ★ If not, is there an acceptable rationale which would justify the initiative?
- ★ Does the initiative rely unnecessarily on subsidies or other forms of intervention which are unacceptable to MCC?
- ★ If so, is there an acceptable rationale for undertaking the initiative on that basis?
- ★ Will the initiative result in a market distortion?
- ★ If so, is there an acceptable rationale?

Social and Environmental
- ★ Does the proposed initiative impair gender equality? Does it help strengthen gender equality?
- ★ Does the proposed initiative violate environmental responsibility?
- ★ Is the supply of skilled human resources sufficient to build and sustain the innovation? If not, how should this be addressed?

Fiscal Accountability
- ★ Are the procedures for the flow of funds from MCC to accountable entities to implementing agents and sub-agents clearly documented?
- ★ If funds will not be fully expended by compact maturity, has the disposition of financial assets by the end of the compact period been finalized in accordance with the MCC policy on Financial Intermediation Activities and Instruments Extending Beyond the Compact Termination Date?
- ★ Have all costs, risks and timelines for initiating, running and closing the initiative been properly estimated?
- ★ Have performance indicators been identified which can effectively track progress of the initiative and is the data sex-disaggregated whenever possible?

Consultative Process/Country Ownership
- ★ Does the proposed initiative provide evidence that it is the outcome of a broad collaborative approach among all stakeholders?

Donor Coordination
- ★ Have other donor, NGO and governmental-funded financial sector initiatives been reviewed to ensure proper coordination and non-overlap?
- ★ Is the proposed initiative part of the country's national strategy and/or congruent with the country's Poverty Reduction Strategy Paper (PRSP)?

Will the initiative accomplish the stated developmental challenge?

Project Design
- ★ Does the initiative address a key developmental challenge (a major impediment to economic growth and poverty reduction)?
- ★ Is the initiative likely to resolve or make considerable progress in resolving that developmental challenge?
- ★ Has the developmental challenge been effectively defined?
- ★ Does the proposal provide a full consideration of the alternatives, and does it document why the proposed initiative is the optimal (least cost and most effective) option?
- ★ Are the goals of the initiative clearly stated?
- ★ What are the proposed activities/inputs which will be undertaken through the initiative?

- What are the expected outputs which will result from the proposed activities and how likely is it that they will be achieved?
- What are the expected outcomes which will result from the initiative, and how likely is it that these outcomes will be achieved?
- How likely is it that the proposed outcomes from the project will overcome the identified developmental challenge, and is this manifested in the economic logic (rate of return)?
- Do the proposed interventions support and link to other elements of the compact?
- Is the size of the proposed initiative appropriate to the target set of beneficiaries?
- Have private sector alternatives been explored to ensure no 'crowding-out' of the private sector in the subject area?
- Has a set of measurement indicators been developed which can track progress against expected objectives, with relevant data sex-disaggregated?

Implementation, Oversight and Budget

- Who is the identified implementing agent?
- How likely is it that the implementing agent will be able to effectively execute the initiative?
  - Is the implementing agent genuinely committed to the initiative?
  - Does the implementing agent have the capacity to manage and report effectively?
- If there are sub-agents (for example, banks involved in on-lending programs), how likely is it that the sub-agents can effectively execute?
  - Is there strong interest in participation in the initiative?
  - Do the sub-agents have the capacity to manage and report effectively?
- How likely is it that the accountable entity oversight body entity will be able to effectively oversee the implementing agent?
- Is the proposed budget sufficient to fund the proposed activities?
- Is the proposed timeline (including intermediate results, milestones and deliverables) reasonable?

Legal and Regulatory/Enabling Environment

- Are there legal and regulatory constraints which will impair the effectiveness of the initiative?
- Do any legal/regulatory constraints particularly impact the ability of vulnerable groups such as women and youth to participate and benefit from projects?
- If so, what measures will be taken to ameliorate any relevant legal and regulatory impediments to the success of the initiative?

Supply, Demand and Accessibility

- Is there strong demand for the products or services proposed to be delivered through the initiative?
- Are the proposed products/services to be delivered not otherwise available?
- What is the likelihood that the targeted beneficiary group will be able to access and use the products and services?

