

## **Cross-cutting issues in the design of the Green Climate Fund**

Background information note prepared by the Technical Support Unit for the Transitional Committee under the guidance of the Co-Chairs

### **Background**

1. The Conference of the Parties (COP) to the United Nations Framework Convention on Climate Change (UNFCCC) in its decision 1/CP.16 entrusted the Transitional Committee (TC) with the design of the Green Climate Fund (GCF) and with the development and recommendation of operational documents for the Fund for approval by the COP at its seventeenth session.
2. Reports on the four workstreams<sup>1</sup> at the second meeting of the TC held in Tokyo, Japan, on 13–14 July 2011 identified a number of critical information gaps. It was agreed that such gaps should be analyzed in order to strengthen the common understanding of TC members of various GCF design elements and options. Some specific issues were highlighted during the Tokyo meeting such as the important inter-linkages between GCF design elements and the implications of choosing one design option over another. Other questions included the legal status of the GCF, how to effectively mainstream gender in GCF operations and other topics discussed later in this note. The Co-chairs invited TC members to submit their suggestions for additional issues to be analyzed and requested the Technical Support Unit to assist by analyzing and preparing background information on the identified issues.
3. This background note is a synthesis of the following: statements and written submissions from TC members and observers relating to the aforementioned information gaps, a targeted literature review, the results of a survey of various funds, and the mapping of linkages between GCF design elements within and between the four workstreams. In conducting the work the advice of various legal experts with different specialization was sought. Submissions have provided the basis for the draft extended outline of the report by the TC to COP 17. This paper provides an overview of key linkages between the options in different sections of the outline, and discusses some of the main implications of choices to be made by the TC. It presents commonalities as discrete options for consideration by the TC. It also highlights key issues or points of divergence about which the TC may hold discussions, citing examples where available.
4. Specifically, this paper discusses options and implications that appear to be of high priority in terms of GCF design decisions to be taken by the TC. The first chapter looks at issues where submissions by TC members proposed different options. These options are presented in text boxes upfront and followed by a brief discussion of linkages and implications. The document does not provide comprehensive synthesis of submissions. Submissions have been presented in compilation documents 8, 9, and 10. These submissions also highlighted issues to be analyzed. More detailed descriptions of the implications of key design elements and cross-cutting issues are presented in the subsequent chapters.

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<sup>1</sup> The TC organized its work through four workstreams as follows:  
(a) Workstream I on Scope, Guiding Principles, and Cross-cutting Issues;  
(b) Workstream II on Governance and Institutional Arrangements;  
(c) Workstream III on Operational Modalities;  
(d) Workstream IV on Monitoring and Evaluation.

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## **Chapter I                    Linkages between GCF design options and main implications of choices to be made**

### **A.    Nomination /Selection of the Board members**

Main options proposed in the submissions

Option 1: GCF Board members are selected and designated by their respective constituencies.

Option 2: Regional Groups shall nominate their representatives to the Board. Nominated Board members will be endorsed by the Conference of Parties.

Option 3: GCF Board members should be selected and designated by their respective constituencies. The two constituencies - developed and developing countries will determine within their respective constituencies the procedures for self-selection of their representatives on the Board. Board members will be selected without approval/ endorsement from the COP, or any other mechanism.

Option 4: Board members should be elected by the COP.

*Main linkages and implications*

1.     Nomination of Board members is linked to membership of the Fund and its legal status. The role of the COP in nomination of Board members is also linked to the arrangement to be agreed between the COP and the GCF.

2.     The starting point for Board composition is decision 1/CP.16, which determines the number of members of the Board: 24–12 each from the two main constituencies to be represented—developed and developing countries. The decision does not provide for observer organizations or other stakeholders to become members. The key issues for further consideration are which Parties are eligible to represent developing’ or developed country Parties on the Board as there is no definition of these terms or the composition of these two constituencies, and what should be the procedures for the nomination and appointment of new members to the Board and any role of the COP in such a process.

### **B.    GCF accountability to the Conference of the Parties**

*Main options presented in submissions*

The GCF shall be governed by a Board, which shall supervise and manage the Fund, and shall be accountable to and operate under the guidance of the COP.

Option 1:

The COP shall decide on its overall policies in line with relevant decisions. In implementing the principle of accountability to the Conference of the Parties, the Board shall submit annual reports to the COP for its consideration and deliberation, on various operational matters, including:

- Strategic priorities, operational policies guidelines and procedures;
- The status of the Fund, in terms of contributions and disbursements, including on shortfalls/surplus of resources and its assets and liabilities, as well as an estimate of additional resources leveraged by the Fund including through private sector engagement;
- The Fund’s annual operational budget;
- The approved projects and activities including, inter alia, funded projects, projects approved for funding pending availability of resources, projects that received conditional approval as well as the total amount of resources committed/ to be committed for approved projects;
- The Fund’s triennial business plan and the Fund’s annual work programme/business plan, including projections for resource allocations to the agreed thematic windows, demonstrating a balance between adaptation and mitigation activities; and
- Any other matters that may be required by the Conference of the Parties.

Option 2:

The Board should have full responsibility for funding decisions and retain independence in decision-making with regard to funding projects and programmes.

Option 3:

The Board will receive guidance from, and be accountable, to the COP consistent with arrangements negotiated between the COP and the Board. The Board will approve any such arrangements.

*Main linkages and implications*

3. There appears to be general agreement among TC members that the GCF shall be governed by a Board, which shall supervise and manage the Fund, and be accountable to and operate under the guidance of the COP. However, members' views differ on the nature/form of guidance and accountability. Suggestions from TC members can be summarized as either:

(a) The COP taking broad policy decisions with the Board responsible to implement the decisions and annually reporting back to the COP on the implementation and operational matters. In implementing the principle of accountability to the Conference of the Parties, the Board shall submit annual reports to the COP for its consideration and deliberation, on various operational matters;

(b) The Board should have full responsibility for funding decisions and retain independence in decision-making with regard to funding projects and programmes; or

(c) The Board will receive guidance from, and be accountable, to the COP consistent with arrangements negotiated between the COP and the GCF.

4. These three suggestions have potential inter-linkages with the following:

(a) The legal standing of the GCF, its governance and institutional arrangements (see chapter II below);

(b) The proposed guiding principles of efficiency and effectiveness as the timing of key policy decisions could be affected;

(c) The resource mobilization process, frequency of meetings and the clear definition of the roles and responsibilities of the Board and the COP;

(d) The monitoring and evaluation as well as the reporting substance and content.

### **C. Legal Status**

*The main option presented in submissions by TC members was:*

The Fund, as a body under international law, shall be endowed with a juridical personality. Consequently, the Fund shall enjoy such legal capacity as is necessary for the exercise of its functions and the protection of its interests, in particular the capacity to enter into contracts, to acquire and dispose of movable and immovable property and to institute legal proceedings in defence of its interests.

The Fund shall avail itself of such privileges and immunities in the territory of the host country, pursuant to the 1946 United Nations Convention on Privileges and Immunities, as is necessary for the fulfilment of its purposes.

The officials of the Fund Secretariat shall similarly enjoy such privileges and immunities as are necessary for the independent exercise of their official duties.

5. The legal status of the GCF will have a major impact on the governance and institutional arrangements of the GCF including (i) the arrangements between the COP and the GCF; (ii) the Board; (iii) the secretariat, (iv) financial inputs; (v) transitional arrangements, and (vi) operational modalities,

including direct access, the process of monitoring, the redress mechanism and independent evaluation. The details of various legal options, their linkages and implications are presented in chapter II below.

