SUBMISSION BY MEXICO

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Subject: **Enabling the full, effective and sustained implementation of the Convention through long-term cooperative action now, up to and beyond 2012**

(e) Enhanced action on the provision of financial resources and investment to support action on mitigation and adaptation and technology cooperation

Mexico welcomes the opportunity to submit, as requested by the AWG-LCA (FCCC/AWGLCA/2008/8), specific proposals on *enhanced action on the provision of financial resources and investment to support action on mitigation and adaptation and technology cooperation*, as contained in paragraph 1 of the Bali Action Plan.

Introduction

The current financial system in place for tackling climate change includes a large number of specific funds, generally with limited scope and an inadequate structure of governance, together with the Kyoto Protocol flexible mechanisms. In particular, the Clean Development Mechanism (CDM) is the only instrument allowing the participation of developing countries, through compensating for excess emissions in developed countries. The CDM does not expand the global scale of mitigation. Moreover, the CDM faces other difficulties and limitations, including the fact that it has not been accepted by all developed economies. The current financial system thus turns out to be insufficient to support the action required in developing countries.

The document *Investment and Financial Flows to Address Climate Change*, developed by the Convention's Secretariat, is invaluable for orienting this process. It indicates that, including public and private sources, global additional investment and financial flows required in 2030 to return global greenhouse gas emissions to current levels would amount USD 200 - 210 billion, 46% of which would correspond to non-Annex I countries (92 - 96 billion dollars). This estimate does not take into account adaptation requirements.

For the energy sector alone, some estimates by the International Energy Agency and the World Bank calculate that additional annual investment requirements needed by developing countries to ensure a low carbon energy future may amount to US$30 billion dollars.

Some of the additional investment needed for mitigation could be met with existing mechanisms (carbon finance, GEF, Official Development Assistance, etc.). The future scope of these mechanisms is uncertain, and depends on the evolution of commitments made by developed countries. However, even using the most optimistic estimates, the mechanisms that exist today would not be able to reach the necessary level of investment.

In consequence, we face the challenge of designing a financial mechanism able to broaden the scale of mitigation and adaptation activities. Such an instrument must be financially feasible, equitable, predictable, efficient and inclusive, while encouraging the full participation of countries, both developed and developing, based on their own circumstances and needs.

A World Climate Change Fund

Proposal
Mexico proposes that as part of an agreed outcome resulting from the Bali Action Plan, a World Climate Change Fund (Green Fund) be multilaterally agreed upon and established as a financial scheme that complements existing mechanisms and ensures the full, sustained and effective implementation of the United Nations Framework Convention on Climate Change (UNFCCC).

Objectives
The Fund would have as specific objectives the following:

- To scale-up funds for mitigation actions,
- To support efforts to adapt to the adverse effects of climate change and the impacts of response measures,
- To provide technical assistance and promote the transfer and diffusion of clean technologies,
- To contribute to the financial underpinning of the new global climate change arrangement based on the Convention.

Contributions
It is expected that all countries contribute to the *Fund* in strict accordance with the principle of *common but differentiated responsibilities and respective capabilities.* Differentiation of responsibilities and capabilities could be determined through the adequate use of three simple indicators:

- **Greenhouse gas emissions.**
- **Population.**
- **Gross Domestic Product (GDP).**

Methods for ascertaining possible contributions could be developed based on several models that combine these simple indicators. Contributions will be determined using an objective formula, periodically subject to review, and based on criteria such as:

A. Polluter pays. This principle allows adjusting each country's contribution to their greenhouse gas emissions, in such a way that the largest emitters contribute the highest financial quotas to the Fund. A reasonable sequence of data is available for CO_2 emissions from burning fossil fuels.

A country willing to use the Fund for reducing emissions from deforestation and degradation activities, must include its land use and land use change emissions for determining its contribution, in accordance with the inventories guidelines set out for the drawing up of National Communications.

With regard to historical emissions and cumulative effects, several possibilities are feasible:

1. To disregard cumulative emissions for determining contributions and take into account only current emissions.
2. To calculate the responsibility derived from historical emissions in terms of their contribution to increasing temperatures (*Brazil's Proposal*).
3. To calculate cumulative emissions from 1990, a general reference for National Communications, or 1992, when the *Convention* was adopted.

B. Equity. In considering equity, not only total emissions but also *per capita* emissions should be taken into account. The climate regime must induce a progressive convergence of *per capita* emissions in order to be equitable.