Incorporating Best Practices and Lessons Learned

- Does the proposed initiative reflect international best practices and have proposed activities been shaped by lessons learned from past projects?

PSD Best Practice Guidelines

In performing due diligence of PSD initiatives the following guidelines should be applied to ensure that the initiative as finally proposed incorporates PSD lessons learned and best practices. This section includes general requirements which provide a lens through which any and <u>all</u> PSD proposed initiatives should be reviewed. It also provides specific requirements which provide best practices in specific subject areas, such as in the areas of access to credit and legal and regulatory reform.

General Requirements

Economic Growth and Poverty Reduction
The proposed initiative should provide compelling evidence that the identified development challenge is a key constraint to poverty alleviation through economic growth. It should clearly demonstrate how the proposed initiative will overcome that challenge, and how this will result in growth and poverty reduction. It should incorporate an economic rate of return analysis per MCC policy, and should include a clear and justifiable underlying logic for the calculation.

In many cases, proposed PSD initiatives will tie in with and/or augment other MCC investments. If so, clear linkages must be made between the overarching compact objectives and how the PSD initiatives will support them.

Sustainability and Subsidies
The proposal should address whether the proposed initiative will be sustainable following the end of the compact. All PSD initiatives do not necessarily need to be sustainable – some may have a specific purpose and intended life if intended to address a market failure or severe market distortion. If the initiative is not intended to be sustainable, it should identify the rationale as to why this is acceptable.

The proposal should address whether the initiative relies on subsidies, partial guarantees or other forms of intervention in the market. If so, it should discuss the rationale for the subsidy and/or intervention, and should identify and document any deviance from World Bank OP 8.30. Subsidies may be appropriate if they are: (i) economically justified; (ii) transparent, targeted and capped; and (iii) do not create unfair competition.

Social and Environmental
The proposal should address MCC's social and environmental requirements and explain how the initiative will comply with MCC's social and environmental policies.

Fiscal Accountability
The proposal should describe the flow of funds from MCC to accountable entity to implementing agents and sub-agents, and explain how these funds will be monitored and audited. Where possible the flow of funds should be shown in graphic form. The proposal should describe the how disposition of financial assets at the end of a compact period (if any) will comply with MCC policy.
The proposal should address how the costs, risks and timelines for initiating, running and closing down the initiative were estimated.

Consultative Process/Country Ownership
The proposal should describe how the initiative was developed in light of the MCC requirement for a broad, collaborative process. The proposal should address how this process was undertaken, and how it has culminated in the proposed initiative.

Donor Coordination
The proposal should demonstrate a strong understanding of previous and on-going donor PSD initiatives. The proposal should demonstrate that it has been developed in consultation and coordination with other donor, NGO and governmental PSD sector initiatives and should incorporate lessons learned from those initiatives. It should integrate with those activities and present a plan for on-going coordination. As part of due diligence, a synopsis of other donor, NGO and government PSD initiatives should be included.

Project Design
The project design should clearly articulate the development challenge which the initiative is designed to address, why the developmental challenge identified is critical, and what proposed activities will be undertaken through the initiative to meet the development challenge. It should identify the outputs which are expected to result from the inputs and show the linkage between inputs and outputs (how does the former accomplish the latter). It should address the expected outcomes (the end result of the initiative), the likelihood of the expected outcomes being achieved, and the ways in which outcomes will be measured (sales growth, amount of loans outstanding,

value of exports, etc.). Finally, it should demonstrate a clear linkage between the expected outcomes and the developmental challenge – how the proposed outcomes are expected to overcome the identified developmental challenge.

There are three general baskets of PSD assistance instruments: (i) Financial Support (loans, grants, credit guarantees, equity investment); (ii) Advisory Services (technical assistance and training); and (iii) Enabling Environment Strengthening (legal and regulatory, investment climate). Most successful PSD projects provide an integrated package of these three elements, building upon the various initiatives which may already be in place.

Risk need to be identified and, to the extent possible, mitigation strategies should be documented and built into the program design. Risks to be considered include not only the risk that a program has unintended consequences (e.g. a higher loss rate than anticipated) but also the risk that demand for the product is significantly higher or lower than the assumed level of demand.