#### **D. Participation/Membership**

6. The membership of the GCF is linked to legal status of the Fund. Main options are:

Option 1: All Parties of the UNFCCC will be the members of the Fund if the Fund is provided legal personality through a decision of the COP.

Option 2: Any Party to the UNFCCC may decide to participate in the GCF if the GCF does not have a legal personality or is provided legal personality by a Party e.g. like the Global Environment Facility and Global Fund.

Option 3: Any Party to the UNFCCC may become a member of the Fund by acceding to the treaty establishing the GCF if the GCF is established through a new treaty e.g. like the MDBs.

#### **E. Financial Inputs**

*Main options presented in submissions were:*

- The Fund will “seek to mobilize financial resources” in accordance with Article 11, as well as Articles 4, paragraphs 3, 4 and 5 of the Convention.
- The Green Climate Fund will accept finance from multiple sources, primarily government but also non-government sources. The Board will periodically consider possible new sources of finance.
- Option 1: Finance will be raised by issuing bonds on capital markets.
- Financial inputs to the Fund will be in the form of:
  - Option 1: Finance will be primarily accepted in grant form;
  - Option 2: Finance will be accepted in a variety of forms, including grants, loans, and investments and private sector contributions.
- The Green Climate Fund will use a replenishment process to mobilize financial inputs in complement with a system of continuous inputs.
  - Option 1: In accordance with Article 4.3 and relevant decisions of the Conference of the Parties, the provision of financial resources shall reflect “appropriate burden sharing among the developed country Parties”.
    - Option 1a: The negotiation of the scale of assessments to be applied to developed countries should be carried on under the COP.
  - Option 2: A replenishment process will be developed by the Board that includes guidelines for the periodicity and the negotiation process for the overall level of funding required for the replenishment period.

*Main linkages and implications*

7. Overall, TC members have underlined that the GCF shall be larger than any existing climate finance entity and be scalable over time and a significant share of new multilateral funding should flow through the GCF.

8. The different specific proposals on sources and inputs could affect the overall amount, and sustainability of funding available from the GCF. The use of bonds and interactions with associated capital markets in particular would impact the legal arrangements and complexity of Trustee services whether inside or outside the Fund. Moreover, this will require the definition of strict criteria and operating rules for all the options.

## **F. Financial Instruments**

*The main option presented in submissions was:*

- The GCF shall provide grants;
- Option: The Green Climate Fund will also provide a variety of non-grant instruments and sector budget support.
- Reflows from the Fund's investments will be dedicated to further GCF programming in developing countries.
- The Board will seek to optimise the mobilisation of additional public and private resources at national and international levels.

*Main linkages and implications*

9. The implications of the decision on which option will be adopted are primarily on (i) the overall size of the GCF and (ii) the level of engagement with private sector. Depending on the instruments available, such as guarantees, structured finance, risk capital, the business model chosen for the GCF (wholesale or retail), there will be an impact on size and staff know-how required in the Secretariat of the GCF. The inter-linkages are with the (i) legal arrangements, (ii) forms of inputs (sources) of funds, and (iii) Board responsibilities.

## **G. Operational modalities**

### **1. Eligibility**

*Main options presented in submissions were:*

The TC members have noted that the Board will formulate detailed operational guidelines for plans, programmes and projects that are eligible for funding in each of the thematic areas covered by the Fund, taking into account the recommendations of relevant thematic bodies under the Convention.

On the nature of support provided, submissions from members can be summarised as follows:

- Option 1: finance from the GCF should be used to cover incremental costs.
- Option 2: finance from the GCF should be used to cover incremental and full costs.
- Option 3: finance from the GCF should be used to cover full adaptation costs and incremental mitigation costs.

*Main linkages and implications*

10. The inter-linkages are primarily secondary or tertiary with regards to eligibility and funding criteria to be adopted by the Board and applied by recipient entities. The selection of one option over the other could also impact the amount of funding made available to individual programs and projects and therefore (i) the amount of co-financing needed and (ii) the number of programmes and projects for which funding will be available.

## **2. Funding Windows**

*Main options presented in submissions were:*

- The Green Climate Fund will have thematic funding windows.
- In the context of the need to ensure balance between adaptation and mitigation:
  - Option 1: The Green Climate Fund will initially have funding windows for adaptation and mitigation.
  - Option 2: The Green Climate Fund will initially have funding windows for adaptation, mitigation, and additional window/s for:
    - Option 2a: REDD plus
    - Option 2b: the private sector
    - Option 2c: capacity building
    - Option 2d: technology development and transfer
    - Option 2e: SIDS and LDCs
- The Board shall have the ability to add and remove windows as necessary.
- Capacity development and technology development and transfer activities that are embedded within these areas will cut across the thematic funding windows. Funding will be available in each window for these activities.
- In addition, readiness and preparatory activities that are not thematic shall be supported by the Green Climate Fund, including the preparation of national climate plans and strategies, the development of in-country institutional arrangements to access, manage, and programme climate change financing, and studies and financial projections that will allow us to prioritize the needs within countries and Regions. The Fund will have a dedicated window or facility or sub-structures to support these specific ‘readiness’ activities, although undertaking readiness activities shall not be a precondition for accessing other GCF resources.
- The Board may establish committees or panels to oversee day-to-day governance of windows.

*Main linkages and implications*

11. The fund design inter-linkages are primarily with the (i) delegation of responsibility for such decision-making to the Board and (ii) whether or not contributors can earmark all or part of their contributions.

12. The implications however are broader, ranging from potentially attracting more funding because of interest from contributors, to spreading the overall funding so thinly that it is difficult to achieve “scale” or “transformation”. The decision could also impact on the ability to achieve balance between adaptation and mitigation if too many windows are established at the outset, but on the other hand could limit private sector participation or other activities relating to the overall objectives or guiding principles. Moreover, they are not all mutually exclusive. Different sets of rules may need to be prepared for each of them. The issue of a committee of experts for guidance can be considered in line with the chosen windows structure and reflected in governance in terms of relation between the Board. Further aspects of the proposed windows and sub-structures of the GCF, their linkages and implications are discussed in chapter IV below.

### **3. Access Modalities**

*Main options presented in submissions were:*

- The Green Climate Fund will make optimal and appropriate use of the full range of means of implementation available. Recipient countries shall be able to access the Fund both directly as well as through accredited multilateral and international partners chosen by them. Both modalities can be used simultaneously.

*Direct Access*

Option 1: Recipient countries will nominate a national implementing entity for accreditation. Once accredited, this entity may then enter into agreements with multiple executing agencies for particular activities.

Option 2: Multiple implementing entities from a recipient country will be able to apply for accreditation.

- Implementing entities may be national, regional, non-governmental or private entities.

*Multilateral/International Access*

- Recipient countries will be able to access the Fund via accredited multilateral and international entities, including UN agencies, Multilateral Development Banks, and International Financial Institutions.
- The Board will manage an accreditation process for entities to access the Green Climate Fund.

*Country Coordination Mechanisms*

- To promote coherence in programming at the national level, developing countries will designate a coordination mechanism. The nature of this mechanism shall be based on national context. It shall:
  - Be responsible for coordination and consultation among all relevant stakeholders at the national level, including vulnerable groups such as women, on the development of GCF funding proposals, including ensuring the coherence of proposals with national climate plans and strategies;
  - Consider and, if appropriate, give a no objection approval to all GCF funding proposals.
- The liability and accountability for activities financed from the Green Climate Fund will rest with implementing entities.

