SPECIAL SESSION ON CLIMATE CHANGE

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Financial Resources and Investment for Climate Change

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I. Overall Context

1. Estimates of adaptation cost for all developing countries are very large and could globally amount to as much as US$86 billion per year in 2015 according to the UNDP's 2007 estimate[1]. In addition, financing required for Africa's low carbon development, for example to increase access to low-carbon energy and to safeguard its forests are expected to be very large. A new climate change deal should provide new international finance to meet this scale of challenge.

2. Compared to these large requirements, total existing commitments to funds that have been set up with voluntary contributions under the UNFCCC to assist developing countries amount to just about US$ 300 million -- of which only half have been disbursed. In addition to the above, modest resources are available from one of an array of financing instruments that are designed to achieve multiple climate-related objectives. With the exception of the Adaptation Fund[2], which was established under the Kyoto Protocol with funding derived from a two percent levy on the proceeds from Clean Development Mechanism (CDM) projects, all the other financing initiatives are voluntary.

3. The large shortfall of funding for adaptation in developing countries has made financing an important issue in the context of the climate negotiations. The need for new sources of funding was made explicit in the Bali Action Plan (BAP). Thus, besides underlining the need to provide developing countries with adequate, new and additional financial resources from official and concessional sources, the BAP also emphasized 'innovative means of funding' and the 'mobilization of public- and private-sector funding and investment, including facilitation of carbon-friendly investment choices'.

4. Besides the large funding shortfall, there are equally significant challenges concerning the structure, governance and allocation of the funds. Most common among concerns by developing countries are the disproportionally larger role of developed countries in decisions on allocations and disbursements, complex and lengthy procedures that render access to funding difficult, and in certain cases, the lack of appropriateness of some of these instruments to low-income countries where the economies are predominantly based on agriculture, forest resources and natural resources. This has led to developing countries expressing a strong preference for having all financing institutional arrangements under the control of the UNFCCC's Conference of Parties (COP).

II. Existing financing mechanisms

5. There has been a proliferation of new climate-related funding initiatives covering both adaptation and mitigation that can be regrouped either by the sources of funding -- initiatives funded by international public contributions, which cover the majority of existing mechanisms and those that rely on market-based carbon finance, including the Adaptation Fund or by their governance structure – funds coordinated under the authority of the UNFCCC/Kyoto protocol (informally referred to as Convention funds) and those that are either managed directly by the funding bilateral agencies or administered by the World Bank and other multilateral agencies, also known as non-Convention funding initiatives.

6. Under the aegis of the UNFCCC, three funds have been established to address climate-related needs and are managed by the Global Environment Facility, as the primary facilitator of the financing

[1] There is a wide range of global estimates for incremental adaptation costs, prompting for further research on the topic.
[2] The Adaptation Fund is expected to become operational later in 2009.

mechanism under the Convention. The Special Climate Change Fund was created to fund projects in capacity building, adaptation, technology transfer and climate change mitigation. The Least Developed Countries Fund was designed to help the Least Developed Countries cover the costs of preparing and implementing their National Adaptation Programmes of Action (NAPAs). Resources generated under these funds are far from meeting African countries' needs for climate adaptation. The Adaptation Fund, the most recent among the conventions Funds, was established to finance adaptation projects and programmes in developing countries that are Parties to the Kyoto Protocol. Funding is derived primarily from the proceeds of a 2% levy on transactions under the CDM. Developing country Parties generally support the governance structure of the Adaptation Fund, since it allows for stronger representation of developing countries. Created in 2001, the Adaptation Fund is only expected to become operational towards the end of 2009.

7. The *Clean Development Mechanism (CDM)* was established under the Kyoto Protocol to assist developing countries Parties in promoting sustainable development and to facilitate developed (Annex I) Parties in complying with their emission reduction commitments. In 2007, proceeds from the sale of emission credits from CDM projects amounted to US$ 7.4 billion, or triple the value in 2005. The CDM thus provides developing countries with a significant source of carbon finance to help promote sustainable development. But although the CDM has proven successful in generating emission reduction projects in many developing countries, only 30 out of the registered[3] 1600 projects worldwide were located in Africa, with 15 of them in South Africa.[4] Only South Africa has issued Certified Emission Reduction (CER) receipts, or in other words, now has credits available to sell. A number of factors explain Africa's low share of CDM transactions. They include barriers related to CDM procedures and modalities; coverage of CDM; financial, institutional and capacity barriers in host countries; and, the fact that greenhouse gas emissions in Africa, with possibly the exception of South Africa and Nigeria, are low.