On the one hand, some emissions derive from productive processes linked to the satisfaction of a population's most basic needs and should be differentiated from those of countries with a much greater level of development. On the other hand, terrestrial and marine ecosystems may absorb a small amount of emissions without contributing to the growth of atmospheric concentrations. Every person on Earth should benefit equally from this environmental service.

C. Efficiency. Emissions can be differentiated in relation to the scale of the economic activity producing them. The *carbon intensity* (emissions per unit of GDP) of an economy reflects precisely this differentiation factor. Carbon intensity can be reduced by introducing technological improvements to increase efficiency. Nevertheless, it also can be induced through structural changes in the economy, such as greater development of the services sector, with its relatively lower emissions.

D. Payment capacity. A country's economic capacity to tackle climate change could be represented by an indicator such as GDP *per capita*, and in terms of the relative size of a national economy in proportion to the global economy. GDP can be expressed in terms of current prices or purchasing power parity, to take into account the relative purchasing power of each country's currency.

As with several other factors, it would seem equitable to agree that those with greater capacity make larger contributions to the *Fund*. Experience already exists in multilateral fora for determining contributions according to countries' capacity to pay (e.g. United Nations, World Bank, International Monetary Fund, among others).

Mexico is aware that the best objective formula for determining contributions will be that reached through consensus. This would be of utmost importance for providing stability and predictability to the financing scheme and potential alternatives to models of "voluntary contributions" for specific ends or "official development assistance", both of which will be maintained, being complementary to the proposed system.

It is suggested that negotiations focus first on general arrangements and organizational concepts, including the contributions structure and the complementary nature of the proposed *Fund*. Once the general scope and structure of contributions have been defined, the most important parameter will be determining the total scale of financial resources to be mobilized by the *Fund*. Whichever formula is adopted, the total amount of the *Fund* should be scalable and be increased periodically, without requiring the restructuring of the formula for relative contributions.

In its initial phase, it is expected that the Fund should mobilize no less than 10 billion USD per year. Several mechanisms could mobilize new financial resources that could be directed to the Fund, such as auctioning permits in domestic cap and trade systems in some developed countries, or the possibility of taxing air travel, without putting excessive pressure on public financing.

Developing countries that choose not to join the Fund would be excluded from its benefits, without any penalty. The creation and operation of the Fund should not represent a disadvantage to any developing country.

Distribution of resources for mitigation activities

In principle, all countries, developed and developing, could benefit from the Fund. The mitigation activities to be supported shall be defined by contributing countries, based on their own development needs and in accordance with their national circumstances. These activities should nevertheless determine mitigation results that are **real, measurable, reportable and verifiable.** In this sense, it is necessary to adopt baselines derived from periodic emissions inventories with strict methodologies such as those used for National Communications under the Convention. This reference to baselines abates transaction costs and overcomes the need of much stricter additionality tests of CDM projects derived from their offsetting nature.

Activities eligible for receiving support from the Fund could be on a variety of scales, from isolated activities and projects to programs, sub-sectors, entire sectors or sub-national approaches. The Fund will thus be able to cover the intermediate scale between isolated projects, which would still be supported by the Clean Development Mechanism and the Joint Implementation Mechanism of the Kyoto Protocol, and whole economies -a scale corresponding to developed countries' national emissions mitigation commitments included in Annex B of the Kyoto Protocol.

The distribution of resources between proposals will be determined by the criteria and guidelines issued by the COP. For example, resources could be allocated in the first instance as a function of the funding given to a unit of emission reduction. A second possible criterion would be the total volume of emissions reductions.

Eligible activities could include the following:

- **"Grey" Agenda**
  - Increased energy efficiency in various sectors.
  - More efficient, non-renewable energy sources with lower emissions.
  - Large scale promotion of renewable energy sources.
  - Greenhouse gas capture and storage.
  - Reduction of fugitive emissions.
  - Programs for greener buildings, including reduced household energy consumption (energy efficient lighting and electric appliances).
  - National programs for methane management (landfills, livestock, mining).
  - Waste and residual waters management.
  - Changes in transport modal structure.
  - Introduction of low emissions vehicles.
  - Reduction of emissions from fluorinated gases.
  - Access to and development of clean technologies.

- **"Green" Agenda**
  - Reducing emissions from deforestation and degradation of forested lands.
  - Reforestation, afforestation and revegetation.
  - Forest fire prevention and control.
  - Reducing emissions from cropland soils.
  - Production and use of biofuels under strictly sustainable conditions.