Financial support and capacity development will be provided by the Green Climate Fund for institutional strengthening at the national or regional level

*Main linkages and implications*

13. The linkages are many- beginning with the ability of GCF to be transformative in the way climate finance is delivered by direct access to national entities at scale, but also on design elements such as fiduciary standards, monitoring and evaluation, safeguards and accountability mechanisms, Board responsibilities (including legal status of the GCF), funding criteria, accountability mechanisms, and related legal arrangements and detailed operational guidelines. The direct impact on Secretariat size, the structure of the Fund, and transaction costs and the indirect impact on the attractiveness of the GCF to contributors are potentially significant. The details of different access modalities, in particular direct access modalities, along with their linkages and implications are further discussed in chapter V below.

#### **4. Allocation Processes**

*Main options presented in submissions were:*

- Country Allocations:
  - Option 1: The Green Climate Fund will consider proposals as they are received based on national climate strategies.
  - Option 2: The Board will develop and use criteria for allocating resources among recipient countries;
    - Option 2a: The Board will develop a resource allocation formula
    - Option 2b: The Board will develop an allocation “floor” for SIDS and LDCs and an allocation “ceiling” for all countries.
    - Option 2c: The Board will develop a system of performance-based allocations
  - Option 3: The Board will determine allocation methods within windows that can vary across windows
    - Option 3a: Adaptation resources will be prioritised for developing countries that are particularly vulnerable to the impacts of climate change, including LDCs, SIDS, and African countries.

*Main linkages and implications<sup>2</sup>*

14. The decision will impact the predictability of where GCF resources will flow and the ability to achieve balance of funding for mitigation and adaptation. The decision could also impact on the interest of contributors if it negatively impacts the Board’s ability to ensure that results are rewarded and/or an accountability mechanism for lack of agreed results. Specific additional/cross-cutting windows/facilities like private sector and capacity development, if agreed, will also be affected by the allocation processes. The decision on whether or not there are allocation processes and, if so what the system should look like, is interlinked with a range of other design elements. This includes Board responsibilities, the secretariat functions and transaction costs, and the monitoring and evaluation systems designs.

#### **5. Fiduciary Standards**

*Suggestions from TC members can be summarized as either:*

- (i) Appropriate, high standards are applied consistently at all levels of GCF operations both centrally and at the national, regional and local level;
- (ii) Appropriate standards are adopted that take into account diverse national standards, including conditional accreditation of national implementing entities.

*Linkages and Implications*

15. The decision regarding fiduciary standards will directly impact the criteria to be established regarding the level of access available to implementing entities -both multilateral implementing entities (MIEs) and national implementing entities (NIEs)- to the Fund itself and related legal, monitoring, evaluation, risk management and auditing functions. Similar to the implications of several other “control functions” the decision on fiduciary standards will have implications on risks and will subsequently will impact on the interest of contributors to participate in the Fund. If the Fund requires flexibility on the implementation, an accreditation process that allows the implementing entities to operate with their own operating rules and procedures may be appropriate.

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<sup>2</sup> Further information can be found in Background Note TC-2/WSII/4+TC-2/WSIII/5 on Operational Modalities; and Scoping Paper TC-2 WSIII/2 on Accessing Finance.

## **H. Engagement of the Private Sector**

*Main options presented in submissions were;*

- To achieve its objectives, the Fund will need to mobilise and leverage private sector activity on climate change more effectively and to a greater scale than has been done to date. The Green Climate Fund will therefore aim to maximize the potential amount of private capital that can be leveraged with public financing where appropriate. GCF financing should be utilised to catalyze private sector investment and mobilise national and local private sector actors to as great an extent as possible. Mobilising and leveraging additional private sector finance is a key means of scaling-up climate finance.
- The Green Climate Fund will improve ‘enabling environments’ to promote ongoing private sector activity by assisting the development of the policy and regulatory environments necessary to attract and lower the risks of investing in developing countries, including through capacity building, risk reduction, and concessionary funding.
- Option: the GCF will have a private sector window/arm.

*Main linkages and implications*

16. Most TC members agree that engaging the private sector is a key part of transforming economies; however, there are important implications for the options for how to go about that. Creation of a private sector window or facility, for example, could ensure that supplementary resources are available if a country allocations system is adopted by the GCF. It could also offer specialised financial instruments that are not appropriate for other windows. Such a proposal has important linkages with (i) the windows of the Fund, (ii) as well as approvals processes and (iii) access modalities. Further issues related to the private sector engagement, its institutional linkages and implications are discussed in chapter VI below.

## **I. Monitoring and Evaluation**

### **1. Monitoring**

*In text presented in submissions, there is general agreement that:*

Projects and programs funded by the GCF are be regularly monitored for efficiency and effectiveness in line with rules and procedures that shall be established by the board.

While there is potential convergence on the need for regular monitoring, there is no convergence on where the responsibility for monitoring lies.

Option 1:

The Secretariat shall monitor the efficiency and effectiveness of GCF operations and report regularly to the Board.

Option 2:

The Board or a designated sub-committee of the Board, with support of the Secretariat, monitors the Fund’s portfolio of projects and programs.

Option 3:

The Secretariat, with support from implementing entities, shall monitor efficiency, effectiveness, outputs and outcomes and report to the board.

*Linkages and Implications*

17. This has implications for the roles and functions of the Board and the Secretariat. It may be challenging for the Board, or a designated sub-committee of the Board to monitor all the projects and programs funded by the GCF, if the portfolio grows significantly, while still performing their core Board functions. It might be more efficient for monitoring to be built into core project design and implementation and carried out by implementing entities, with the Secretariat providing oversight functions for the implementation of such monitoring.

## **2. Independent Evaluation**

*In text presented in submissions, there is general agreement that:*

The GCF shall have an independent evaluation mechanism to evaluate the performance of the Fund, including its (i) entities, (ii) programs and projects at all levels, (iii) funding delivery agency/implementing entity, (iv) thematic and project level. There are however differences on the structure/nature of this independent mechanism.

There are proposals that:

- (i) An independent evaluation unit be established as part of the core structure of the GCF;
- (ii) An independent evaluation mechanism that will be wholly or partially contracted to independent external parties;

### *Linkages and Implications*

18. The implications of the arrangements and the scope of independent evaluation are primarily related to the operating costs of the GCF. There is also a question as to how the overall operation of the Board and the GCF will be reviewed periodically (many institutions set up special external, high-level panels for such purposes).

19. There are differences on the roles of the Board and the COP regarding the independent evaluations.

(a) There are proposals that periodic overall performance reviews of the Fund, including its institutions (Board, Trustee, Implementing Entities) are to be conducted by the COP<sup>3</sup> while the Independent Evaluation Unit will report to the Board on matters pertaining to projects and programmes financed by the GCF only.

(b) There are other proposals that the Independent Evaluation Unit should be wholly accountable to the Board.

20. The responsibility of who commissions the Independent Evaluation and who the Independent Evaluation Unit reports to has implications on the relationship of the GCF and its Board to the COP.

