

The World Bank Group

INTERNATIONAL BANK FOR RECONSTRUCTION
AND DEVELOPMENT
AS TRUSTEE AND ADMINISTRATOR FOR THE
PROTOTYPE CARBON FUND
WORLD BANK REFERENCE
TF023446

REPORT AND FINANCIAL STATEMENTS
June 30, 2002



Trust Funds Division

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AND DEVELOPMENT
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**REPORT AND FINANCIAL STATEMENTS
June 30, 2002**

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INDEPENDENT AUDITORS' REPORT

To: International Bank for Reconstruction & Development
as Administrator for the Prototype Carbon Fund

We have audited the accompanying balance sheets for the Prototype Carbon Fund for which the International Bank for Reconstruction and Development (IBRD) acts as Trustee and Administrator, as of June 30, 2002 and June 30, 2001 and the related statements of income (loss), changes in equity and cash flows for the years then ended. These financial statements are the responsibility of IBRD's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and International Standards on Auditing. Those standards require that we plan and perform our audit to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such financial statements present fairly, in all material respects, the financial position of the Prototype Carbon Fund as administered by the International Bank for Reconstruction and Development at June 30, 2002 and June 30, 2001, and the results of its operations and its cash flows for the years then ended in conformity with International Accounting Standards.

Deloitte Touche Tohmatsu (International Firm)

November 18, 2002

PROTOTYPE CARBON FUND

BALANCE SHEETS

As of June 30, 2002 and June 30, 2001

Expressed in U.S. dollars

	<u>June 30, 2002</u>	<u>June 30, 2001</u>
ASSETS		
Equity in pooled investments (Note 2)	\$ 14,391,580	\$ 12,104,204
Investment income receivable (Note 2)	62,509	154,153
Receivable from other trust funds (Note 3)	21,405,610	20,722,323
Advance payment for emission reductions (Notes 2, 5)	595,000	300,000
Valuation allowance for advance payments (Note 6)	(595,000)	(300,000)
	<u>35,859,699</u>	<u>32,980,680</u>
TOTAL ASSETS	<u>\$ 35,859,699</u>	<u>\$ 32,980,680</u>
LIABILITIES AND EQUITY		
LIABILITIES:		
Accrued fund development expenses (Note 2)	\$ 930,000	\$ 1,200,000
Accrued project development expenses (Note 2)	193,000	193,000
Accrued administrative expenses (Note 2)	178,281	17,162
Accrued performance-linked expenses (Note 4)	140,000	90,000
	<u>1,441,281</u>	<u>1,500,162</u>
Total liabilities	1,441,281	1,500,162
EQUITY:		
Capital contributions pledged (Note 2)	145,000,000	145,000,000
Notes receivable on capital contributions (Note 2)	(102,117,990)	(109,137,677)
Capital contributions paid in (Notes 1, 2)	42,882,010	35,862,323
Retained deficit	(8,463,592)	(4,381,805)
	<u>34,418,418</u>	<u>31,480,518</u>
Total equity	34,418,418	31,480,518
TOTAL LIABILITIES AND EQUITY	<u>\$ 35,859,699</u>	<u>\$ 32,980,680</u>

See notes to financial statements.

PROTOTYPE CARBON FUND

STATEMENTS OF INCOME (LOSS)

For the Year Ended June 30, 2002 and the Year Ended June 30, 2001

Expressed in U.S. dollars

	July 1, 2001 to June 30, 2002	July 1, 2000 to June 30, 2001
REVENUE		
Realized investment income (Note 2)	\$ 872,621	\$ 981,758
Net unrealized gain on equity in pooled investments (Note 2)	57,985	127,228
Premium income (Note 2)	11,315	18,000
Total revenue	<u>941,921</u>	<u>1,126,986</u>
EXPENSES		
Project-related expenses - project preparation (Note 2)	2,977,619	966,660
Performance-linked expenses (Note 4)	90,000	90,000
Administrative expenses (Note 2)	1,661,089	1,291,133
Valuation allowance for advance payment expense (Note 6)	295,000	300,000
Total expenses	<u>5,023,708</u>	<u>2,647,793</u>
NET LOSS	<u><u>\$ (4,081,787)</u></u>	<u><u>\$ (1,520,807)</u></u>

See notes to financial statements.