To avoid imbalances, an upper threshold (e.g. 15% of the Fund's total amount) is proposed on withdrawals by any single developing country. If any developing country reaches that limit and uncommitted resources still remain, that country may request additional resources up to a maximum of the available yearly total.

It would be desirable to include among the criteria adopted for the selection and allocation process, one whereby those countries assuming greater commitments receive larger incremental resources.

While the CDM only relocates mitigation efforts, enabling the Parties in Annex B of the Kyoto Protocol to comply with their obligations without increasing the scale of mitigation provided for under this instrument, the Fund would expand the overall scale of mitigation, by incorporating efforts undertaken voluntarily by developing countries and enhanced through incentives from contributor developed countries.
Developed countries will only be entitled to use a fraction of their contributions (e.g. 70%), so that developing countries may have access to financial resources much bigger than their own contributions. This must be the stronger incentive for developing countries´ participation in the *Fund*.

A part of the total contributions to the Fund could be set aside for the benefit of Least Developed Countries, which in general terms are likely to be most affected by climate change. Negotiations might include the possibility that Least Developed Countries could benefit from the Fund without making a contribution to it, as long as they comply with the general rules of its operation.

Possible future links with existing carbon markets
Whenever the Kyoto cap and trade scheme and the *Fund´*s operation stabilize, it might be useful to analyze whether mitigation efforts under multilateral supervision supported by the Fund could determine the accreditation of carbon units, subject to discount rules to be agreed upon to ensure the environmental integrity of the scheme. However, the fungibility of these carbon units with those from other instruments, such as the mechanisms established under the Kyoto Protocol, must be subject to careful consideration. Ensuring this capacity of exchange and avoiding double accounting for the same mitigation effort, would open the possibility of a major private sector participation in the *Fund* and establish functional connections between this scheme and those –existing or potential– based on cap and trade principles. In this case it would be necessary to establish a stricter additionality requirement for the activities of developing countries supported by the *Fund*, and to increase the commitments of developed countries to take into account the greater ease of compliance arising from the enlarged scale of the new instrument constituted by the *Fund*.

Derived Funds: adaptation and technology
Should mitigation efforts, adaptation, and the development, transfer and deployment of clean technologies be undertaken separately, financial mechanisms should be designed for each of these activities. The proposed *Fund* could establish linkages between mitigation, adaptation and technology transfer and development. To that end, it is proposed that all contributions received by the Fund should be subject to a double levy, to be determined through negotiations.

The first levy would be for the Adaptation Fund, at present only fed by contributions from the CDM operation (2% of the share of proceeds). This enlarged Adaptation Fund would maintain the scheme of governance agreed by Decision 1/CMP.3. Regardless of any other involvement with the Fund, developing countries particularly vulnerable to the adverse effects of climate change would benefit from the creation and operation of it. Within a year of operation it could generate resources to promote adaptation measures, which would be of a similar magnitude to those accruing to the current Adaptation Fund through the operation of the CDM over its entire first commitment period.

The second levy, similar in scope to the first, would enable the development of a Clean Technology Fund, to promote:

A. Technical assistance for project preparation, including those that can be referred to the Fund.

B. Transfer and development, demonstration and dissemination of technologies that are close to acquiring commercial status and that even in the short term, would allow beneficiary countries to reorient their development towards a lower carbon economy.

Governance

The Fund will operate under the aegis of the COP, and will be subject to general guidance from the latter steered through an inclusive and transparent governance scheme. All contributing and beneficiary countries, developed and developing, will participate in the system. This arrangement must contribute to the achievement of a sense of collective ownership.

The operation of the Fund will depend on an Executive Council, constituted by representatives of all participant countries. They should be grouped in a balanced and practical way. The Council will have three independent counselors: i) a scientific counselor, ii) a counselor from the multilateral development banks, and iii) a counselor from social organizations. Developing countries will have the same relative weight and voice as developed countries. Being a financial instrument, country representatives to the *Fund* would be from Finance Ministries or their equivalent. The Executive Council will report annually to the COP of the *Convention*.

The Executive Council will have two support committees:

Scientific Committee. To be established in consultation with the Intergovernmental Panel on Climate Change, it will issue recommendations about policies, strategies and programs that the *Fund* can support.

Multilateral Banks Committee. It will issue recommendations in its field of competence.

Setting up the Fund should not lead to the creation of a new bureaucratic organization or an additional administrative burden, the COP will decide upon an existing multilateral institution that has global and financial experience in the field, for administering the Fund.