CLIMATEFOCUS

Green Climate Fund and the Paris Agreement

Climate Focus Client Brief on the Paris Agreement V
February 2016

TOUS ENSEMBLE POUR LE CLIMAT
cop21.gouv.fr #COP21

- The Paris Agreement and the supporting Decision include provisions on finance that both directly and indirectly relate to the role and operation of the Green Climate Fund (GCF).
- The Agreement emphasizes the GCF's role as a key provider of predictable financial resources in the post-2020 framework.
- The introduction of a floor of USD 100 billion annually on the level of climate finance going forward post-2025 acknowledges that climate finance needs to be further scaled-up.
- A roadmap to achieve this funding level is expected to introduce clarity on Parties' pledges, supporting the GCF in making future funding decisions.
- Development of modalities for the accounting of financial resources and the requirement to provide biannual reporting will introduce further transparency to the funding and operating of the GCF.
- Developed countries are to continue taking a leading role in mobilizing climate finance, which is already reflected in the contributions made into the GCF to date.
- Funding is to be balanced between mitigation and adaptation initiatives, acknowledging the importance of sustainable development co-benefits and prioritizing action in Least-developed Countries (LDCs) and Small Island Developing States (SIDS).

Introduction

The 21st session of the Conference of the Parties to the UNFCCC (COP 21) held in Paris has delivered a framework for post-2020 climate action. The Paris Agreement commits Parties to aim to hold global temperatures well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C. Regularly updated nationally determined contributions (NDCs) represent the action plans that are to lead to a peak in global greenhouse gas emissions 'as soon as possible'. Further provisions on voluntary and transparent approaches to cooperation, including internationally transferred mitigation outcomes and non-market approaches targeting both mitigation and adaptation measures in a sustainable manner, lay the groundwork for future mechanisms that may evolve under the Agreement.

One common denominator underlying the realization of all these goals – availability of finance – deservedly features in a standalone section in the Paris Agreement (Art. 9). This Climate Focus Client Brief presents our assessment of what the Paris Agreement means for climate finance, and in particular how it relates to the role and modalities of the GCF.

The Green Climate Fund

The GCF has been established with the objective to mobilize climate finance to support scaled-up mitigation and adaptation action in developing countries. It was first mentioned in the Copenhagen Accord in 2009 and was formally established one year later during the COP 16 held in Cancun, Mexico. In 2011 the GCF adopted its governing instrument, in which it recognized its objective to '*promote the paradigm shift towards low-emission and climate-resilient development pathways by providing support to developing countries to limit or reduce their greenhouse gas emissions and to adapt to the impacts of climate change*'.

Adopted as an operating entity of the Financial Mechanism of the UNFCCC and confirmed in this function for the Paris Agreement, the fund has the ambition to channel a significant portion of future climate finance from both the public and private sector.

With USD 10.2 billion of climate finance pledged to the GCF and USD 5.9 billion confirmed as of January 2016, the GCF and its funders still have a long way to go to get close to the climate finance target of USD 100 billion annually. The fund has however come a long way since its conceptualization in 2009 – it has found its home in South Korea, defined its scope of activities and its mission, developed proposal templates, investment criteria and approval procedures, initiated readiness programs and accredited 20 international and domestic entities through which disbursements can be channeled. Just before the COP in Paris, the GCF approved funding for the first set of eight projects for a total of USD 168 million. The fund is ready to scale-up its funding allocations and intends to award up to USD 2.5 billion in 2016.[1]