PROTOTYPE CARBON FUND

STATEMENTS OF CHANGES IN EQUITY

For the Year Ended June 30, 2002 and the Year Ended June 30, 2001

Expressed in U.S. dollars

For the Year Ended June 30, 2001

	<u>Capital Contributions</u>	<u>Notes Receivable</u>	<u>Retained Deficit</u>	<u>Total Equity</u>
BALANCE, JULY 1, 2000	\$ 135,000,000	\$ (108,356,569)	\$ (2,860,998)	\$ 23,782,433
CAPITAL CONTRIBUTIONS:				
Public sector participants	-	5,278,892	-	5,278,892
Private sector participants	10,000,000	(6,060,000)	-	3,940,000
Net loss	-	-	(1,520,807)	(1,520,807)
BALANCE, JUNE 30, 2001	<u>\$ 145,000,000</u>	<u>\$ (109,137,677)</u>	<u>\$ (4,381,805)</u>	<u>\$ 31,480,518</u>

For the Year Ended June 30, 2002

	<u>Capital Contributions</u>	<u>Notes Receivable</u>	<u>Retained Deficit</u>	<u>Total Equity</u>
BALANCE, JULY 1, 2001	\$ 145,000,000	\$ (109,137,677)	\$ (4,381,805)	\$ 31,480,518
CAPITAL CONTRIBUTIONS:				
Public sector participants	-	3,398,887	-	3,398,887
Private sector participants	-	3,620,800	-	3,620,800
Net loss	-	-	(4,081,787)	(4,081,787)
BALANCE, JUNE 30, 2002	<u>\$ 145,000,000</u>	<u>\$ (102,117,990)</u>	<u>\$ (8,463,592)</u>	<u>\$ 34,418,418</u>

See notes to financial statements.

PROTOTYPE CARBON FUND

STATEMENTS OF CASH FLOWS

For the Year Ended June 30, 2002 and the Year Ended June 30, 2001

Expressed in U.S. dollars

	July 1, 2001 to June 30, 2002	July 1, 2000 to June 30, 2001
	<u> </u>	<u> </u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (4,081,787)	\$ (1,520,807)
Adjustments to reconcile net loss to net cash used in operating activities:		
Increase in unrealized gain on pooled investments	(57,985)	(127,228)
Decrease/(Increase) in investment income receivable	91,644	(115,942)
Increase in receivable from other trust funds	(683,287)	(2,458,892)
Increase in advance payment for emission reductions	(295,000)	(300,000)
Increase in allowance for advance payment	295,000	300,000
Increase/(Decrease) in accrued administrative expenses	161,119	(23,466)
Decrease in accrued fund development expenses	(270,000)	(400,000)
Decrease in accrued project development expenses	-	(233,000)
Increase in accrued performance-linked expenses	50,000	65,000
	<u> </u>	<u> </u>
Net cash used in operating activities	(4,790,296)	(4,814,335)
	<u> </u>	<u> </u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(2,229,391)	(4,404,557)
	<u> </u>	<u> </u>
Net cash used in investing activities	(2,229,391)	(4,404,557)
	<u> </u>	<u> </u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital contributions	7,019,687	9,218,892
	<u> </u>	<u> </u>
Net cash provided by financing activities	7,019,687	9,218,892
	<u> </u>	<u> </u>
NET INCREASE IN CASH	<u> </u>	<u> </u>
	-	-
CASH, BEGINNING OF PERIOD	<u> </u>	<u> </u>
	-	-
CASH, END OF PERIOD	<u> </u>	<u> </u>
	\$ -	\$ -

See notes to financial statements.

PROTOTYPE CARBON FUND

NOTES TO FINANCIAL STATEMENTS

June 30, 2002

1. ORGANIZATION AND OPERATIONS

The Prototype Carbon Fund (the Fund) was established in 1999 by the International Bank for Reconstruction and Development (IBRD) as a mechanism to help countries reduce global concentrations of greenhouse gases (GHG) and thereby minimize the adverse impacts of climate change on developing countries. The operational principles of the Fund are: (1) to invest in projects that are intended to generate high-quality GHG emission reductions in developing countries and countries with economies in transition, (2) to endeavor to effect an equitable sharing between the Fund participants and the developing countries of any emission reductions and other benefits arising from such projects, and (3) to disseminate broadly the knowledge gained in the development of the Fund and the implementation of the projects.

The Fund is administered by the IBRD as Trustee. Pursuant to the Fund's governing document, the Trustee is authorized, among other things, to accept capital contributions to the Fund from the participants, invest the funds collected, and establish a committee responsible for overseeing the operations of the Fund (the Fund Management Committee).