Due diligence should discuss whether the proposed initiative will duplicate other private sector funded initiatives. Generally, MCC will not support activities which result in 'crowding-out' of the private sector. Given the size of the MCC footprint, however, the proposed PSD initiative may be able to perform an organizing role in harmonizing the many smaller PSD initiatives which are likely to be in place.

Due diligence must show how (to the extent possible) the initiative is coordinated with other initiatives proposed within the compact. The proposal should provide a means of measuring progress, including a baseline (starting measurements) and performance indicators that are sex-disaggregated, to the extent possible, and reported on a periodic basis.

Implementation, Oversight and Budget

The proposal should address how the initiative will be implemented, overseen and funded. It should identify who the implementing agent is proposed to be and in what ways the implementing agent is qualified for that role.

If there are sub-agents (for example, banks involved in on-lending programs) it should address how those sub-agents will be selected. The proposal should address how determination will be made of the effectiveness of the sub-agents to serve as financial intermediaries and to manage and report effectively.

The proposal should address the proposed budget and demonstrate that it is sufficient to fund the proposed activities.

Cost estimates may be difficult to assess because of different cost structures of potential providers. For example, the costs of a technical assistance provider based in Europe may be different than for a US-based provider because of exchange rates, transportation costs, and wage scales. Budgets should generally assume a relatively high-cost provider so as not to under-fund projects.

Legal and Regulatory/Enabling Environment

The proposal should discuss the overarching environment in which the initiative will occur and any factors therein which will have an impact on the success of the initiative. This will include the legal and regulatory environment (e.g., legislation supporting enforcement of property rights, the capacity of the courts to enforce this legislation, ambiguity or inequality in regards to women's rights to own land or access credit) and the overall enabling environment (e.g., employment flexibility, restrictive labor laws that bar women from working after certain hours or in certain industries, constraints to transfer/export of products).

Supply, Demand and Accessibility

The proposal should address the demand for the products or services which are proposed to be delivered through the initiative. It should address whether the proposed products and services to be delivered are available in the market place, and if not, why not. If the products and services are available, it should address whether the initiative will be duplicative, and if not, what will be different.

It should address the ability of the targeted beneficiary group to access the products and services, and in the case of credit programs, the physical access of beneficiaries to financial institutions.

Incorporating Best Practices and Lessons Learned

Due diligence should address how the proposal incorporates lessons learned and best practices, where possible drawing from the results achieved by similar initiatives.

Specific Requirements: On-Lending Initiatives

Is the identified development challenge a key constraint to poverty reduction through economic growth?

Broadly speaking, private sector enterprises are affected by three factors: (i) demand for their goods and services, (ii) the business environment in which they operate, and (iii) the way in which they respond to market opportunities. The ability of firms to respond to market opportunities is strengthened when they can access credit. But care must be taken to distinguish among differing circumstances in which access to credit might be cited as the problem. Low levels of lending may be attributable to appropriate risk aversion on the part of lenders, market distortion or failure, or to a lack of suitable demand. Efforts should be made to ascertain the specific causes of the problem so that the root causes can be addressed along with the symptoms.

Will improving access to credit provide a credible solution to the developmental challenge?

If access to credit is determined to be a key constraint, assessment should be undertaken as to whether the initiative as proposed will be effective in solving the developmental challenge in light of the framework identified above (demand for good and services, business environment and firm response). In general, financial services in most developing and transitional economies do not adequately serve the needs of small and growing businesses. However this is usually less a function of supply (liquidity) and more of a problem of insufficient intermediation skills, weak enabling environment and inappropriate credit instruments, among other possible factors. As such, program design should take into consideration: (i) the beneficiaries who should benefit from the program; (ii) the enabling environment in which the program will be implemented; (iii) the proposed intermediaries who will implement the access to credit programs; and (iv) the financial instruments to be used.

Beneficiaries and Demand

The perception of a financing gap may mask fundamental problems at the firm level or within the enabling environment. To what extent does demand for credit outstrip supply, and what is the cause? Is it an issue of pricing, extreme risk aversion on the part of lenders, the legal and regulatory environment, lack of acceptable credit proposals, or a combination thereof?

If a financing facility is proposed, documentation should be provided that the size of the facility proposed is appropriate to the target set of beneficiaries and within the capacity of the institutions which would act as financial intermediaries. Where specifically is the unmet demand – which is the specific target audience?

