Climate Funds Update

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The Green Climate Fund

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The newest actor in the multilateral climate finance architecture is the Green Climate Fund (GCF). The GCF is an operating entity of the Financial Mechanism of the UNFCCC. Parties committed to create it at COP 16 in Cancun, Mexico, and after a year-long Transitional Committee Process to agree on its design parameters, its governing instrument was adopted at COP 17 in Durban, South Africa. Over time, the GCF is supposed to become the main channel for public climate finance. The GCF is a legally independent institution hosted by South Korea, with its own secretariat, and the World Bank as its interim trustee. It functions under the guidance of, and is accountable to, the UNFCCC COP. The 24 GCF Board members, with equal representation of developed and developing countries, and support from the secretariat have been working to operationalise the fund since their first meeting in August 2012. While substantial work has been done, there is much that remains to be agreed before the GCF will be "ready" to raise and start disbursing finance. The lack of clarity on long-term climate finance and, in turn, the likely funding that will be committed to the GCF is a major challenge for bringing this fund from concept to reality. It will be important to try and seek greater clarity on this count at the Warsaw COP, and in the lead up to Paris.

Overview

At its 5th meeting in Paris in October 2013, the GCF Board made important decisions to advance the operationalisation of the GCF, building on its Berlin (March 2013) and Songdo (August 2013) meetings. In the immediate term, the GCF will offer grants and concessional loans, and work through a wholesale model – using the executing capacities of partner organisations that will work as implementing entities – rather than a "retail model" in which it would manage program execution directly. The criteria for accrediting GCF implementing agencies are under development. Funding will only be accepted in forms of grants, concessional loans and paid-in capital contributions. Allocation will need to consider the urgent needs of LDCs, SIDS and African countries, including support for local private sector actors.

The Board also recruited an executive director for the fund, Hela Cheikhrouhou (formerly of the African Development Bank), who heads the GCF Independent Secretariat. It also approved an initial structure for the Secretariat. The secretariat will move to the G-Tower in Songdo, South Korea by November 2013, as Korea was approved as the host country of the GCF. A number of Board committees have been established to oversee risk management and investment approaches. In addition, a Private Sector Advisory Group including external experts will support efforts to attract private sector investment in climate action in developing countries.

The GCF is mandated to take a country-driven approach, and this has been central to Board decisions taken to date. This principle is intended to guide all GCF investment decisions. The GCF will also support readiness and preparatory activities, that will enable countries to develop sound programs and strategies, monitor and evaluate results and meet fiduciary standards as well as environmental, social, and gender safeguards.

The GCF is intended to channel "a significant share of new multilateral funding for adaptation," which is structurally underfunded in the current global climate finance architecture, and balance its allocation between adaptation and mitigation. While the precise volume of finance to be channeled through the GCF is still unclear, it could handle potentially tens of billions of dollars per year. This would be significantly higher than the USD 7.2 billion pledged to the Climate Investment Funds, the largest multilateral climate funds that exist today, or to the Global Environment Facility, which is the longest standing source of climate finance. Pledges for the fully operational GCF are expected to be sought in September 2014 at the earliest, thereby setting out an implicit timeline for GCF operationalisation. To date, the only formal pledges to the GCF have been for its administrative budget, though Korea has committed USD 40 million specifically for readiness and preparatory support activities. As an operating entity of the financial mechanism of the Convention under Article 11, the GCF it is "accountable to and functions under the guidance of the COP".

The GCF Business Model Framework and its Operationalisation

The governing instrument only outlines the broad framework and general direction for the GCF, which has given the board substantial flexibility about how to operationalise the Fund. In exercising this discretion, however, the Board members bear responsibility for making decisions that secure the ambition of the fund, and allow it to achieve its overriding objective of: "in the context of sustainable development ... promoting the paradigm shift towards low-emission and climate-resilient development pathways."