## **J. Accountability Mechanisms**

*Main options presented in submissions were:*

Some members have proposed accountability mechanisms to be included in the GCF while others did not mention this design element. It is not clear whether or not a lack of mention implies an option of not having such mechanisms. There were different options proposed for disclosure including:

Option 1: A specific GCF information disclosure policy applied uniformly for GCF-supported activities or

Option 2: Implementing entities use their existing information disclosure policies or establish disclosure policies that are acceptable to the Board.

The suggestions for a Redress Mechanism were either

- (i) A uniform application of a specific GCF policy; or
- (ii) Use of existing mechanisms of MIEs and NIEs if they demonstrate equivalence to GCF mechanism.

### *Linkages and Implications*

21. The decision on whether to have accountability mechanisms and their “reach” will have implications on legal arrangements, the criteria for access by implementing entities, the staffing and costs of the Secretariat, the accountabilities of the Board and related issues.

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<sup>3</sup> Through the review of the Financial Mechanism of the Convention.

22. The lack of accountability mechanisms would affect the risk profile of the GCF and thereby the operationalisation of direct access modality, possible levels of interest and willingness of contributors to participate and consequently the overall amount of funding available as well as sustainability of funding.

23. It is also important to clarify how these mechanisms (information disclosure, redress and integrity) will function knowing that several potential implementing entities already have their own well-established mechanisms which could also be used on GCF funded projects. Moreover, the availability of these is likely to be elements of the fiduciary standards that have been proposed that implementing entities are required to meet.

## **Chapter II            Legal status of the Green Climate Fund**

24. This chapter provides background information on key legal issues related to whether the GCF would or would not have independent legal status. The functions of the GCF and its modalities of operation are the main considerations in order to determine the appropriate legal status of the GCF. The options range from the GCF having no legal status to being conferred legal status under any of the processes described below.

### **A.    GCF has no legal status**

25. The TC could recommend that the GCF should have no legal status. In that case, the GCF would exist and operate on the basis of decision 1/CP.16 and further decision(s) made by the COP on its operating modalities, including its designation as an operating entity of the Financial Mechanism. Under this option, the GCF itself would not have legal capacity to contract and thus would be unable to enter into legally binding agreements, including agreements with contributors to, or implementing entities of, the GCF. In addition, without legal status the GCF liability would not necessarily be limited to the GCF's assets, as would be the case if the GCF had legal personality.

26. In this situation, arrangements for Trustee and independent secretariat services for the GCF would need to be concluded between the COP and the selected institutions for the services to be provided by them for the GCF. Those institutions then would need to enter into any required agreements with contributors to the GCF, as well as its implementing entities. If this option is considered, it would be important for there to be clarity on the responsibilities of the institutions that would enter into contracts on behalf of the GCF. For example, if the interim Trustee or the secretariat were to enter into agreements with implementing entities, what would be the responsibilities of the trustee or secretariat with respect to the use of the funding by the implementing entities? Would the Trustee or the secretariat be expected to monitor the use of the funds by implementing entities? What actions would the trustee or secretariat be expected to take if there were to be fraud or misuse of funds? Would they be expected to exercise discretion or not only at the direction the Board? How does this interplay with the oversight functions of the Board -is there a duality of responsibility?

27. The absence of legal status for the GCF could result in Board members being liable for potential damages to third parties caused by GCF funded programmes/projects. This would be the case if Board members are not entitled to certain privileges and immunities for their participation in the GCF.

28. The advantage of this option would be that it might be faster and simpler to implement than establishing the GCF as a separate legal entity. The disadvantage of this approach is that the GCF would not be able to enter into direct legal agreements with the implementing entities and the GCF and its Board members might be exposed to greater liability and less control than if the GCF were a separate legal entity. In addition, the Trustee and institution providing secretariat services might not be willing to enter into such agreements on behalf of the GCF as they may view such responsibilities as being beyond the scope of the limited responsibilities as Trustee and secretariat. Parties might also be of the view that such responsibilities exceed those envisioned of the trustee and secretariat. That might be particularly applicable in the case of the Trustee, which is expected to have a limited and non-operational role, as provided in the decision 1/CP.16.

### **B.    The GCF has legal status**

29. The TC could recommend for approval by the COP that the GCF should have appropriate legal status. The legal status conferred to the GCF will determine the rights, duties, powers and privileges with which the GCF will be able to operate independently to achieve its purposes and objectives to fulfil its functions. However, this also raises questions as to which elements of legal status are appropriate for the

GCF and how it should obtain this status. The key elements of the legal status include the following:<sup>4</sup> (i) International juridical or legal personality<sup>5</sup>; (ii) legal capacity<sup>6</sup>; and (iii) privileges and immunities<sup>7</sup>.

30. The different means through which the GCF could acquire or be conferred with these elements are as follows:

- (a) New International treaty: negotiated by the COP and ratified by Parties to the UNFCCC;
- (b) A decision of the COP of the UNFCCC;
- (c) A decision of another intergovernmental process;
- (d) A legislative act by the government of one or more Parties.

#### **1. New international treaty**

31. The TC could recommend that the GCF be established as a new international organization/institution through a new treaty or international agreement. This could be a standalone treaty or protocol or the GCF could be included as part of any future legal agreements on climate change under the UNFCCC. Such a treaty could include provisions for the legal status and privileges and immunities of the GCF and its officials, as well as for the GCF to conclude a Headquarters Agreement.

32. A treaty or protocol could be negotiated and adopted by consensus by the COP in accordance with Article 17 of the United Nations Framework Convention on Climate Change, which states that the COP may, at any ordinary session, adopt protocols (including new treaties and agreements) to the Convention. The text of any proposed treaty shall be communicated to the Parties by the secretariat at least six months before such a session.

33. The establishment of the GCF through a treaty would provide uniformity and consistency in its legal status and the privileges and immunities accorded in the jurisdictions of the Parties to the UNFCCC which decide to ratify this treaty. However, the process of negotiation and adoption of such a treaty, the national legislative process for ratification and the entry into force would take time - the estimated minimum time period could be three years.

#### **2. Decision of the COP**

34. The TC could recommend that the GCF could be conferred with international juridical personality through a COP decision. A Party to the UNFCCC would need to take legislative action to give effect to such a decision.

35. However, this approach would not provide for privileges and immunities for the GCF to be extended to other countries, and would expose the GCF and its officials (Board members and secretariat staff) to legal action in countries where the GCF has no enjoy privileges and immunities. To ensure that GCF has

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<sup>4</sup> Further information on the elements of legal status and the options for conferring legal status are contained in the background note prepared for workstream II: Governance and Institutional Arrangements, "Review of the legal status of select international funds and financial institutions" TC-2/WSII/2 dated 29 June 2011.

<sup>5</sup> International juridical or legal personality would provide the GCF inter alia with capacity to enter into agreements with States and other international organizations; and the legal capacity to contract with implementing entities, to borrow and lend money, issue guarantees and make other investments, to employ staff, to acquire property, and to institute legal proceedings in defence of its interests.

<sup>6</sup> Legal capacity would provide to the GCF the capacity to contract with implementing entities, to borrow and lend money, issue guarantees and make other investments, to employ staff, to acquire property, and to institute legal proceedings in defense of its interests.

