

ADAPTATION FINANCING MECHANISMS

Policy Brief¹

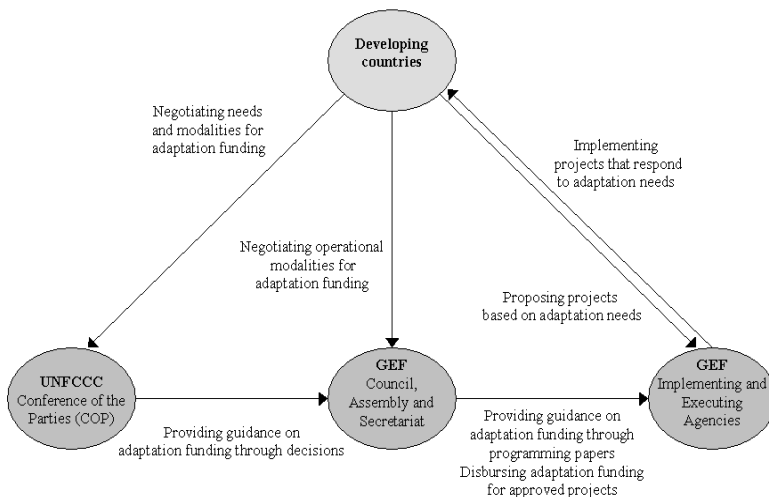
By Richard J.T. Klein and Benito Müller

1. Access to current funds

Governance and eligibility

In Marrakech in 2001, at the seventh session of the Conference of the Parties (COP7) to the United Nations Framework Convention on Climate Change (UNFCCC), three financial instruments were established to support adaptation activities in developing countries: the Least Developed Countries Fund (LDCF), the Special Climate Change Fund (SCCF) and the Adaptation Fund (AF). The LDCF and the SCCF are operated under the UNFCCC and managed by the Global Environment Facility (GEF), similar to the Strategic Priority “Piloting an Operational Approach to Adaptation” (SPA), which the GEF established under its Trust Fund. The AF is not yet operational. It is not managed by the GEF but by a special Adaptation Fund Board (AFB), which is developing specific operational policies and guidelines to be approved this year.

The operational GEF-managed funds provide support to meet the additional costs of adaptation. The remaining costs are to be borne either by the recipient country and/or by bilateral or multilateral donors. The least developed countries that are a Party to the UNFCCC (this excludes Somalia) are eligible for funding from the LDCF, while all developing countries are eligible for funding from the SCCF and the SPA. The eligibility criteria for the AF have not yet been finalised. In Marrakech, Parties decided that in principle all developing countries are eligible, but four years later in Montreal they recognised low-lying and other small island countries, countries with low-lying coastal, arid and semi-arid areas or areas liable to floods, drought and desertification, and developing countries with fragile mountainous ecosystems as being particularly vulnerable to the adverse effects of climate change.



The governance system of the GEF-managed funds is shown in Figure 1. This governance system is aimed at meeting developing countries' needs for adaptation by providing funding for adaptation projects in accordance with guidance developed for the respective financial instruments. Once a financial

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Figure 1. Governance system of financial instruments for adaptation under the UNFCCC and the GEF.

instrument is operational, eligible countries can propose projects based on their adaptation needs through one of the three implementing agencies of the GEF: the United Nations Development Programme (UNDP), the United Nations Environment Programme (UNEP) and the World Bank. Seven additional executing agencies, including the African Development Bank and other regional development banks, contribute to the implementation of GEF projects.

The AF, expected to become operational later this year, is the first financial instrument under the UNFCCC and its Kyoto Protocol that is not based solely on voluntary contributions from donor countries. It receives a 2% share of proceeds from project activities under the Clean Development Mechanism (CDM) and can also receive funds from other sources to support concrete adaptation projects. The AF also has a rather different governance system, resulting in a different process of accessing funds. Parties decided in Poznań last year that short and efficient project development and approval cycles and expedited processing of eligible activities shall be developed. Unlike the GEF-managed financial instruments, eligible Parties have the option of direct access to the AF, that is, without the involvement of a multilateral implementing entity but using a national implementing entity instead. The details of the direct-access modalities are being finalised by the AFB and should become clear later this year.

Delivery to date

The GEF has provided funding to all non-Annex I Parties (developing countries and countries with economies in transition) to support enabling activities, such as vulnerability and adaptation assessments as part of their National Communications. In addition, 48 least developed country Parties have each received USD 200,000 from the LDCF to prepare National Adaptation Programmes of Action (NAPAs), which serve to identify urgent and immediate adaptation needs. Thirty-nine NAPAs have been produced to date.