The first GCF Board and its co-chairs Zaheer Fakir (South Africa) and Ewan McDonald (Australia) sought to make the board an efficient decision-making forum, rather than a negotiating body. The Interim Secretariat would play a supporting role in executing the vision of the Board, whose co-chairs acted as its CEO in the absence of an Executive Director for the Fund.

Progress has been slow because of differences between developed and developing countries on visions for the Fund that reflect longstanding tensions from the Transitional Committee design phase of the GCF (see the 2011 and 2012 CFF 11 for a detailed discussion). Key points of difference include the extent to which public contributions should be central to the GCF, the role of the private sector in delivery and whether the GCF should evolve from a fund to a full-fledged bank. Below we summarise some of the key decisions taken in 2013.

Objectives, results and performance indicators and results management framework: In 2013, the GCF Board spent a fair amount of time developing a results management framework against which the impact, effectiveness and efficiency of its funding will be assessed. The results framework defines the elements of a paradigm shift towards low-emission and climate resilient country-driven development pathways, within individual countries, and aggregated across Fund activities. At the Paris meeting in October 2013, 14 initial results areas to be refined and expanded over time were adopted. The focus areas include: low-emission transport and energy access; low-emission power generation at all scales; sustainable land and forest management (including REDD+ implementation); scaling up adaptation; and support for public goods such as "knowledge hubs". The Board decided that more work was needed, especially on additional adaptation result areas. Initial performance indicators for adaptation and mitigation were also agreed, aimed at capturing both outputs funded, as well as the transformative impact of activities. In this context, the indicators also assess co-benefits and gender-sensitivity of GCF investments. A set of additional criteria focusing on development and environment co-benefits of investments, their scalability and non-public funding additionally leveraged will also be included in assessing Fund performance. By mid-2014, the Board plans to finalize a detailed results management framework.

Structure and Organization of the Fund and Establishment of the Independent Secretariat: The Board decided that the Fund would be initially organised along thematic lines with only adaptation and mitigation funding windows and a Private Sector Facility, but with the flexibility to evolve over time; for example, by adding other windows such as one for REDD+. A small-grants facility is also an option. Since January 2012, an Interim Secretariat with a skeleton staff seconded from the UNFCCC and the Global Environment Facility Secretariats supported the GCF Board. As noted, in 2013, efforts to establish an independent secretariat gained momentum. After appointing an Executive Director through a competitive recruitment process managed by the Board, at the Paris meeting, it also approved its initial staffing and structure. The Secretariat will have 5 units: country programming, mitigation and adaptation, private sector facility, external affairs and support services. It will recruit 38 professional and management staff, including 4 experts on mitigation, 4 on adaptation, and 4 on the private sector facility. The Board approved an administrative budget of USD 18.8 million for 2014, contingent on resource availability. The Board also decided to establish accountability mechanisms, including an independent evaluation unit reporting to the Board, an integrity unit and an independent redress mechanism to address complaints related to Fund operations. It will consider their exact form and functions in early 2014.

Financial Instruments: The GCF Board agreed to initially offer only grants and concessional loans. Over time the Fund may offer other financial instruments such as equity investments or risk guarantees. The GCF secretariat will have to develop a risk management approach and recruit specialised expertise to explore these options with guidance from a Board Risk Management Committee. The Committee will review investment proposals and instruments and recommend them for approval. Some developing country Board members are concerned that more complex financial instruments would move the Fund towards a bank structure, thus undercutting the core mandate of the GCF as an operating entity of the financial mechanism of the UNFCCC, which focuses on meeting the additional costs of climate change-related interventions through concessional financing.