<sup>7</sup> Privileges and immunities would provide to the GCF and its officials, including Board members and secretariat staff, inter alia immunity from legal claims, arrest, and search and seizure in national jurisdictions/courts for the official activities of the GCF, and the GCF from taxation. It should be noted that this would be functional and not diplomatic privileges and immunities. In return, the GCF is required to provide alternative mechanisms to address claims and disputes brought against the GCF and its officials, such as dispute settlement procedures. In addition, if the GCF is to borrow funds from private lenders, consideration will need to be given as to whether the privileges and immunities of the GCF would apply to the GCF's obligations with respect to such borrowings or whether recourse to national courts should be permitted.

protection against legal claims worldwide for its activities, privileges and immunities would need to be conferred through the national laws and/or international agreement on privileges and immunities in each country where it would operate.

**3. Decision of another intergovernmental process or institution**

36. The TC could recommend for approval by the COP that the COP could invite another intergovernmental process or another institution to confer the requisite legal status and privileges and immunities on the GCF. In so doing, the COP would transfer to that process or institution the decision on the process for conferring the legal status on the GCF. The process for conferring the required legal status on the GCF would therefore depend on the mandate and powers of that intergovernmental process or institution.

**4. Legislative action by the government or governments of one or more Parties**

37. The TC could recommend for approval by the COP that one or more Parties be invited to accord the appropriate legal status to the GCF. Such a decision could define the legal status to be conferred - i.e., international juridical/legal personality, legal capacity, and/or privileges and immunities. Privileges and immunities, in particular, would be required in all countries where the GCF operates to ensure that the GCF and its officials have protection against legal claims. The process and timeline for the conferment of the requisite legal status would then depend on the legislative process of the government of the Party or Parties concerned.

## **Chapter III          Governance and Institutional Arrangements of the Green Climate Fund**

### **A.    Key legal issues concerning governance and institutional arrangements**

38. The legal status of the GCF will have a major impact on the governance and institutional arrangements of the GCF. This section considers a number of key legal issues concerning the governance and institutional arrangements for the GCF with respect to: (i) the arrangements agreed between the COP and the GCF; (ii) the Board; (iii) the secretariat, (iv) financial inputs; (v) transitional arrangements, and (vi) operational modalities, including direct access, the process of monitoring, the redress mechanism and independent evaluation.

#### **1.    Arrangements between the COP and GCF**

39. The establishment of the GCF by the COP is based on the broad powers and authority of the COP to establish new bodies/entities under the Convention. As an entity under the Convention, the GCF is accountable to and functions under the guidance of the COP, the supreme body of the UNFCCC. The COP has the authority within its mandate to designate the GCF as an operating entity of the financial mechanism.

40. For the GCF Board to conclude arrangements with the COP, the GCF would need to be established not by the COP but through a new treaty/international agreement or by another intergovernmental process or institution and have the appropriate international legal personality of its own or drawn from institution hosting the GCF so that it can enter into arrangements with the COP.

#### **2.    The Board**

41. If the GCF has no legal status, it will depend on another institution hosting the Fund for all of its administrative/ secretariat services and operational functions. This would mean that the GCF would not have its own staff but would be staffed by and under the administrative rules and procedures of the host institution. This could limit the ability of the GCF Board to select and appoint the head and other officials of the secretariat.

42. If the GCF has legal status, and is operating as a separate entity, it will have the authority, within its mandate, to determine its operational rules and policies and to adopt its own staff and administrative rules and procedures.

43. The essential rules for the operation of the Board could be contained in the design document or a framework document for the establishment of the Fund. The Board could be mandated to develop additional rules and procedures, including rules on conflict of interest, confidentiality, and a code of conduct for members and alternate members of the Board, and other entities of the GCF.

#### **3.    The secretariat**

44. Decision 1/CP.16 provides that the GCF shall be supported by an independent secretariat. The TC may wish to consider the process for the selecting and/or establishing an independent secretariat, and the administrative arrangements for the initial phase of the GCF - for fund mobilization and administrative support to facilitate establishment and initial Board meetings and the pledging process. The GCF may also choose to contract out the secretariat services to an existing institution.

45. If the TC recommends the establishment of an independent secretariat, two options may be considered for such arrangements. Each of these options for initial administrative arrangements has implications relating to broader GCF management issues; (a) establish an independent secretariat immediately; or (b) establish a transitional secretariat pending final decision on an independent secretariat.

- (a) Establish an independent secretariat with a core management and administrative team.
- This would require early decisions on detailed procedures for establishing an independent secretariat and for hiring the immediately required staff, and on the operational and human resource policies for the secretariat.
  - A host country or institution for the independent secretariat could be endorsed by the COP, based on the recommendation of the TC, and the necessary legal and administrative arrangements for hosting the independent secretariat approved by the COP or the GCF, if the GCF has the appropriate legal status.
  - The terms of reference (TOR) of the core management and administrative team of the independent secretariat would require endorsement as part of COP decision based on a recommendation of the TC; or the GCF Board could be mandated to prepare the TOR for staffing arrangements.

46. This option would ensure that the independent secretariat is established and operational as soon as possible. To ensure that necessary staff is in place as soon as possible, the TC could recommend for an institution to undertake the initial staffing arrangements, as necessary, including the recruitment of the Head of the secretariat and core administrative staff based on the TOR or the secondment of staff from relevant institutions.

(b) Establish a transitional secretariat immediately to support the Green Climate Fund Board, pending final decision on an independent secretariat.

- This option would ensure that arrangements are in place for transitional secretariat support to the GCF Board while further consideration of the independent secretariat continues.
- To ensure that this decision is not further delayed, the TC could recommend that the GCF Board be mandated to take a decision on the independent secretariat.
- The TC could recommend the key TOR for the transitional secretariat, including the key staffing requirement; or could recommend that the GCF Board be mandated to determine the staffing arrangements required for the transitional secretariat
- A host institution for the transitional secretariat could be endorsed by the COP, based on recommendation of the TC, and the necessary legal and administrative arrangements for hosting the transitional secretariat for approval by the COP or the GCF, if the GCF has the appropriate legal status.

47. This option would ensure that transitional arrangements are in place to support the GCF Board, and that the Board is mandated to make the final determination regarding the permanent secretariat.

## **B. Financial Inputs**

48. The legal status of the GCF may affect the types of financial inputs into the GCF. If the GCF does not have a legal status, funding can be provided to the trust fund for the GCF in the form of grants, as is the case for other programs that do not have legal status, like the GEF and the CIFs. From a legal perspective, it would also be possible for there to be capital contributions to the GCF, as is the case for the trust funds for the CIFs, which do not have legal status. From a legal perspective, as in the Clean Technology Fund under the CIFs, the trustee of the GCF trust fund could also enter into loan agreements to accept loans for the trust fund. In such case, the trustee would not have any personal liability under such loan agreements and the loans would be repayable only from the available resources in the trust fund. However, the blending of various types of financial inputs into a trust fund would raise a number of issues that would need to be addressed. First, measures would need to be put in place to ensure that the trust fund would have sufficient resources to make payments on the loans to the trust fund as such payments fall due. Together with any investment income earned on the trust fund resources pending their disbursement, outgoing finance from the trust fund would need to

generate sufficient reflows of principal and interest to repay the loans to the trust fund. Second, a determination would need to be made as to whether grant and capital contributions to the trust fund could be used to repay the loans to the trust fund if the GCF income is inadequate.

49. If the GCF has legal status, then the GCF could enter into loan agreements directly with contributors and potentially could raise funds in the capital markets through bond issuances. In either case, the lenders would need to be satisfied that the GCF would have the resources to repay the borrowings and private lenders would price the loans according to their assessment of the credit risk of the GCF. If the GCF has no legal status, then some other institution (such as the trustee) would need to conclude agreements for all GCF financing instruments. In that case, there would need to be clarity on the responsibility of that institution for the use of funds by the implementing entities and for pursuing repayments due under non-grant instruments and for recovery of misused grant funds. Only net reflows from GCF investments would be available to be used for further GCF programming. If the GCF financial inputs include loans or other investments, reflows would need to be used first to service those loans or investments.