To address specific adaptation needs, however, only 76 countries (about half of all non-Annex I Parties) have received support from the GEF-managed funds, through a total of sixty adaptation projects. More projects are in the pipeline, but several years can pass between project identification and project implementation. Table 1 presents an overview of the sixty approved projects by size, region, scale and sector. The total amount of grants is USD 182.7 million; which is almost insignificant compared to the estimated annual adaptation needs (see Section 2).

Table 1: Overview of approved adaptation projects in terms of size, region, scale and sector.

| Fund | SPA | LDCF | SCCF | Total |
|-------------------------------------|------|------|------|-------|
| Total projects | 22 | 23 | 15 | 60 |
| Total grants (USD million) | 50.0 | 65.2 | 67.5 | 182.7 |
| Average project grant (USD million) | 2.3 | 2.8 | 4.5 | 3.0 |
| Projects by region | | | | |
| Africa | 6 | 16 | 6 | 28 |
| Asia | 5 | 3 | 3 | 11 |
| Latin America | 4 | – | 4 | 8 |
| Europe | 2 | – | – | 2 |
| SIDS | 3 | 4 | 1 | 8 |
| Projects by scale | | | | |
| Local | 1 | – | – | 1 |
| National | 13 | 23 | 12 | 48 |
| Regional | 7 | – | 2 | 9 |
| Global | 1 | – | 1 | 2 |
| Projects by sector | | | | |
| Agriculture/livestock/forestry | 6 | 9 | 5 | 20 |
| Water resources | 4 | 3 | 4 | 11 |
| Coastal zones | 6 | 5 | 1 | 12 |
| Cross-sectoral | 6 | 4 | 4 | 14 |
| Disaster risk reduction | – | 2 | 1 | 3 |

Non-convention funds

According to UNFCCC Article 11.5, developed country Parties may also provide, and developing country Parties avail themselves of, financial resources related to the implementation of the Convention through bilateral, regional and other multilateral channels. There are now several initiatives specifically dedicated to adaptation, based on official development assistance (ODA). The highest-sourced of these initiatives is

the World Bank's Pilot Programme for Climate Resilience (PPCR), with a total budget of USD 240 million. In addition, new bilateral initiatives focusing on adaptation include the Cool Earth Partnership launched by Japan, which intends to deliver up to USD 1 billion in support of adaptation over a period of five years, the UNDP–Spain Millennium Development Goals Achievement Fund with up to USD 22 million over four years, the German International Climate Initiative with up to USD 200 million over five years, and the European Commission's Global Climate Change Alliance (GCCA) with up to USD 84 million over three years.

The access modalities for the bilateral initiatives have been designed to be consistent with the donor agencies' general policies concerning partner countries. The PPCR has recently selected, based on expert advice, the following eight countries and two regions as the beneficiaries of its adaptation support: Bangladesh, Bolivia, Cambodia, Mozambique, Nepal, Niger, Tajikistan, Zambia, the Caribbean and the South Pacific.

2. Adequacy of current financial instruments

Financial adequacy

The UNFCCC secretariat estimated that by 2030 the annual additional investment and financial flows needed worldwide would amount to USD 60–182 billion, some USD 28–67 billion of which would be needed in developing countries. In spite of the many efforts already made by developing countries, in many cases external support will be required to meet current and future adaptation needs. Article 4.4 of the UNFCCC commits “developed countries to assist the developing country Parties that are particularly vulnerable to the adverse effects of climate change in meeting costs of adaptation to those adverse effects.” This assistance is understood to come in the form of new and additional funding, that is, beyond what developed countries are already providing or planning to provide as ODA.

As of November 2008, USD 262.3 million had been pledged for adaptation under the LDCF and SCCF, of which USD 132.7 million has been allocated (see Table 1). The SPA has allocated all USD 50 million it had available. The amount of money that will be available from the AF depends on how much the CDM is used and on the price of carbon. Estimates vary from USD 80–300 million per year during 2008–2012. Although it is not assumed that the aforementioned investment needs be covered fully from adaptation funds generated under the UNFCCC, it is clear that there is a large mismatch between estimated investment needs for adaptation, and the amount of funding available from current financial instruments.