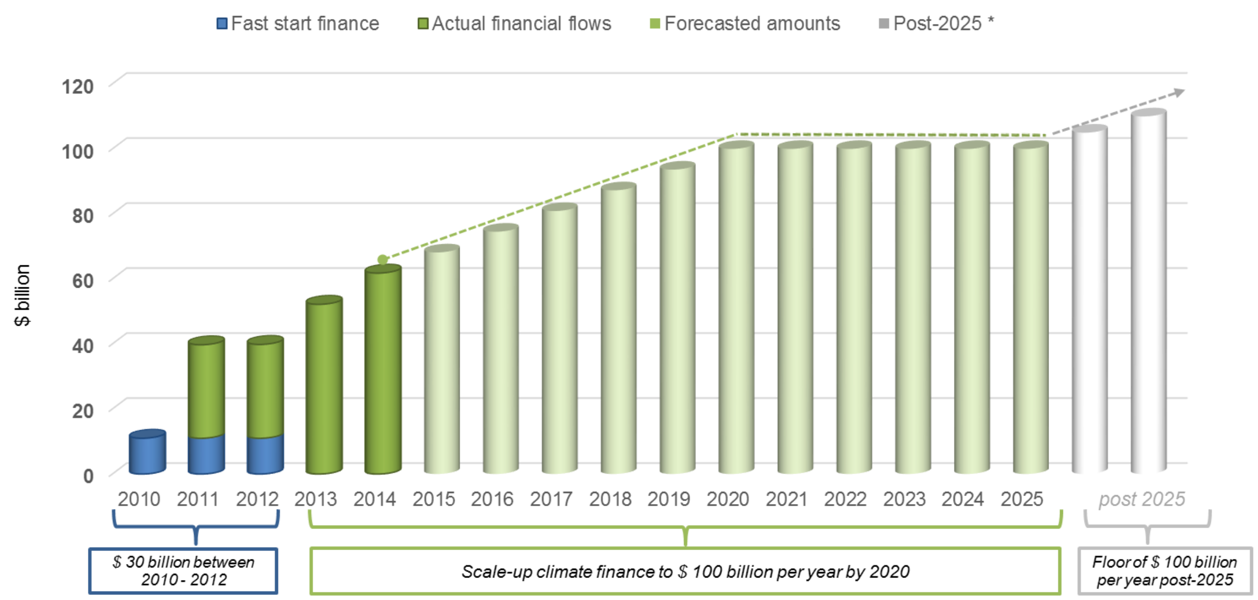
The outcome of Paris is relevant to the modus operandi of the GCF as it reiterates the key role the fund is to have in a post-2020 framework, highlighting the fund as a key provider of predictable financial resources. The Paris Agreement and the accompanying Decision provide additional provisions on finance that are relevant to the GCF, including on funding ambitions, its contributors, earmarking of funds and its subsequent accounting and reporting.

Funding ambitions

The Paris Agreement does not explicitly refer to the GCF and the amount of funding that it is to mobilize. The text recognizes however that '*the Financial Mechanism of the Convention, including its operating entities, shall serve as the financial mechanism of this Agreement' (Art. 9.8)*. The Financial Mechanism was established under the Convention (Art. 11) to formalize and streamline efforts to provide concessional financial resources to developing country Parties. Designated bodies – the operating entities – are entrusted to realize the goals of the Mechanism. The GCF, together with the GEF, are the two operating entities of the Financial Mechanism of the Convention and the Paris Agreement and as such represent the main channels through which future sources of international climate finance are expected to flow in the years to come.

The Paris Decision, serving as guidance for the implementation of the Paris Agreement and pre-2020 action, '*strongly urges developed country Parties to scale up their level of financial support, with a concrete roadmap to achieve the goal of jointly providing USD 100 billion annually by 2020 for mitigation and adaptation'* (para 115*)*. The Decision furthermore mentions that prior to 2025 the COP shall set a new '*collective quantified goal from a floor of USD 100 billion per year'* (para 54). The reason both quantitative targets are missing from the actual Agreement is a pragmatic one – in doing so the COP has enabled the US President to adopt the Agreement as 'sole-executive agreement' under US law, without the requirement for the US Senate to approve.

Figure 1: Overview of current and foreseen climate finance flows



* Note: A common framework for tracking climate finance flows is currently missing. The presented data on actual flows was sourced from the UNFCCC *"Biennial Assessment and Overview of Climate Finance Flows Report"* with respect to 2010-2012 and the OECD report on *"Climate Finance in 2013-2014 and the USD 100 billion goal"* for the period of 2013-2014. Future forecasts are based on pledges confirmed in the Paris Agreement.

[1] GCF. http://www.greenclimate.fund/-/-we-want-to-take-the-momentum-from-paris-and-ramp-it-up-. February 2016

From the perspective of the GCF, while the annual target of USD 100 billion is in itself not new, the introduction of a floor on the level of climate finance going forward post-2025 presents an acknowledgment that climate finance needs to be further scaled-up in order for the Agreement's objectives to be realized (see Figure 1). The GCF is explicitly recognized in the Decision as a key multilateral funding source that is to support the flow of '*adequate and predictable financial resources'* (para 55). The urge to develop a roadmap for reaching the stated financing target by 2020 and beyond is also a significant development given the current ambiguity revolving around the magnitude and origin of future finance flows. More certainly and clarity on Parties' future funding pledges and its underlying terms and conditions will support the GCF in making funding decisions going forward.

Sources of funding

Article 9 of the Agreement stresses that '*developed country Parties should continue to take the lead in mobilizing climate finance from a wide variety of sources, instruments and channels' (Art. 9.3)*. This follows the Convention's principle of common but differentiated responsibilities and respective capabilities, as also reiterated in the Agreement (Art. 2.2). Which country should take on what responsibility, and how this relates to the annual USD 100 billion target by 2020 is left open and will be based on self-assessment and determination.