### **C. Transitional arrangements**

50. In order to ensure that the GCF is fully operational, it would require some transitional arrangements. The transitional mechanism may require the conclusion of legal agreements by the COP with the interim trustee and for a transitional secretariat. These arrangements will have financial implications which the COP should address (see section 3. on secretariat above). This period may kick-start some of the work of the GCF, including the pledging process, the accreditation process, the different funding instruments and access channels/modalities offered by the GCF. The GCF Board members and alternate members would need to be appointed as early as possible to provide the necessary guidance during the transitional period.

### **D. Operating Modalities**

51. This section presents the key legal issues related to access modalities, the monitoring processes, redress mechanism and the issue of the independent evaluation unit.

#### **1. Access Modalities**

52. Either national designated authorities or implementing entities are to bear responsibility for the use of GCF funds.

53. If the GCF has legal status, the GCF would be able to enter into agreements with such entities and they would be directly accountable to the GCF for the use of the GCF funds. In that case, decisions would be needed on what role the GCF would have in monitoring the use of GCF funds and how this role would be carried out (directly by the GCF or by other entities contracted by the GCF).

54. If the GCF has no legal status, then, as a legal matter, the national designated authorities or implementing entities would need to enter into agreements with some other institution (such as the trustee) to bear contractual responsibility for the use of the funds. In that case, there would need to be clarity as to the responsibility of that institution for monitoring the use of funds by the national designated authorities or implementing entities and for the actions to be taken if it has been determined that the funds have been misused. The responsibilities of the entities involved in direct access, the functions of the (national designated authorities, implementing entities, the trustee and the secretariat) will need to be clear. This is an important element, since major issues such as liabilities related to the use of funds are the heart of this.

**2. Monitoring**

55. Monitoring may be affected by the GCF's legal status. If compliance with social and environmental standards and achievement of anticipated results are to be monitored, the entity responsible for complying with those standards and achieving results should be contractually obligated to do so.

56. If the GCF has legal status, it would conclude such contracts. In that case, the GCF would also need the operational capacity (either internally or through contractor) to perform such monitoring and to exercise remedies in cases of non-compliance.

57. If the GCF does not have legal status, then some other entity would need to be party to the agreements with GCF recipients and be the entity that would have the legal right to enforce compliance under those agreements. Decisions would be required as to the extent that entity would be responsible for monitoring compliance and how decisions to exercise remedies would be made (e.g., at the direction of the Board).

**3. Redress Mechanism**

58. It has been proposed by some members that there be an independent inspection unit to receive complaints and evaluate the implementation of the GCF's social and environmental safeguards. Decisions would be needed on the jurisdiction of such unit (for example, who would be eligible to submit complaints and what would be the permitted scope of such complaints) and the consequences if the unit determined that there had been non-compliance. Decisions would be needed on the procedures to be followed by the unit and whether there would be an appeal mechanism. The relationship between the GCF unit and inspection units within implementing entities would also need to be clear, for example, should the implementing entity system be exhausted before appeal to the GCF's inspection mechanism. Moreover, a decision would be needed as to whether and how affected people would be compensated.

**4. Independent Evaluation**

59. It has been proposed that the GCF design includes an independent evaluation unit to carry out independent evaluations of the overall performance of the Fund. A decision would be needed as to whether such unit would be entitled to carry out evaluation of the programmes/projects of implementing entities and the process. The relationship between the GCF unit and the evaluation units in implementing entities would need to be clarified.

## **Chapter IV            Green Climate Fund windows and details on their implications**

60. This section outlines options on GCF windows presented by TC members and maps their key implications. The aim of the section is to provide TC members with the relevant information in order to select from and combine different options on windows.

### **A. Purpose**

61. Views of members on the role of windows could be summarized as follows:

- Inputs: Windows could be used as a way to arrange financial inputs coming into the GCF for particular issues and themes. These inputs could be divided either by contributors through earmarking or by the Board.
- Outputs: Windows could be used as a way to deliver finance from the GCF. Particular recipients or group of recipients, financing instruments, or access modalities could be grouped together in delivery windows.
- Management: Windows could be used as structure for the purpose of managing funds i.e. procedures, processes and governance

### **B. Thematic and other windows proposed**

62. The choice of options on windows could have a number of implications for the functioning of the GCF. This section outlines the key implications for each proposed window.

#### **1. Adaptation and Mitigation**

- These two windows could support simpler accounting and ease in accounting of balance between adaptation and mitigation funding.
- Both themes are sufficiently broad to contain many key activities to be funded. This reduces the overall number of windows and prevents fragmentation and division of overall Fund resources.
- These two themes fit most clearly with other elements of the existing climate finance architecture and so could promote strong synergies and complementarity.
- Mitigation window could employ some form of crediting mechanism to incentivize private sector.

#### **2. REDD plus**

- A dedicated window could increase financial inputs from dedicated forestry sources.
- It could allow for development and use of dedicated REDD plus mechanisms that require specific criteria and processes to operate within the Fund.
- It could allow for a sub-committee for dedicated REDD plus stakeholders, such as in the REDD plus Partnership.
- A separate window could reduce synergies with other mitigation activities, including land use.

#### **3. Private Sector**

- A separate window could leverage financial inputs from dedicated sources, such as private sector philanthropic sources.
- It could improve the efficient delivery of dedicated, supplementary funding for private sector activities without drawing finance from national allocations, especially in smaller countries with less developed financial markets like SIDS and LDCs.

- It could also allow for specialised instruments and programme cycles best suited to private sector activities.
- It could allow for a sub-committee that includes private sector stakeholders, which is important for attracting private philanthropic money to the Fund.

**4. Readiness<sup>8</sup>**

- A dedicated window could provide resources in addition to those of mitigation adaptation. As readiness is a preparatory activity, a window could avoid having to use resources from mitigation or adaptation windows.
- It could provide flexibility for reducing the volume of finance needed for preparatory activities over time and even eventually removing the window altogether.
- A separate window could reduce synergies with other activities if not appropriately structured.

**5. SIDS and LDCs**

- A separate window could give simpler access to resources for these countries as well as provide greater visibility to their needs.
- A window for recipient countries in parallel to mitigation and adaptation windows could cause overlap and accounting difficulties between windows.
- It may not increase funding levels over a country allocation system in which these countries are given increased portions within the Fund

**6. Capacity Building and Technology Development and Transfer**

- In practice, it is difficult to disaggregate these activities from mitigation and adaptation. A separate window could cause overlap between windows, which could in turn cause accounting difficulties. A separate window could reduce synergies with other mitigation and adaptation activities.
- A dedicated window does offer dedicated resources for these issues, although this is not necessarily more efficient or effective. Moreover, a window would likely not provide more funding than could be achieved through quotas within the mitigation and adaptation windows.
- Synergies under the proposed windows to support capacity-building and readiness activities could be explored.

**C. Overarching considerations for the proposed windows**

63. Given the implications of the many different window options, a number of key overarching implications may be considered:

(a) More windows could mean smaller windows. Increasing the number of windows could mean that funding will be spread more thinly, possibly affecting the predictability of funding for the windows. This suggests reducing the number of windows where operationally efficient and feasible.

