

## **CLIMATE FINANCE: PROPOSALS ON GOVERNANCE**

### **A non-paper by the Governments of the UK, Mexico, Norway and Australia**

Under the Bali Action Plan, countries agreed that developing countries will have “improved access to adequate, predictable and sustainable financial resources and financial and technical support, and the provision of new and additional resources, including official and concessional funding.” Finance is needed to support adaptation, mitigation (including forestry), technology cooperation and capacity building in developing countries. Agreement on climate change finance will be integral to an ambitious global deal in Copenhagen.

A critical question for Copenhagen will clearly be on the scale of need. However at the same time it will be important to establish how climate finance is going to be provided and governed. This non-paper seeks to address this issue. It sets out some core principles; proposes some overall architecture to govern climate finance; proposes a new Climate or Green Fund or Funds; and emphasizes the importance of leveraging finance from the private sector, particularly through an expansion of carbon markets.

#### **Some core principles**

- Financing will need to be scaled up significantly and urgently, starting fast and rising over time.
- Public finance should be predictable and of sufficient scale and scope to meet future needs.
- Private finance and carbon markets should play a complementary role, depending on national and international policy frameworks. Finance should be deployed to provide the right economic incentives for all countries to fight climate change.
- Around 50% of international public finance should be provided for adaptation in developing countries, with priority for the poorest, least developed and most vulnerable countries, including small island developing states.
- Climate change financing for both adaptation and mitigation is critical to the achievement of development goals and climate change needs to be mainstreamed within development practice and existing institutions. Some have stressed that climate finance should be clearly new and additional to finance already committed for MDG achievement. Some have suggested it could be ring-fenced and accounted for through separate structures. Others have pointed to the clear overlap between climate and development objectives.
- The system of international finance to address climate change needs to be better coordinated, predictable and of sufficient scale and scope to meet future financing delivery needs. An effective institutional framework will be essential in building confidence and delivering the necessary scale of finance in a durable way.

- Delivery of funding should be in line with developing countries' national sustainable (low carbon and climate resilient) development plans and priorities and country-led. Funding should be delivered in a programmatic way.
- There should be direct access to international finance where fiduciary standards allow and country level trust funds should be considered, among other alternatives, where direct access is not possible. Given the multiple channels of finance and the complexity of addressing climate change, it will be important to effectively coordinate delivery of finance to, and reporting against, country-led national plans. It will be important also to streamline reporting and to provide technical assistance and capacity building for developing countries, including, where requested, to support developing countries to develop and implement proposals.
- Given the need to have immediate effect, fast start funding should be directed through existing bilateral and multilateral channels, rather than lose time in establishing a new fund for these initial years. Activities that could be supported by fast-start include: drafting or finalizing national low carbon growth and adaptation plans; improving in-country capacity to design and implement national climate change actions; supporting urgent and priority adaptation needs; supporting mitigation activities, including forestry. Funding could also be used to help prepare developing countries to take full advantage of post-2012 financing arrangements.
- The quantum of public financial resources to support climate change action in developing countries has been increasing rapidly over the last few years. The growth in funding from fast start commitments would be expected to continue beyond 2012.

### **Overall architecture**

- All finance provided to tackle climate change, whether through bilateral or different multilateral channels, needs to be included and counted within the overall framework.
- It will be important to ensure co-ordination and co-operation between financing mechanisms including multilateral, regional and bilateral finance and any new innovative sources. All these, if delivered in line with the low-carbon and climate-resilient priorities of developing countries, should be recognized transparently in the system of climate finance, for example through reporting in National Communications, and subjected to measurement, reporting and verification. International verification should be applicable to activities funded through international channels. In addition, a process of international peer review (or equivalent) could be used to facilitate the enhancement of national communications.
- Countries have suggested different approaches to determine overall contributions to international public finance. One option proposed is that all countries would contribute except the least developed, and developing countries would be net beneficiaries. To enhance the certainty and predictability of climate finance the scale of countries' contributions could be determined in accordance with an agreed scale of assessed or indicative contributions and other comparable methods. The Government of Mexico has proposed to use income (GDP), emissions, population and carbon intensity as the basis to determine such a scale of contributions. Other criteria could also be explored. These approaches could be applied

broadly, limited to a predetermined set of countries or evolve over time. Some countries have proposed specific numbers, including absolute numbers for contributions and ranges of numbers for shares of GDP. Whilst recognizing the responsibility of developed countries, future climate finance arrangements should be responsive to future changes in the global economy.