Forms of capitalisation: While the Governing Instrument of the GCF states that developed countries will provide the bulk of GCF financial inputs, the Board decided to allow for flexibility in resourcing. Initially, it will only accept grants from the public and private sector, paid-in public capital contributions and concessional public loans. Over time, it may attract other forms of finance - from the private sector, as well as alternative sources (for example new taxes or levies from which funding might be raised for the GCF). By accepting loan contributions, however, the risks and concessionality of finance that the GCF will be able to offer recipients may be constrained, as it will need to make an adequate return on its investments to be able to repay these loans. These risks will also need to be carefully overseen by the Board's standing Risk Management Committee. Developing countries can also contribute to the fund, and indeed, the GCF host-country South Korea has already provided USD 2 million in finance for the secretariat and made informal pledges of USD 40 million finance for the GCF's programming for readiness and preparatory support.

Allocation: The GCF Board is supposed to "balance" allocation between mitigation and adaptation, but the term balance is not defined in the governing instrument or the UNFCCC COP decision in 2011 that established the Fund. The Board initially approved allocation under a theme-based approach for adaptation, mitigation and the Private Sector Facility (PSF), respectively. Allocation for adaptation is to consider the urgent and immediate needs for the most vulnerable countries (LDCs, SIDS and African States), while resources allocated under the PSF are to focus on local private sector actors, including Small and Medium Enterprises. The Board plans to agree on a comprehensive resource allocation system for the GCF by mid-2014, which might also consider geographical balance, cross-cutting proposals and results-based approaches in the distribution of GCF funding among countries. It is not yet clear if the Board will support minimum and/or maximum allocation floors to allow the largest possible number of developing countries to benefit from GCF resources.

Country Ownership: The Board confirmed country ownership and a country-driven approach as core principles of the Fund. A National Designated Authority (NDA), or a focal point, will act as the main point of contact for the Fund, and ensure the consistency of funding proposals with national climate and development plans. Countries will have flexibility on the structure, operation and governance of NDAs, though the board has sought guidance on good practices in coordination and stakeholder engagement for the Fund. The board will also have to decide on a transparent "no objection" procedure through which countries can either endorse or raise concerns about proposed programs or projects. This is intended to ensure recipient country ownership of funding for programs that are not implemented by governments; for example, through the private sector. While developing countries have been weary of funding for projects that don't reflect their interests, there is also a recognised need for private sector funding to be nimble and simple.

Access Modalities: Like the Kyoto Protocol's Adaptation Fund, the GCF will give recipient countries direct access to funding through accredited national implementing entities. Countries can also access funding through accredited sub-national, international and regional implementers and intermediaries (such as multilateral development banks, UN agencies; but also national development banks, regional development banks, private sector institutions and non-governmental organizations). Work has started to agree on accreditation criteria and processes. Implementing entities will need to meet strong fiduciary standards to ensure good financial management, and have best practice environmental and social safeguards in place. A team of Board members and senior external international experts will oversee the accreditation criteria and process, informed by good practice standards and policies in place at institutions such as the World Bank Group, the GEF and the Adaptation Fund. Developing countries have also been keen to explore modalities for enhanced direct access in 2014, which would allow developing country based institutions to receive an allocation of GCF finance and then make their own decisions about how to programme resources, rather than only accessing smaller amounts of finance at a time for discrete projects and programs approved by the GCF board. One modality to this end could be through national climate change trust funds, which create a forum for nationally driven country programming and have their own project pipeline

Readiness and Preparatory Support: Least Developed Countries, Small Island Developing States and some developed countries on the GCF Board have made the case for early support for "readiness activities" that would build country capacity to access and program GCF finance effectively. As a first funding priority under such activities, the Board decided to support national and regional implementing entities and intermediaries to meet GCF accreditation standards. This is intended to ensure that these standards do not become a barrier to direct access to the GCF. The Fund will also provide readiness support to strengthen the institutional capacities in recipient countries for country coordination and multi-stakeholder consultation mechanisms as needed, as well as to prepare country programmes and project pipelines. In 2014, the Board will consider a detailed work programme for providing readiness and preparatory support. In parallel, the government of Germany is providing EUR 40 million in finance for readiness activities in selected pilot countries, working through bilateral agencies, and multilateral institutions, including UN agencies. The Independent Secretariat is supposed to develop a work programme that complements and coordinates ongoing initiatives. The USD 40 million funding pledged by South Korea is also expected to support readiness activities.