(b) Different issues require different types of arrangements. There is recognition among submissions that the purpose of the funding windows may be different depending on the issue at hand, including:

- (i) ***For cross-cutting issues creating windows could cause a lack of coherence and could complicate accounting.*** Activities such as capacity development/technical assistance and technology development and transfer are often embedded within other themes and

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<sup>8</sup> Such a dedicated window or facility was referred to in submissions. Readiness is used in submissions to refer to preparatory activities such as strengthening national institutional arrangements, rather than technical assistance that is embedded within projects and programmes.

programmes. Their presence could be secured through embedding them within the main thematic windows, including use of specific quotas or earmarking as appropriate.

(ii) **Using windows for country prioritisation could cause an overlap between windows.** Dedicated resources for particularly vulnerable countries, including SIDS and LDCs, are not separate from the thematic issues that the Fund supports. Therefore, a separate window could lead to operational complexities. An alternative approach for maintaining dedicated resources for vulnerable countries could be for the Fund to develop and apply prioritisation criteria or country allocations within or across thematic funding windows.

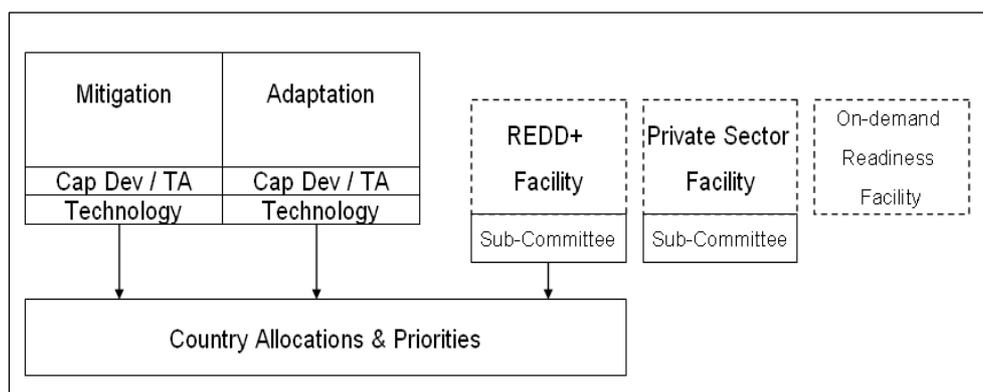
(iii) **Specialised issues require special governance and operational arrangements in addition to adaptation and mitigation windows.** For issues that are preparatory or that may require specific operational and governance systems, more tailored mechanisms alongside the broader windows may be needed, such as dedicated “facilities” within the Fund:

- For the private sector, this could overcome the barrier to raising supplementary funds from non-governmental sources. In addition, such a facility could include specialised governance arrangements that overcome the barrier of private sector engagement but still ensure compliance with the Fund’s overall objectives.
- For REDD plus, this could allow for the development of specific results-based payments systems as well as dedicated governance arrangements for key REDD plus stakeholders.
- For readiness, this could allow for an on-demand system to be used, rather than the country allocations system which could be used for the main thematic windows. In addition, this facility could later be reduced in size relative to the overall GCF and even eventually removed.

(iv) **Particular issues may require special arrangements for financial inputs.** For issues such as private sector or readiness activities, the implications above suggest that resources may be required that are supplementary to overall country allocations, if agreed, for mitigation and adaptation. Using windows or facilities for such activities allows for varied systems for capitalization across issues. For example, financial resources for a private sector window/facility could be accepted after a threshold for overall Fund volume is reached or a ceiling for each contributing country (percentage of overall contribution) is allocated thus ensuring that early resources are for country allocations, if country allocations are agreed. For readiness activities, it is likely that the grant resources will mainly be required and at an early stage. Moreover, demand for such support could vary between countries; an on-demand funding approach could be used financed by a certain percentage of grant inputs to the GCF. This could then be scaled down over time.

64. The various implications and aggregate conclusions of these implications suggests that the GCF may need a variety of mechanisms in order to effectively support the wide variety of themes and issues necessary to address climate change. The figure is an illustration of one possible model.

**Figure 1. Options for windows**



## **Chapter V            Access modalities**

65. An important defining characteristic of the GCF emerging from TC discussions and submissions, consistent with 1/CP.16, is a commitment to strong country ownership and country-led identification, formulation and implementation of policies, programmes, projects and other activities, developed through a process that ensures the involvement of relevant sub-national, national and regional institutions and stakeholders. In particular this focuses on the following:

- Recognition of the capacity and rights of developing countries to identify their own priorities for the allocation of resources;
- Opportunities for strong alignment of GCF support with national and sub-national plans and relevant programmes;
- The potential for a simplified, improved and direct access to funding, assuming there is sufficient accountability;
- Promotion of a balanced partnership between climate financing contributors and recipients; and
- Creating the conditions for strong attention to the concerns of vulnerable and marginalized groups, assuming that the planning processes of multi-stakeholders are followed.

66. Within this agenda, there are a number of key operational characteristics emerging for the GCF as follows:

- Use of appropriate access modalities, including direct access<sup>9</sup> as a key modality to enhance country ownership;
- Balancing of innovations in the way that funds are accessed with appropriate attention drawn to managing the risks of their inefficient or ineffective use; and
- Use of a programmatic rather than project-by-project approach to achieve transformational impact.

67. This section outlines the various options presented by TC members and maps their key implications. The aim is to provide TC members with the relevant background material in order to select from and combine different options on access modalities.

### **A. Options on access modalities**

#### **1. Direct and multilateral/international access**

68. The submissions call for the GCF to make optimal and appropriate use of the full range and means of implementation services and channels available. Though a preference exists for use of direct access where appropriate, other access modalities are also considered important alongside and simultaneously with direct access. Moreover, it is also acknowledged that there would be opportunities for GCF to achieve its goals by supporting activities at the regional or global levels.

69. One key option among the submissions is whether the GCF will utilize both grant and non-grant financing instruments. If the Fund is to offer non-grant instruments, the question is whether the fund itself would be able to act as a financial intermediary (i.e. have banking functions) or whether it would rely on international or national financial entities to perform this function and so convert grant funding from the GCF into concessional loans.

*Key Implications:*

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<sup>9</sup> Direct access is defined herein as access to funding without the involvement of intermediary international implementing entities (such as MDBs, UN agencies or international financial institutions).

- To enter into agreements with national implementing entities, the GCF should have a form of legal personality (see chapter III above)
- The use of multiple implementing arrangements in parallel poses a challenge to coherence in programming and may require coordination point or mechanism at the country or regional level, and
- Regional and global projects/programmes may require alternative processes

## **2. Country coordination mechanisms<sup>10</sup>**

70. A potential point of convergence arising from submissions is for the use of national coordination mechanisms in developing countries to coordinate GCF programming in the context of national climate change action plans and strategies. By definition such mechanisms would need to be broadly representative of national interests and could as appropriate oversee the development and implementation of plans through a multi-stakeholder participatory process as in other large public funds, such as the Global Fund.

71. There are some key questions, however, related to the precise role of national coordination mechanisms. For example, whether there would be one mechanism or mechanisms; what is their role in approval of proposals/submissions to the GCF, what is their role in terms of accreditation, and what is their role in terms of channelling finance (and so liability) and in selecting implementing entities?