Consideration should be given to developing the capacity of the beneficiaries to act as effective borrowers. Increasing financial literacy may result in stronger proposals, thereby lowering transaction costs and risk premium.

Programs which offer mentoring/advisory services in conjunction with other forms of supply-side support to financial intermediaries seem to have greater success. To what extent are or should business advisory services be available to potential beneficiaries as part of the program?

The most important test of whether an intervention will be successful is whether beneficiaries will exploit it. It is important to assess what obstacles may exist from the perspective of the targeted beneficiaries, e.g. literacy, lack of familiarity/trust with financial intermediaries, cultural attitudes toward debt, etc.

Enabling Environment

A review of the system of contract enforcement and dispute resolution should be done to assess whether attention needs to be extended to reforms that may influence the extension of private credit. The World Bank's "Doing Business" reports generally provide insight as to whether non-credit issues explain access to credit problems.

For example, it is often difficult in emerging markets to perfect a security interest in collateral, and to enforce that security interest in the event of default. Insolvency procedures are often unreliable and subject to judicial discretion. In some cases this can be mitigated through the introduction of secured lending/commercial finance techniques in combination with the introduction of a pledge registry for movable property.

Accurate information is also a universal problem in developing countries. Accounting and auditing practices are often weak, and credit information is often difficult to obtain.

In addition, certain barriers in the legal and regulatory environment may prevent women from accessing credit, such as unequal access to property in a collateral-based banking system. An assessment of such potential barriers should be made, and potential solutions recommended to remove any existing gender barriers.

Intermediaries/Implementers

In most cases, supporting existing financial institutions (on-lending) is preferable to creating stand-alone SME credit programs. However this will depend upon the capacity of the proposed participating financial institutions – in some instances, de novo special purpose institutions have been instrumental in fostering competition and providing lighthouses for other institutions.

Attention should be given to the credit culture of the proposed financial intermediaries. While losses are to be expected, programs should not be supported if it is unlikely that losses cannot be stabilized at an acceptable level before the end of the compact period.
The capability of a small financial institution, e.g. an MFI, to deliver new financial instruments should be carefully questioned. Interviews with such intermediaries are necessary to determine both their willingness to participate, their capacity to underwriting effectively, and whether additional capacity building efforts may be required. Consideration needs to be given to how intermediaries have performed in other donor programs and their ability to file reliable reports in a timely manner.
Criteria need to be in place to determine which financial institutions are eligible to participate.
Interviews with regulators, when available, are important to make sure that financial institutions that are on watch lists are not included as participants unless special controls are added.

If institutional strengthening is proposed, documentation should be provided showing how the provision of technical assistance to financial institutions or regulators will support the creation of a stronger credit culture, increased competition within the financial sector, improve regulation, or otherwise strengthen the financial sector.

Flexibility should be maintained to adjust program terms during the compact period to respond to actual loan or guarantee loss experience. In identifying participating financial institutions, care should be given to ensuring broad geographic coverage and the ability of beneficiaries to physically reach financial institutions and vice versa. If this problem is not addressed, high delivery costs may make a project unrealistic.

Instruments/Initiatives

Consideration should be given to the credit instruments which will be offered. Banks in developing countries will often lend only on the basis of real property (land and buildings) and/or on personal guarantees, which has the effect of excluding poor applicants and female applicants with good ideas but limited collateral.

Tenor is a particular problem in most developing countries – banks are rarely willing to lend on a medium to long term basis (2-5 years). Few investments are likely to have a repayment horizon which can be met on a short-term basis. A common problem for SMEs is a lack of financing for SMEs above the micro-finance level and below the level at which commercial banks generally show interest. Attention should be given to requirements for funding with regard to both size and term.

Inclusion of subordinated or quasi-equity instruments should be considered (e.g., preferred stock, debt with warrants). But such instruments need to be reviewed to determine if they can be easily understood by providers as well as beneficiaries and should require minimal legal documentation.

What are the alternative credit instruments with which the proposed activity would compete? MCC project should not dissuade other private sector entrants, including MFIs, in a meaningful way.

Is the proposed initiative properly structured?