Private Sector Facility: The Private Sector Facility (PSF) is to provide funding to private actors, and support activities that enable private investment in low carbon and climate resilient approaches. While there was discussion of the need for a separate governance structure for the facility, it has been decided that the Facility will operate under the guidance of the full GCF board.

There has been particularly strong interest in the private sector facility from developed countries, who want their limited public finance to leverage and crowd in private sector investments. There is also a case for public finance to be used to address market failures that impede private investment in mitigation and adaptation. Indeed, many governments see this as key to ensuring that the GCF meets its objective of realizing a paradigm shift towards low carbon and climate resilient development. Initially, the PSF will use only grants and concessional loans provided to accredited implementing agencies and intermediaries. Over time, the range of instruments to be used could expand, and direct finance to private sector actors might be considered. The Board decided to establish a 20 person Private Sector Advisory Group (PSAG) that will make recommendations to the Board on Fund-wide engagement options and opportunities with the private sector. It is to be composed of four private sector representatives, each from developed and developing countries, in addition to two civil society experts and three Board members, each from developed and developing countries. The four formal GCF active observers from the private sector and civil society will participate as well.

Gender: At its last Board meeting in 2013, the Board reaffirmed the need for GCF actions to take a gender-sensitive approach in all its funding. It will consider practical options to this end in early 2014 in conjunction with key decisions on the BMF. This should make the GCF the first dedicated climate fund to develop a gender policy before the beginning of its funding operations. The Board will also have to address other gender provisions in the governing instrument, including the need for gender balance among the Secretariat staff and in the GCF Board (which currently only has 3 women on the 24 person Board, and 3 female alternate Board members).

GCF Relationship to the UNFCCC and the COP: The GCF is an operating entity of the UNFCCC's financial mechanism. It is to be "accountable to and function under the guidance of the COP". The GCF Board has sought to define the arrangements between the COP and the GCF. The Standing Committee on Finance (SCF), a complementary UNFCCC body aimed at taking stock and ensuring accountability in the global climate finance architecture, has also developed recommendations to this end in parallel. In October 2013, the GCF Board reaffirmed its full responsibility for funding decisions. It will prepare an annual report on its programmes, policies and priorities and status of resources. It will respond to feedback and guidance received in reaction from the COP. In addition, the COP will have the authority to commission an independent assessment of the GCF, which would evaluate overall Fund performance, including that of its Board and the adequacy of its resources, in connection with periodic reviews of the UNFCCC financial mechanism.

Stakeholder and Observer Input and Participation: The GCF governing instruments anticipates extensive stakeholder participation in the design, development and implementation of the strategies and activities financed by the GCF. Stakeholders are broadly defined as "private sector-actors, civil society organizations, vulnerable groups, women and indigenous peoples." The Board will need to operationalise this mandate in the context of making arrangements for country-ownership and coordination with the fund, and in accreditation criteria for implementing entities and intermediaries. Support for stakeholder engagement will also be essential to GCF readiness support.

There is also a provision for stakeholders to observe the deliberations of the Fund, and for 2 active observers from the private sector and civil society, respectively, to provide input at Board meetings. In 2013, the Board established GCF specific accreditation procedures for observer organizations (international institutions, civil society groups and the private sector). The Board approves application of interested groups on a no-objection basis before each Board meeting. Active civil society and private sector observers (from developed and developing countries, respectively) have been identified by mid-2013 for a two year period through a self selection process. GCF active observers can only make interventions at the invitation of the co-chairs. Unlike with other funds, they are not invited to suggest agenda items for Board meetings, or request expert input to the Board discussion. They are also currently unable to participate in committees and panels of the Board – which is where many decisions are taken in parallel to full board meetings and intersessionally – unless specifically invited.