The GCF strives to mobilize finance from both developed and developing countries, with developed countries taking a lead in contributing resources. The fund's Initial Resource Mobilization (IRM) period started in June 2014 and lasts until 2018, during which new pledges will be accepted on an ongoing basis. From the USD 10.2 billion currently pledged to the fund, USD 9.3 billion comes from developed country Parties.[2]

At the same time, reflecting the demise of the formal distinction between Annex-1 and non-Annex-1 countries pursuant to the Annexes of the UNFCCC, the Agreement also encourages developing countries to provide financial support on a '*voluntary basis'* (Art. 9.2). This reference was included as a result of developed nations stressing the point that certain developing countries are also in the position to contribute international climate funding. The GCF has already succeeded in mobilizing pledges from a number of developing countries – from the total of 38 state governments that have already announced intended contributions to the fund as of January 2016, eight represent developing countries. Together, these pledges amount to almost ten percent of total funding made available to the GCF.

The Agreement further notes the '*significant role of public funds'* (Art. 9.3), which are to be mobilized beyond previous efforts. So far all pledges received by the GCF represent public funds. However, the fund is open to non-public allocations and plans to include innovative ways to accept contributions from private entities and individuals. The fund is in the process of setting up the Private Sector Facility with the objective to mobilize private capital flows by tapping into international businesses and capital markets. As such, the GCF will also be in the position to directly support the Agreement's broad ambition to '*make finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development'* (Art. 2.1c).

Finally, the Decision also encourages non-Party stakeholders to scale up their climate actions '*including those of civil society, the private sector, financial institutions, cities and other subnational authorities'* (para 134*)*. Here too the GCF has started booking progress, with the municipalities of Brussels and Paris pledging around USD 1 million each. All in all, this means continuation of business as usual for the GCF.

Allocation of funding

The Agreement has strengthened the case for equal allocation of future climate funding between mitigation and adaptation action. Financial resources are encouraged to be '*a balance between adaptation and mitigation, taking into account country-driven strategies, and the priorities and needs of developing country Parties, especially […] least developed countries and small island developing States'* (Art. 9.4). This is in recognition of the fact that the bulk of investments to date have been dedicated to mitigation measures globally.

This outcome directly supports the GCF's investment strategy that already seeks a balance between mitigation and adaptation over time, encouraging geographic balance and a fair allocation across a broad range of countries. Specifically, the fund strives for a minimum allocation of fifty percent of the adaptation funds towards particularly vulnerable countries, including LDCs, SIDS and African States.[3]

The fund also stresses the importance of promoting environmental, social, economic and development co-benefits and taking a gender-sensitive approach. The requirement to take into account broader sustainable co-benefits of supported mitigation and adaptation action also comes back in the Agreement's text, which calls for the promotion of '*sustainable development and environmental integrity'* (Art. 6.1).

[2] GCF pledge tracker. Available on: http://www.greenclimate.fund/contributions/pledge-tracker

[3] GCF. Available on: http://www.greenclimate.fund/ventures/funding

Technology transfer is another area that will be supported by the GCF. The Agreement refers to the Financial Mechanism to strengthen cooperative action on technology transfer by facilitating *'access to technology, in particular for early stages of the technology cycle, to developing country Parties'* (Art. 10.5). This support is to target the Technology Mechanism that was introduced in Cancun and is reiterated in the Agreement. The GCF acknowledges in its governing instrument the need to support technology development and transfer, thereby implying that it is already mandated to cooperate in this field and can be expected to scale-up its efforts to support technology deployment and dissemination.

The GCF is also called to provide assistance with the preparation and communication of nationally determined contributions as well as for the formulation of national adaptation plans (paragraphs 15 and 47). This area of support is likewise recognized by the fund, which mentions the eligibility to fund nationally appropriate mitigation actions (NAMAs), national adaptation plans of action (NAPAs), national adaptation plans (NAPs) in its governing instrument.

LDCs and SIDS

The Agreement calls on operating entities of the Financial Mechanism of the Convention to '*aim to ensure efficient access to financial resources through simplified approval procedures and enhanced readiness support for developing country Parties, in particular for the least developed countries and small island developing States, in the context of their national climate strategies and plans' (Art. 9.9).* This request comes in timely for the GCF, which is committed to consider the needs of countries that are particularly vulnerable to climate change, including LDCs and SIDS.

The fund is currently working on simplifying access by developing '*enhanced direct access'* modalities and simplified processes for approval of proposals for certain activities, in particular small-scale projects (> USD 50 million).[4] Also, a pilot request for simplified proposals may be launched by the fund targeting small-scale activities in LDCs and SIDS in the areas of serving urgent adaptation needs and other priorities.

In terms of readiness, the fund is also contributing its part by making available funds for to support developing country applicants with the accessing GCF money. The support program, which has already been extended to around 20 countries (almost all consisting of LDCs or SIDS), targets assistance with the accreditation process, the identification of a pipeline of suitable projects, and knowledge sharing. The fund agreed to release a further USD 14 million in 2016 to continue readiness efforts and encourage developing countries to tap into the fund's resources.[5]

Results-based finance

The Agreement does not go into specifics concerning the actual design of possible funding mechanisms. However, clear reference is made to the role of results-based payments as a possible funding scheme for incentivizing emission reductions from deforestation and forest degradation as well as related co-benefits (Art. 5.2).