Fiscal accountability concerns are particularly high in on-lending programs because of the potential for corruption and capture. Too often, beneficiaries have seen on-lending programs as grant programs in disguise with resulting low rates of repayment.

Oversight/Accountability

Procedures for the flow of funds from MCC through accountable entity to financial intermediaries must be understood and documented. Proper auditing and monitoring procedures should be established within the proposal.

Estimated budget and timeline

The proposed timeline should demonstrate the ability to accomplish the intended initiative within the compact period (with the ability of access to credit programs to extend beyond compact-end).

Impact measurement and results indicators

The proposal should document the intended impact from the initiative and the intermediate indicators by which results will be measured. In access to credit programs, indicators may include:

- ★ Loan disbursement
- ★ Revenues
- ★ Job creation

Compliance with MCC gender and environmental requirements

The proposal should document that the initiative will comply with MCC guidelines:

- ★ Analyze particular barriers that women may face in accessing credit. This includes examining legislation and regulations that may create special barriers for women, such as collateral requirements, loan co-signatory requirements, discriminatory bank practices, weak or non-existent credit registries that do not capture women's repayment records in microfinance, and women's lack of financial and business management skills that may result in lower ability to comply with bank requirements during the loan application process.
- ★ Design programs that support women's ability to access credit in all forms (geographic, business line, funding). This includes, among others, addressing issues identified in the above analysis by adjusting collateral requirements, reforming discriminatory regulations, and tailoring training activities to women.
- ★ Loan eligibility criteria prohibit loans for banned pesticides and chemicals in accordance with partner country standards and MCC environmental guidelines.

Will the proposed initiative be sustainable?

In general, access to credit programs should be designed to be sustainable; however in some instances (market failure) such programs may be structured on a special purpose basis. Subsidizes can be appropriate so long as the are highly targeted, fill a specific market need, and are not intended to be perpetual.

Sustainability of participating institutions and transfer to skills

Consideration should be given to the credit culture (underwriting and portfolio management skills) of participating institutions. In almost all cases, on-lending programs should include a technical assistance component to transfer credit/risk management skills to participating institutions.

Particular attention should be given to the selection of participating institutions with regard to capital adequacy and the ability to absorb losses.

Use of subsidies

Subsidies can take multiple forms. Interest rate subsidies that are directed at intermediaries as an inducement are more acceptable than subsidies directed at end users (borrowers), but should in any case be tested to determine the extent to which they might dissuade private sector participation in the same activity.

Subsidies may be used as an inducement in selected circumstances to draw financial institutions toward new market segments or regions. Such subsidies might include full or partial reimbursement of operation costs for a short period of time. However, such subsidies are appropriate only when there is a likelihood of sustainability when these inducements cease.

Partial guarantee structures that guarantee intermediary losses in excess of 50% should generally be rejected as carrying too high a degree of moral hazard. Partial guarantee programs may be used when there is judged to be a difference between lenders' perceived risks and actual market risk. However, in such cases, technical assistance will usually be required to upgrade credit analysis and risk management skills so that market activity will persist beyond the end of the guarantee program.

Transition plan

MCA counterparties should be aware of the MCC policy with respect to the disposition of financial assets at the end of a compact period, and (if so intended) the proposal should document how the proceeds from the initiative will be transferred and tracked.

Is the proposal coordinated with other Private Sector Development initiatives as well as other elements within the compact?

It is likely that there will be several other micro-finance and/or on-lending programs in place. As such, it is particularly important that the MCC funded program compliment and not compete with other programs. In addition, MCC on-lending initiatives should be developed in harmony with other compact initiatives to as to leverage compact impact.

Coordination with other donor/governmental initiatives

Most developing countries have numerous micro-finance programs and many have SME on-lending facilities. Proposals should ensure that these programs are identified, and that pricing and terms on these programs be roughly comparable.

On-lending proposals should show how the MCC funded program will be uniquely targeted and not simply additive. Due diligence should address consultations held with all the key donors and NGOs and document the outcomes of these meetings.

Coordination with other compact initiatives

Generally on-lending programs will be structured to support other compact components focusing on rural or SME development. Care should be taken to consider areas of overlap with these activities to align the geographic coverage and take into consideration other donor programs operating on the same population or area.