Information Disclosure and Communication Strategy: The disclosure practice of the GCF has improved significantly over the past year. Board meeting documents are now posted on the GCF website at the same time they are sent to Board members, advisors and active observers (www.gcfund.net). A comprehensive information disclosure policy is also under development, and the Board agreed that there would be an assumption of disclosure, and documents would be only kept confidential on an exceptional basis under special circumstances (a "negative list approach"). The Board, however, has objected to live webcasting of its meetings: a decision that drew criticism from many stakeholders and observers because live webcasting would present a relatively low cost way to increase transparency and public awareness of the process. Other climate finance bodies, for example the CDM-Board and the Adaptation Fund Board, routinely webcast their meetings. The video recordings of the Board sessions will only be available to registered users via the GCF-website three weeks after the Board meeting. The Secretariat is in the process to develop a communication strategy, which will set parameters of sharing information with the public, and its engagement strategy to build global awareness and support for the GCF.

Resource Mobilisation: As noted, resource mobilisation is one of the major challenges before the Fund, and a point of controversy. While developing countries have sought early clarity on resourcing, developed countries have wanted clarity on the business model of the Fund before they can justify pledging resources. In October 2013, the Board agreed to finalise work on the first eight operational core policies in order to "trigger" a first formal replenishment meeting. This would then be followed up with a more formalised replenishment process (akin to that used for the GEF or the World Bank's International Development Association). No date has formally been committed to for this process, but there is an expectation that the UN Secretary General's Climate Summit in September 2014 will be the impetus for a first pledging meeting.

The next two GCF Board meetings are supposed to prioritize and focus essential decisions, notably (1) an initial Fund and Secretariat structure; (2) risk management and investment frameworks; (3) the results management framework and associated indicators; (4) an accreditation process for implementing entities and intermediaries, including fiduciary standards and social and environmental safeguards; (5) initial allocation procedures; (6) funding approval process with initial criteria; (7) modalities for the operation of the adaptation and mitigation windows and the PSF; and (8) the terms of reference for the Fund's accountability and redress mechanisms. So far, the Fund only has USD 9 million to pay for administrative costs, which will not cover its budgeted administrative costs of USD 18.8 million in 2014.

Outlook for 2014

Much work remains to be done in 2014 to get the GCF ready to receive and programme significant resources. Three Board meetings are planned in 2014 (in late February, late May and early September). If these proceed on schedule, it is hoped that the eight work areas outlined above can be addressed successfully in order to trigger a first formal pledge meeting by September 2014. Two new co-chairs will need to manage this challenging agenda: in October, the Board elected Manfred Konukiewitz (Germany) and Jose Maria Clemente Sarte Salceda (Philippines) for a one year term. The new co-chairs should be able to rely on an independent Secretariat with growing staff and expertise to support this work (though recruiting these personnel will be a slow process). It is hoped that the Board will be able to delegate more decisions to the Secretariat, in a spirit of efficiency, placing trust in its new Executive Director. In turn, the new Director takes on a substantial responsibility for shepherding this complex work program through to timely completion.

Although the Durban decision on the GCF stressed the need for an "early and adequate replenishment process", based on voluntary contributions, it does not address how to secure sufficient long term capitalisation of the Fund. This issue is, of course, linked to wider UNFCCC negotiations on long-term finance, which remains unresolved despite a two-year work program that began in 2011.

Developed countries will need to indicate broadly how much they are willing to contribute to the GCF in the medium and long-term as part of their commitment to raise long-term climate finance to US$100 billion from public and private sources per year by 2020. Without clarity on this count, it will be impossible for the GCF to get down to business. But developed and developing countries will both share responsibility for designing a Fund that can be effective, and uses the resources that it raises well in order to fulfil its visionary mandate.

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The Climate Finance Fundamentals are based on Climate Funds Update data and available in English, French and Spanish at **www.climatefundsupdate.org**

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