It is unclear whether or not developed countries share the concern about the mismatch between required and available funds. At COP6-bis in Bonn in 2001, twenty developed countries committed to providing USD 410 million per year towards adaptation funding. The Institute for European Environmental Policy recently analysed the extent to which the European Union and its Member States have met their share of the commitment (which amounts to USD 369 million). It found that “the average annual level of financial support to developing countries collectively provided by the 15 EU Member States ... through specific multilateral climate change related funding channels falls well short of the level ... to which they committed themselves. Whether or not the EU is complying with its political commitment under the Bonn Declaration depends entirely on these Member States' bilateral aid efforts and any additional contributions through other multilateral channels. Unfortunately, the information on such efforts in most of these countries' National Communications under the UNFCCC is insufficient to enable even an informed observer to make a reliable judgment about the volume of aid additional to 2001 levels that is effectively being provided at the present time.”

Technical adequacy

In addition to the financial inadequacy of the current funds, the funds are also widely considered to be technically inadequate, based on views expressed by developing country Parties and various evaluations. For example, at COP12 in Nairobi in 2006, Parties requested the GEF, among other things, to further simplify its procedures and improve the efficiency of the process through which developing country Parties receive funding, and to explore options to address concerns of developing country Parties on requirements for leveraging additional funds for projects.

A series of independent studies that analysed the GEF-managed funds in terms of their efficiency, fairness and responsiveness to developing countries' needs have shown several shortcomings. For example, in 2006

the GEF Evaluation Office concluded that the GEF activity cycle is not efficient, that the situation has grown worse over time and that GEF modalities have not made full use of trends towards new forms of collaboration that serve to promote efficiency. According to the GEF Evaluation Office, the cycle management of the GEF lags behind international good practice in terms of efficiency.

In view of the fact that the current global funds for adaptation are not only technically but also financially inadequate, the question arises as to whether or not alternative arrangements for adaptation funding, such as bilateral and multilateral ODA could address the concerns of developing countries and better meet their needs. On the one hand the amount of money provided by ODA is much larger than what is available under the UNFCCC; on the other hand adaptation would have to compete with other, more immediate development priorities. In addition, ODA has its own set of eligibility and disbursement criteria, on which developing countries have limited influence. Moreover, support for adaptation is a commitment under the UNFCCC, whereas ODA is voluntary. Financially and technically adequate global funds for adaptation are crucial if international climate policy after 2012 is to be a truly global endeavour, whereby global funds serve as a catalyst for providing additional resources from bilateral and multilateral sources.

3. The next generation of funding instruments

The lessons learned from the performance of existing instruments climate change funding have led to a number of key developing country demands, namely that financing needs to be (i) new and additional to ODA, (ii) predictable and timely, (iii) adequate in size, (iv) appropriate in form, and (v) equitable.

These demands are by no means new. What is new is that because of the ongoing international effort to bring the current negotiations on the future UN climate change regime to a successful conclusion in December in Copenhagen, there is a unique chance to bring about a systemic change in international climate change finance which finally heeds these demands, as part of an overall 'Copenhagen package.'

One of the most promising starting points in this respect is the August 2008 submission by the G77+China on making the existing financial mechanism of the UNFCCC operational so as to make it fit for the purpose of handling adequate amounts of financing, that is between USD 50 and 150 billion annually. A recent detailed study of how this could be achieved in a Reformed Financial Mechanism (RFM) has shown that, in order to satisfy the above-mentioned demands, funding has to be significantly consolidated in a single international instrument, and decision-making devolved to designated entities in the eligible recipient countries.

Consolidation of payments – making sure that unlike the current fragmented ODA system, payments by developed countries towards complying with their financial commitments are largely centrally managed – is crucial to assure that all eligible countries get a fair share of the funding, and that there is an agreed balance between the different funding windows (adaptation, mitigation, technology transfer, etc.).

Devolution of funding decisions – delegating the funding decisions on specific activities to recipient country entities – is not only essential for the efficiency of the whole instrument, it also provides for genuine 'direct access' to, and 'ownership' of the funding instrument by developing countries.

The current negotiations on the financial architecture for climate change restitution to developing countries are at a cross-roads. In the absence of a consensus on an acceptable architecture, it is unlikely that developed countries will be adopting financial commitments that are adequate to deal with the climate change burden in developing countries. And without such commitments, developing countries will not be able to achieve the desired agreed outcome in Copenhagen.

It is therefore of paramount importance that Ministries of Finance, particularly from the most vulnerable countries, not only take an interest but a lead in these negotiations to safeguard their countries' vital financial interests in this sphere. On 8 April 2009, Algeria, on behalf of the Africa Group, made a submission proposing draft negotiating language for the upcoming UNFCCC negotiations that includes key elements on financing in support of the G77+China position. Whether or not this position will prevail depends to a large extent on how united developing countries are behind the submission. The negotiations that led to the Adaptation Fund are proof that if the developing world is united, it can achieve its aims in these negotiations.