The sequencing of activities should be consistent with the sequencing and timelines for the activities that the financial sector intervention is expected to support.

Specific Requirements: Legal and Regulatory Reform

Is the identified development challenge a key constraint to poverty reduction through economic growth?

The legal and regulatory environment in which businesses must operate is a critical factor in private sector development. That said, more often than not legal and regulatory reform initiatives are likely to be elements within initiatives rather than overt stand-alone initiatives.
In compact initiatives in which legal and regulatory reforms are proposed, the proposal should clearly document the intended benefit of such reforms in terms of economic impact. If legal and regulatory reforms are proposed as a sub-activity within another activity, the proposal should reflect what the impact will be if the reforms are not accomplished.

Is the proposed initiative a credible solution to the developmental challenge?

In order to have the intended impact, legal and regulatory reforms must not only be embodied as changes in law, but embodied in the overall legal, economic and social fabric as well. For example, if the proposed activity is primarily focused on improving the operations of courts, it may also be concerned with upgrading other related components in the legal system (e.g., private bar, law schools, lawyers in government agencies), to avoid uneven progress in the system.

Beneficiaries and Demand

The proposal should document how the intervention will overcome the identified impediment – from the practical perspective of the beneficiary.

Enabling Environment

The proposal should address the overarching enabling environment, particularly related policies, laws, regulations and procedures. This is the water in which the activity swims or drowns. For example, if an initiative aims to build courts to improve access to justice, it must also consider all of those aspects beyond bricks and mortar – issues of capacity building, dissemination of information, and case management to note just a few.

Implementation

Laws and regulations are implemented through the justice system, and the proposal must document how legal and regulatory changes will be implemented and enforced. For example, several developing countries have adopted modern bankruptcy laws; however the judicial system commonly refuses to enforce such laws as a matter of social custom.

Is the proposed initiative properly structured?

The proposal should describe the flow of funds as well as oversight. MCA counterparties should be aware that if governmental entities will be implementing the initiative, there are particular limits to what MCC can support (i.e., goods or outside consultants are permissible, but salaries or other payments to government officials are not). The proposal should provide some sort of starting measurements, whether our goal is to speed the resolution of commercial disputes, or increase the number of labor disputes that are addressed through mediation.

Impact measurement and results indicators

Indicative indicators for legal and regulatory reform achievement might include:

- the speed the resolution of commercial disputes
- The increase the number of labor disputes that are addressed through mediation.

Compliance with MCC gender and environmental requirements

The proposed activity should support women's access to justice, legal services, or other law-related services. The activity should promote broader access to legal services, particularly to disadvantaged groups, and not just expand services to groups (such as business owners) that may already have greater advantages than ordinary citizens.

Geographic issues should be documented in the proposal – the initiative should have significant impact beyond merely the capital or major cities.

Will the proposed initiative be sustainable?

In the case of legal projects particularly, sustainability may largely depend on government budgets, rather than increased revenues, as well as sustained political will.

Sustainability of participating institutions

The proposal should document the commitment of the government to fully fund legal and regulatory reform initiatives, as well as the likelihood that the policies, laws and regulations be made and implemented on a consistent and transparent basis.

Consideration should be given to whether there is a personal or political dynamic that prevents or corrupts change or is not being harnessed to promote change.

Transfer of skills

With initiatives which will require a new set of skills or expertise, the proposal should document how training/skills transfer will be executed. Where skills transfer is proposed, it should identify how the persons responsible for policy and implementation with respect to the activity will gain the knowledge they need to make good decisions and implement them.

Is the proposal coordinated with other Private Sector Development initiatives as well as other elements within the compact?

It is particularly important that proposed legal and regulatory reform initiatives emerge from a true consultative process, and are coordinated with other legal and regulatory/judicial reform initiatives.

Coordination with other donor/NGO/governmental initiatives

The activity should evidence input from all relevant legal groups (government, judiciary, private bar, academia, law-related NGO's, women's legal and advocacy groups) as well as non-groups private business, civil society, and others.

Coordination with other compact initiatives

In virtually all cases, legal and regulatory reforms will coordinate directly with other compact initiatives. The proposal should make a clear linkage between the activities and the intended cause and effect.