There have been two closings of the Fund representing the deadline for entering into Participation Agreements. As of the First Closing of the Fund on April 20, 2000, six Public Sector participants and 15 Private Sector Participants had purchased an interest in the Fund by signing Participation Agreements. As of the Second Closing of the Fund on October 31, 2000, two additional Private Sector Participants had entered into Participation Agreements. Public Sector Participants were each required to contribute US\$10 million to the Fund and Private Sector Participants were each required to contribute US\$5 million. Participants provided their contributions either through the delivery of an unconditional promissory note made payable to the Trustee upon demand, or through advance payments to separate holding trust funds managed by IBRD as Trustee. As of June 30, 2002 and June 30, 2001, capital contributions paid in by the Participants, are as follows:

NOTES TO FINANCIAL STATEMENTS
June 30, 2002

Expressed in U.S. dollars

Public Sector Participants	Amounts paid as of June 30, 2002	Amounts paid as of June 30, 2001
Canada	\$ 1,182,600	\$ 730,000
Finland	1,182,600	730,000
Japan Bank for International Cooperation	1,182,600	730,000
Netherlands	1,182,600	730,000
Norway	1,182,600	730,000
Sweden	1,182,600	730,000
Total Public Sector Participants	\$ 7,095,600	\$ 4,380,000
Private Sector Participants	Amounts paid as of June 30, 2002	Amounts paid as of June 30, 2001
BP Amoco	\$ 586,300	\$ 360,000
Chubu Electric Power Company Inc.	586,300	360,000
Chugoku Electric Power Company Inc.	586,300	360,000
Deutsche Bank	5,000,000	5,000,000
Electrabel	586,300	360,000
Fortum OYJ	586,300	360,000
Gilde Strategic Situations B. V.	586,300	360,000
Gaz de France	586,300	360,000
Kyushu Electric Power Company Inc.	586,300	360,000
MIT Carbon Fund	586,300	360,000
Mitsubishi	586,300	360,000
Norsk Hydro ASA	586,300	360,000
RWE Aktiengesellschaft	586,300	360,000
Shikoku	586,300	360,000
Statoil	586,300	360,000
Tohoku Electric Power Company Inc.	586,300	360,000
Tokyo Electric Power Company Inc.	586,300	360,000
Total Private Sector Participants	\$ 14,380,800	\$ 10,760,000
Total all Participants	\$ 21,476,400	\$ 15,140,000
Plus receivables from other trust funds	21,405,610	20,722,323
Total Capital Contributions Paid In	\$ 42,882,010	\$ 35,862,323

continued

NOTES TO FINANCIAL STATEMENTS

June 30, 2002

2. SUMMARY OF SIGNIFICANT ACCOUNTING AND RELATED POLICIES

Basis of Accounting - The accompanying financial statements are prepared in accordance with International Accounting Standards. These financial statements are presented on a comparative basis for two fiscal periods: year ended June 30, 2002 and year ended June 30, 2001.

Use of Estimates - The preparation of financial statements in conformity with International Accounting Standards includes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

Cash - The Fund places the funds it receives from the Participants under IBRD investment management (see *Equity in Pooled Investments*).

Equity in Pooled Investments - Amounts paid into the Fund, but not yet disbursed, are managed by IBRD, which maintains a single investment portfolio (the Pool) for all of the trust funds administered by IBRD and the International Development Association (IDA). Under the Pool's current investment strategy, a significant portion of the Pool is invested in liquid instruments such as U.S. Treasury securities and other high-grade bonds.

IBRD maintains the investments on a pooled accounting basis: investment income is allocated to each trust fund on a pro-rata basis. Equity in pooled investments represents the Fund's pro-rata portion of the Pool's market value at the end of the period. The corresponding pro-rata realized and unrealized gains or losses accrue to the Fund in the period in which they occur.

Capital Contributions - The Fund derives its funding primarily from contributions provided by its Participants. Each Participant's contribution is recorded in full as Capital Contributions Pledged upon execution of a Participation Agreement between the Participant and the Fund. Amounts not yet paid in are recorded as Notes Receivable on Capital Contributions and shown as a reduction of Capital Contributions Pledged on the balance sheet. The notes receivable are settled through cash payments upon the Trustee's request, in accordance with an annual budget and business plan approved by the Participants.

Advance Payment for Emission Reductions - The Fund enters into agreements for the purchase of emission reductions (ERs) with external parties. In some instances, the purchase agreements contain provisions for the Fund to pay for ERs prior to their delivery. Such prepayments are recorded by the Fund in the balance sheet as Advance Payment for Emission Reductions. The amounts accumulated in the Advance Payment for Emission Reductions account will be reclassified to Emission Reductions on the balance sheet when qualifying ERs are delivered to the Fund. Due to significant uncertainties surrounding the quantities and value of ERs for which the advance payments are made, an appropriate allowance has been established.

continued

NOTES TO FINANCIAL STATEMENTS

June 30, 2002

2. SUMMARY OF SIGNIFICANT ACCOUNTING AND RELATED POLICIES *(continued)*

Premium Income - Participants who enter into Participation Agreements after the First Closing pay the Fund a premium in an amount equal to 2.5% of their required annual contributions. The premium payments are not taken into account in determining the Participants' interests in the Fund, or in the calculation of the size of the Fund. Income from premiums is recognized in the statements of income (loss) as earned.