8. Stricter technical and procedural requirements for CDM projects have diverted many small project developers to the *voluntary carbon market* whose value of transactions grew by 240% in 2007 to US$331 million. The voluntary market trade is driven mainly by heavy emitting companies wanting to prepare for expected mandatory emissions trading rules in their jurisdiction, firms offsetting their emissions as part of a green marketing strategy and environmentally-motivated individuals. Controversy over the integrity of carbon offsets being generated in the unregulated voluntary market has given rise to a range of independent third-party administered standards for the validation of offset projects and the verification of their carbon and wider benefits. Paramount among these is ensuring real and permanent carbon sequestration, promoting wider environmental sustainability and delivering positive outcomes for local communities. Access to the voluntary carbon market could provide a good learning path towards the more regulated CDM and future similar market-based mechanisms for REDD

9. While the amount of proceeds from the sale of emission credits from CDM projects has so far been insignificant for Africa, recent information shows an encouraging upward trend in the number of new CDM projects. As of April 2009, 23 African countries have submitted a total of 102 CDM projects[5] in the CDM project pipeline. It is therefore essential that African governments both capitalise on existing carbon market opportunities, and develop a clear position for post-2012 negotiations, in order to increase the flow of resources needed to meet the challenges of climate adaptation and sustainable development.

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[3] The approval of CDM projects goes through a rigorous process of review; only developers of registered projects can issue Certified Emission Reduction receipts (CERs).

[4] The other African countries with registered CDM projects are Egypt and Morocco (4 projects), Nigeria and Tunisia (2 each), and Kenya, Tanzania and Uganda (1 each). Source: IGES CDM Project Database (May 2009).

[5] UNEP Risoe, CDM/JI Pipeline Analysis and Database (May 2009).

More importantly, the sustainable development component of CDM projects provides an opportunity for African countries to develop the expertise and capacity to prepare and implement projects aiming to enhance sustainable development and to contribute the global mitigation efforts. Countries should therefore strongly advocate for due recognition to be given to the sustainable development objective of the CDM.

10. Funding initiatives that are managed outside of the UNFCCC's coordination are much larger in volume terms and are designed to address both adaptation and mitigation challenges. These are summarized in Table 1.

Table 1 - Summary of existing climate change funding initiatives outside of UNFCCC (non-Convention Funds)

FUND	PLEDGED AMOUNT/ ADMINISTRATOR	SHORT DESCRIPTION
Climate Investment Funds (CIF) that encompasses the Strategic Climate Fund (SCF) and the Clean Technology Fund (CTF).	$6.3 billion, World Bank	Piloting new approaches or scaling up activities in developing : ♦ The SFC: on increasing climate resiliency; reducing emissions from deforestation and forest degradation (under consideration); and iii) scaling up renewable energy. ♦ The CTF on demonstrating and transferring low-carbon technologies.
Forest Carbon Partnership Facility (FCPF)	$165 million, World Bank	Focusing on mitigation through REDD.
Carbon Partnership Facility (CPF).	$470 million, World Bank	Supporting developing countries towards lower carbon development paths. Components of the Investment Framework for Clean Energy and Development (CEIF).
Congo Basin Forest Fund (CBFF)	$200 million, AfDB	Promoting biodiversity conservation, natural resource management and mitigation through REDD.
Strategic Priority on Adaptation (SPA)	$50 million, GEF	A 3-year pilot programme for adaptation planning.
UN-REDD Program	$35 million, UNDP	Focusing on mitigation through REDD.
MDG Achievement Fund – Environment and Climate Change window (MDG)	$90 million , UNDP	Focusing on adaptation and general mitigation.
EU-Global Climate Change Alliance (GCCA)	$300 million (€220m), EU	Focusing on adaptation, general mitigation and REDD.
Cool Earth Initiative (Japan)	$10 billion, Japan	Focusing on adaptation and mitigation activities.
Environmental Transformation Fund (UK)	$1.2 billion (£800m), UK	Focusing on adaptation and mitigation with some components administered by World Bank and AfDB (Congo Basin Forest Fund).
International Climate Initiative (Germany)	$170 million (€120 m), Germany	Focusing on adaptation and general mitigation.
International Forest Carbon Initiative (Australia)	$180 million (AUD 200m), Australia	Focusing on mitigation through REDD.