- The certainty and predictability of climate finance could also be increased by identifying particular sources through which some of the required funds could be raised. Different methods could be used for raising funds for different purposes. The Norwegian proposal aims to draw finance from national and international auctions of emissions permits, and could be designed to secure predictability and sustainability. Countries that undertake commitments on emissions limitation and reductions that can be quantified could participate, and this counted towards their contributions.
- A number of innovative sources have also been proposed to provide climate finance, including use of the revenues from measures to reduce emissions from international aviation and shipping.

### **A new fund or funds**

- A number of parties, including the G77 / China, Mexico and the US, have proposed the establishment of a new Climate or Green Fund. To ensure a clear allocation of finance to mitigation and adaptation purposes, such a fund could have separate windows for adaptation and, mitigation (including forestry, technology cooperation and capacity building). Others have proposed separate funds for adaptation, forestry and technology, recognising the different needs in these areas. In either case, such a fund or funds would support country-led national plans comprising programmes, projects and policies.
- On mitigation the allocation of resources from a new fund would be based on the recognition that direct economic incentives for developing countries are crucial to encourage developing countries to scale up their national efforts. In addition to support for capacity building and technology co-operation, funding for mitigation actions could primarily be delivered through results-based mechanisms, for fully additional verified emission reductions relative to predetermined agreed reference levels. Such incentives could allow further actions from developing countries relating to the emissions either avoided or captured by specific projects. Developing countries would also be expected to mobilize domestic resources to help finance to their own effort, subject to their respective capabilities.
- On adaptation the poorest, least developed and most vulnerable countries, including small island developing states, should take priority.
- The creation of such a fund or funds should occur at the same time as better use is made of existing mechanisms, including the Global Environment Facility, which should be reformed where necessary to be more efficient and effective.
- There is now emerging consensus on the governance of a Climate or Green Fund, as proposed by Mexico:

- It should have a high-level board under the policy guidance of, and accountable to, the Conference of the Parties, with equal representation of developed and developing countries, and an equitable, efficient and transparent governance structure.
- To ensure rapid start-up and efficiency, the administration of such a Green Fund could be entrusted to an existing international financial institution. It could deliver funding through institutions as identified by the developing country, in partnership with other domestic and international public and private financial institutions. The green fund could offer a range of financial instruments, including grants and concessional finance, tailored to financing needs.
- Any new fund should abide by principles of balanced representation, streamlined operational procedures, low administrative costs, transparency and efficiency; should demonstrate delivery of results and should deliver expedited and more predictable access to finance, while retaining attention to fiduciary standards and safeguards.

### **Private and carbon market finance**

- Public finance can leverage private flows and there are opportunities for the private sector to invest in all developing countries, including the least developed. Effective use of public finance can leverage substantial private sector funding, creating a multiplier effect on any public funding provided. All actors, including the international financial institutions, should explore ways to bring extra private finance into developing countries.
- The funding available to developing countries through carbon markets, whilst embryonic, shows signs of potential growth. The level of carbon market finance will depend on several factors, particularly the level of reductions in developed country emissions. Reformed, broadened and strengthened carbon markets have the potential to deliver substantial new private investment in developing countries, complementary to public finance, and consistent with sustainable financing and environmental integrity. The Copenhagen agreement should agree to reform the existing carbon market and agree to the development of new, larger scale mechanisms as soon as possible. This would improve efficiency and bring significant benefits to developing and developed countries.