The GCF recognizes the value of incorporating results-based financing, in particular for incentivizing mitigation action through payment for verified results and explicitly mentioning REDD+ as a good candidate. Of interest to many project developers is whether the GCF could expand its form of results-based financing to the purchase of emission reduction units generated by old or new market mechanisms, such as the Clean Development Mechanism (CDM) or the Sustainable Development Mechanism contemplated under Art. 6.4 of the Paris Agreement. Current guidance on the fund's Private Sector Facility mentions the CDM as one mechanism through which private investment into certain small-scale mitigation programs in developing countries can be incentivized.[6] Price guarantees on future Certified Emission Reduction sales are foreseen as one possible avenue through which the Private Sector Facility could encourage private capital deployment at scale.

While the Decision pursuant to the Paris Agreement deals with the pre-2020 context, the role the CDM can play is not mentioned. Reference is made to a CDM-like mechanism supporting sustainable development that could generate exchangeable credits between Parties and is to deliver net mitigation results. Time will tell how the GCF positions its funding activities towards this new mechanism as it takes shape and what role results-based financing will play post-2020.

Accounting

The Paris COP also marks a significant step forward through the introduction of a transparency framework which, amongst others, requests countries to '*develop modalities for the accounting of financial resources provided and mobilized through public interventions in accordance with Article 9.7 of the Agreement'* (para 58).

[4] GCF. Simplified processes for approval of proposals for certain activities, in particular small-scale activities. GCF/B.11/17

[5] GCF. Readiness programme implementation (progress report). GCF/B.11/06

[6] GCF. Business Model Framework: Private Sector Facility. GCF/B.04/07

This push towards harmonizing the accounting of climate finance flows – to be presented during COP 24 in 2018 – is a long-overdue and necessary development if donors are to claim additionality of their contributions. Progress on streamlining accounting methods implies that the GCF will not necessarily need to adopt its own rules on additionality over time.

Another important provision is the requirement for developed countries to submit biennial reports on ex-ante (i.e. projected) as well as ex-post (i.e. actual) levels of assistance provided through public interventions, noting that these reports need to be '*transparent and consistent' (Art.9.7).* Developing country Parties are also encouraged to communicate these flows on a voluntary basis. These requirements are relevant to the GCF as they will put pressure on Parties to work towards the roadmap referred to in the Decision, thereby increasing the transparency and predictability of future funding pledges.

Looking ahead

The outcome of Paris reinforces the role the GCF is expected to play in the post-2020 framework. As one of two operating entities of the Financial Mechanism of the Convention, the fund is to support the flow of adequate and predictable financial resources and as such is well positioned to mobilize a significant proportion of the annual USD 100 billion target by 2020, and beyond. With the fund operationalized and a proportion of the pledged capital signed and paid in, all eyes are now on the types of projects and the forms of funding support that the GCF will venture ahead with.

It is clear that more ambitious pledges from Parties are needed over time to even get close to the USD 100 billion figure. The GCF also has to continue to perfect its modus operandi. Going ahead, the fund should refine its guidance on investment criteria and benchmark indicators, define clearer reporting guidelines and strengthen its environmental and social safeguards. In doing so, it should build on the lessons learned by already established mechanisms under the UNFCCC, such as the CDM. Furthermore, to facilitate access to its funds and unlock the supply of high-quality mitigation and adaptation projects, the GCF also has to scale up its readiness support efforts, in particular targeting the most vulnerable regions of the world. It needs to consider the constraints many developing countries will face with presenting bankable investment opportunities and should work towards introducing innovative funding mechanisms tailored to the needs of local project developers and policy makers.

Finally, while continuing to replenish funds through public avenues, the GCF should strive to leverage private sources of capital. Further development of the modalities of the Private Sector Facility as well as clarity on its funding models will support the fund's strategic positioning towards private businesses and capital markets. Mobilizing these private flows will be pivotal in the GCF's quest to fulfil its objective to achieve a global paradigm shift towards low-emission and climate-resilient development.

Contact: Szymon Mikolajczyk. S.Mikolajczyk@climatefocus.com

OUR OFFICES

Climate Focus (Head Office)
Sarphatikade 13,
1017WV Amsterdam,
The Netherlands

Climate Focus North America (US Office)
1730 Rhode Island Avenue NW,
Suite 601,
Washington, DC 20036
USA

Climate Focus Berlin (Germany)
Schwedter Strasse 253
10119 Berlin
Germany

Colombia Climate Focus (Colombia)
Carrera 11A # 93-94 (oficina 306),
Bogotá, Cundinamarca,
Colombia