Fund and Project Development Expenses - The Fund will reimburse the Trustee for 80% of all costs and expenses incurred by the Trustee prior to the First Closing in relation to the development of the Fund, not to exceed \$2 million, which is to be paid in five equal annual installments. In addition to these amounts, the Fund will also reimburse the Trustee for all costs and expenses incurred by the Trustee prior to the First Closing of the Fund in relation to the identification, preparation, and appraisal of proposed projects. No new expenses were incurred in fiscal years ended June 30, 2002 and June 30, 2001.

Administrative Expenses - The Fund reimburses the Trustee for all costs and expenses incurred in the administration of the Fund. These include salaries and benefits, contracted services, marketing, communications, audits and reporting, and overhead. Administrative expenses are recognized when incurred.

Project-Related Expenses - The Fund will reimburse the Trustee for all costs incurred during each project's preparation, including project negotiation and validation costs. The Fund will absorb the expenses that are associated with each project's supervision and verification of ERs. Project expenses are recognized when incurred.

3. RECEIVABLES FROM OTHER TRUST FUNDS

Certain Participants have elected to deposit all or part of their contribution in holding accounts established as separate trust funds. These trust funds are also administered by IBRD. As contributions become due, at the request of the Trustee, funds will be transferred from those holding account trust funds into the Fund. As of June 30, 2002, three holding account trust funds set up by Canada, Finland and Sweden had contribution balances (less contributions already transferred to the Fund) of \$8,817,400, \$8,197,772, and \$4,390,438, respectively. As of June 30, 2001, the amounts in these holding accounts were \$9,270,000, \$8,211,532, and \$3,240,791 for Canada, Finland and Sweden, respectively.

4. CONTINGENT LIABILITY AND PERFORMANCE-LINKED EXPENSES

During each of the first ten years of the Fund's operations, the Trustee may be entitled to receive a performance-linked payment of up to \$100,000, payable annually upon the approval of the Participants at the annual Participants' meeting. For the fiscal years ended June 30, 2002 and June 30, 2001, the Participants had authorized transfers of \$90,000 each year, respectively, from the Fund to the Trustee as performance-linked payments. The amount of \$40,000 was paid to the Trustee in fiscal year ended June 30, 2002. The amount of future payments can not be reasonably estimated.

continued

NOTES TO FINANCIAL STATEMENTS**June 30, 2002**

5. FIRM COMMITMENT

In fiscal year 2001, the Fund entered into an executory contract (i.e., firm commitment) with the Republic of Latvia for the purchase of ERs in the amount of \$2,477,000. Under this contract, the Fund pays for most of the ERs in installments over 6 years and will make a final payment in fiscal year 2013. The total minimum ERs to be delivered is 105,800 metric tones of carbon equivalent with the first delivery planned for fiscal year 2003. The Fund is also contractually entitled to a share of any additional ERs (over the annual minimum required). For the fiscal years ended June 30, 2002 and June 30, 2001, the Fund made an advance payment of \$295,000 and \$300,000, respectively, to the Republic of Latvia under this contract.

In fiscal year 2002, the Fund entered into an executory contract (i.e., firm commitment) with the Hidroelectrica Guardia Vieja S.A., a Chilean company, for the purchase of ERs in the amount of \$3,500,000. Under this contract, the Fund will pay for ERs in annual installments over the life time of the project and each annual payment is in an amount equal to purchase price multiplies metric tones of carbon equivalent of ERs delivered during the calendar year. The total minimum ERs to be delivered is 1,000,000 metric tones of carbon equivalent with the first delivery planned for calendar year 2002. The Fund is also contractually entitled to purchase an additional amount of 750,000 metric tones of carbon equivalent of ERs over and above the total ERs. In fiscal year 2002, the Fund made no payment under this contract.

In fiscal year 2002, the Fund began negotiating a contract with the Republic of Uganda to implement the West Nile Electrification Project. Once the Republic of Uganda selects the executor for the contract, the contract will become a firm commitment to the Fund at which time financial arrangements of the contract will be finalized.

6. VALUATION ALLOWANCE FOR ADVANCE PAYMENT

Due to significant uncertainties surrounding the quantities and value of ERs for which the advance payment of \$595,000 has been made, a 100% allowance has been established as of June 30, 2001. The amount of the allowance will be monitored and revised, as necessary, if conditions related to these uncertainties change.

7. SUBSEQUENT EVENT

At the Third Annual Participants Meeting, held in June 2002 at Zakopane, Poland, it was proposed to increase the size of capital contributions to the Fund up to the maximum size of US\$180 million. Negotiations are currently under way.

In August 2002, a holding account was established for the contributions from the Deutsche Bank and the amount of \$4,413,700 was transferred from the Fund into this holding account.