Source: Adapted from Brief (author unknown) produced for Financing for Development Conference on Climate Change, Kigali, 21-22 May 2009.

III. Considerations on a future financial framework that reflect Africa's priorities

11. The Bali Action Plan underlines the need for financial support for developing country Parties and, more specifically, emphasizes that future climate funding be ' adequate', 'predictable', 'sustainable' and

'new and additional'. The BAP also recognized that official and concessional funding will not be sufficient and therefore the need to promote 'innovative means of funding' and further efforts to mobilizing private-sector funding and investment, including carbon finance.

12. Based on these key principles, the specific concerns for Africa as expressed in the submission by Algeria to the UNFCCC on behalf of the African Group focused on the following issues:

(i) Level of overall financial resources: reflecting the Bali key principles of 'adequate', 'sustainable' and 'new and additional' and predictable together with a preference for grants over loans;

(ii) Equitable sharing of the burden highlighting the need for African countries to pursue their sustainable development goals and a focus on funding for adaptation; and

(iii) Governance and access: funding to be accountable to the COP, monitorable, reportable and verifiable – the MRV concept introduced in Bali and discussed earlier under Enhanced Mitigation -- direct access with minimal management by intermediaries and avoiding fragmentation.

13. *More focus on capturing opportunities to contribute to the global mitigation effort.* Various mechanisms for financing climate change are being proposed for negotiations:[6] some of these have a large potential to benefit African economies and should be actively supported. While adaptation is a high priority for Africa, opportunities to contribute to the global mitigation effort through funding for Reduced Emissions from Deforestation and Forest Degradation (REDD), which is part of the African Group proposal, could be given more emphasis. Also, given Africa's very low access to modern energy – currently, less than 25 percent of African households have access to electricity - pursuing a low-emissions growth path relying on the large potential of renewable energy– only 7 percent of Africa's hydropower potential is exploited – would strengthen Africa's claim for its fair share of existing and future climate resources in exchange for its active participation in the global mitigation effort, as well as having a positive growth and employment impact.

14. *Governance of funding mechanisms*. As noted above, significantly larger resources are currently available outside the UNFCCC framework than within it thus making it very challenging, at least in the short-term to bring all funding arrangements under the control of the UNFCCC as recommended by Africa and several other developing country Parties.. In the interim, efforts should be directed at aligning the governance systems of non-Convention funds with those that are under the Convention. Particular attention should be paid to equity issues.

IV. Description of the main new financing proposals

15. New international finance is required in large enough volumes and delivered effectively to meet the scale of climate change challenges in Africa. There are various proposals being considered in the climate negotiations on sources of finance:

- *Auctions of emissions allowances:* Each of the Annex I countries receive a number of greenhouse gas units they can release and/or trade (*Assigned Amount Units,* AAUs). The underlying funding principle of this scheme is to auction a certain share of these AAUs to generate revenue rather than giving them out for free. The Norwegian proposal is the broadest with the auction occurring upstream

[6] Details of proposals by Parties are available in the negotiating text for the June COP meeting and is accessible at: http://unfccc.int/resource/docs/2009/awglca6/eng/08.pdf

before the AAUs are allocated to national registries. Germany has already implemented such a scheme at the national level while the US is also considering such a scheme.

- *Carbon market-based levies:* adaptation funding can be generated by applying a levy to the Kyoto Protocol's tradable units generated from the CDM, Joint Implementation projects (CDM-like but where projects are domiciled in Annex I Parties) or other emissions trading. The 2 percent levy on CDM proceeds to raise funds for the Adaptation Fund is an example of a carbon market-based levy.

- *Charges, levies or taxes on emissions, or on specific activities (such as air travel),* in which funds are raised by charging individuals and companies, based on their responsibility for climate change and/or their capability to pay.

- *Assessed contributions of developed country Parties taking into account, for instance GDP, current emission levels or historical contribution to GHG concentration in the atmosphere,* in the range of 0.5 to 1% of GDP (G77 plus China's proposal).

- *Other innovative ways of financing adaptation, such as the issuing of bonds based on the creditworthiness of the bond emitter as guarantees.* The European Commission's proposed Global Climate Financing Mechanism is one proposal in this category.

V. Recommendations to Parties

African countries

- Provide an enabling environment for staying informed on current and proposed procedures and requirements (e.g. well-prepared funding projects/programmes) for access to funding;
- Support the development of plans and initiatives that would effectively and efficiently make use of new international climate change finance.
- Strengthen the institutional and technical capacities to better engage in the CDM process including improving the domestic investment climate.

Developed country Partners

- Provide significant additional resources in line with relevant principles of the BAP, to help finance Africa's adaptation and low carbon development climate challenges.
- Ensure that future climate financing provides new, additional, predictable and sustainable resources including through the new and innovative climate change funding sources.
- Promote an enabling environment to facilitate Africa's access to information and procedures for accessing funding and make effort to keep transaction costs of accessing funds at a minimum.
- Mobilize financing for low carbon development in Africa, for example for Reduced Emissions from Deforestation and Degradation (REDD), agriculture and greater access to clean energy.
- Make the carbon market, including a reformed Clean Development Mechanism, more relevant and fair to Africa.
- Support a fair allocation of international adaptation funding so that the most vulnerable and needy African countries benefit, for example on the basis of climate change impact, national income and ability to cope.

Annex 1

Table 2: Summary of new climate change funding initiatives

FUND	SOURCE OF FUNDS	CLIMATE FUNDS FOR DEVELOPING COUNTRIES/YEAR	OBSERVATION
AUCTIONS OF EMISSIONS ALLOWANCES			
Norway's auctioning of allowances	Part of Annex I Party's allowances withheld, auctioned by international body	US$20-30 billion (bn) annually	Auctioning of allowances appears to be relatively well accepted. The EU has aligned its position with that of Norway.
Germany's International Climate Initiative	9% of emissions permits auctioned domestically	US$80 million (m) for adaptation/forestry; US$80 million for sustainable energy	
US Adaptation & National Security Fund	Portion of revenue from allowance auctions	N/A	
CARBON MARKET-BASED LEVIES			
Extending the levy to Joint Implementation and/or International Emission Trading	Extending the 2% levy on CDM to JI/IET	2008–2012: US$5.5–8.5bn 2013–2020: US$3.5–7.0bn	Parties were unable in Poznan to reach consensus. Low probability for resubmission.
CHARGES, LEVIES OR TAXES ON EMISSIONS OR SPECIFIC ACTIVITIES			
International Air Passenger Adaptation Levy (IAPAL)	US$6 per ticket (Economy class), US$62 per ticket (business/first class)	US$8-10 bn annually, for first five years of operation.	
International Maritime Emissions Reduction Scheme (IMERS)	Levy using the global average price of carbon.	US$9 bn annually if applied world wide.	IMERS has been reviewed and broadly endorsed by various organizations, including UNFCCC, WWF, OXFAM, and UNDP.
Swiss Global Carbon Adaptation Tax	Tax (US$2/t CO2 e) on emissions from fuels. A free emission level of 1.5 tons of CO_2 per capita is applied to all countries	US$48.5 bn annually	There appears resistance to a carbon tax, especially if the tax has to be collected nationally for external use.
Tuvalu's Burden Sharing Mechanism (Adaptation Blueprint)	01% levy on int'l airfares, maritime transport freight charges operated by Annex I 001% levy on int'l airfares, maritime transport freight charges operated by	US$40 m from Annex II; US$30 m from non-Annex I	Additional funding for the UNFCCC Least Developed Country Fund and the Special Climate Change Fund.

	non-Annex I (LDCs / SIDS exempt)		
Mexico's World Climate Change Fund	Mexico suggests the creation of a new fund (US$10 billion per annum) and recommends a 2% adaptation levy	US$200 m per annum.	
ASSESSED CONTRIBUTIONS OF DEVELOPED COUNTRY PARTIES			
G77 plus China	0.5% to 1% of Annex I countries' GNP	US$201-402 bn annually	
OTHER INNOVATIVE FINANCING INITIATIVES			
EC Global Climate Financing Mechanism			