72. Two options could arise from these key questions. First, that country coordination mechanisms could be limited only to coordination function. Here they may be required to approve proposals to be submitted to the GCF and even liaise with national and international implementing entities on division of responsibility at the national level. However, in such an option, no finance would channel via these mechanisms. A second option is where the coordination mechanism itself could be accredited to the GCF. It would then be responsible not only for coordination but also for channelling finance to national executing entities or agencies. One potential advantage of this option could be a reduction in accreditation processing at the GCF level as well as increased coherence at the national level.

73. Submissions indicate that the nature of country coordination mechanisms could vary according to country context. They could take the form of inter-ministerial committees, national climate funds, or key line ministries.

### *Key Implications:*

- If coordination mechanisms (CMs) would not be channelling financial resources there be no legal or operational requirement for their accreditation.
- If CMs would be required to approve activities by all implementing entities, this could increase coherence at the country level.
- CMs could require financing for these services. These could be provided either through the proposed readiness facility or through in-programme funding.

## **B. Accreditation, Monitoring and Recourse Issues**

### **1. Accreditation**

- There appears to be potential convergence that the Board would manage an accreditation process for all entities to access the GCF, developing criteria, including fiduciary standards<sup>11</sup>, for the accreditation process.

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<sup>10</sup> Referred to in submissions as “designated GCF national authorities”, “national networks”, “coordination mechanisms”, and “national entities”.

<sup>11</sup> These standards may cover: planning and appraisal standards for climate investments; a functional internal control system, an adequate reporting system, an external audit independent function, a transparent procurement system, a disclosure and information system, an appeal and redress system, an ethics code, including provisions applicable in case of conflict of interests, corruption and fraud.

74. A key question is whether entities would be able to apply independently for accreditation or whether there would be a linkage created with coordination mechanisms, where they would endorse any accreditation applications by national entities.

75. The accreditation process could build on the experience of the Adaptation Fund, the Global Fund and others which have developed similar direct access procedures.<sup>12</sup> The Board could appoint a committee or panel to handle this process. Implementing entities applying for accreditation would be expected to demonstrate to the Board that they could meet the criteria set, including adherence to fiduciary standards. For accreditation of entities under the direct access modality, key steps could include the following:

- Selection of an entity by the coordination mechanism as appropriate to the needs of GCF program delivery;
- Preliminary assessment of the entity by the coordination mechanism regarding its required capacities;
- Nomination of the entity to the GCF Board for accreditation.

*Key Implications:*

- The potential volume of entities applying for accreditation may necessitate a dedicated accreditation panel with delegated authority by the Board to avoid over-burdening Board meeting time,
- The development of accreditation criteria requires a choice as to the level of strictness. Highly rigid standards that would not rely on the systems of implementing entities could significantly slow accreditation processes; however, weaker standards could increase risk. This may require the Board to explore use of tiered accreditation, as is under consideration by the Adaptation Fund.
- Some national entities applying for accreditation may partially satisfy the criteria and could agree to partner with international implementing entities for the provision of certain functions until their capacities meet the necessary standards

## **2. Monitoring and recourse: lessons learned from relevant funds**

76. The Global Fund for AIDS, Malaria and TB and from other funds indicates that post-accreditation monitoring of direct access activities would be required to ensure the integrity of delivery of approved funds and that there be appropriate recourse mechanisms in place in cases of misuse of funds (or default on concessional lending if used).

*Key Implications:*

- The Fund would require a modality for monitoring the use of funds and compliance to its accreditation standards. Depending upon the legal status of the GCF, this could be conducted through a centralised unit within the Secretariat or through appointed in-country auditors, as is the case through Local Fund Agents within the Global Fund. The Fund would also need to have the contractual right and means to pursue recourse in case of misuse.

## **C. Programmatic approval processes**

77. Most developing countries have prepared or are in the process of preparing national climate change action plans, policies or strategies<sup>13</sup>. Some integrate mitigation and adaptation actions, while

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<sup>12</sup> See TC-3/Inf.2: “Experiences and Lessons Learned from Relevant Funds for the Design of the Green Climate Fund”.

<sup>13</sup> In the context of the UNFCCC, these include nationally appropriate mitigation actions (NAMAs) and national adaptation plans (NAPs).

for others these remain separate. Some have been developed through widely representative multi-stakeholder and participatory processes, while others have been prepared by a single ministry or agency on behalf of the government. The types of actions called for in these plans tend to be largely public sector interventions, though many also identify measures to leverage and mobilize the private sector toward achieving its goals. Finally, the quality and depth of economic, climatological and sociological impact assessments and other analytical work upon which these plans are based varies widely.

78. TC submissions recognize the existence of these plans and demonstrate a commitment to strong country ownership in the programming of GCF resources in support of their implementation - respecting country-led identification, formulation and implementation of policies, programmes, projects and other activities receiving GCF support. TC members have called for all relevant institutions and stakeholders to be involved in the programming process, to demonstrate consideration of both public sector options as well as opportunities to leverage the private sector in achieving GCF goals. There is also support for the GCF to provide appropriate technical support and capacity development for the process of developing and enhancing national low-emissions, climate-resilient development strategies, which would then rely upon the GCF to finance all or part of these plans.

79. Suggestions for activities eligible for GCF financing mentioned in TC submissions include technical assistance, demonstration projects, and programmatic activities to mobilize the public and private sectors at national and international levels to achieve GCF goals. Use of a programmatic approach is meant to obtain sufficient scale of action to achieve transformational impacts<sup>14</sup>. This is coupled with efforts to reduce the transactions costs associated with the approval of individual projects, though support for discrete demonstration activities showing that the promise of significant scale-up would be feasible. There are also calls for small-scale activities to be supported by the GCF with highly expedited approval processes. Support for programmes and projects could be coupled with capacity development to build enabling environments that can catalyze both public and private climate finance at scale and achieve transformative impacts.

80. The process of approvals of proposals would require careful consideration. As noted above, the potential range of implementing entities acting in each country presents a challenge to the coherence of GCF programming at the country level. A number submissions note the potential role of country coordination mechanisms as mitigating this risk. Here, such mechanisms would be required to give an approval (or a no objection approval) to all proposals from accredited implementing entities (national and multilateral), thus giving an opportunity to bring coherence at the country level. Proposals could then move to the Board (or its designated windows or sub-structures) for screening and approvals.

*Key implications:*

- If country plans are to be the basis for approval within the GCF, multilateral, international, bilateral, and other supranational entities would need to be engaged in country coordination activities through coordination mechanisms to develop and gain national approval for their proposed activities in the context of these plans,
- National strategies or plans may have financing timeframes that differ from those of the GCF, in terms of its capitalization, and attention may need to be given to the need to align funding cycles,
- Experience from the early years of the Global Fund shows that too stringent a focus on programming can undermine attention to capacity building needed for sustained delivery, and
- Many country plans are medium and long-term; specific sections or time slices (e.g. first 5 years of plan) may therefore be better suited to GCF funding cycles.

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<sup>14</sup> Note the TC is considering the precise nature of transformational change in a workshop to be held immediately prior to TC3.

## **Chapter VI Private Sector**

81. Private capital mobilization and leveraging would be critical in achieving the scale and funding predictability necessary to accomplish the goals of the GCF. There seems to be a convergence among the views of TC members on this issue, but various areas of uncertainty and divergence remain over the specific types of private sector engagement that should be promoted and the best operational modalities that should be employed. Building from TC member views, this section aims to help clarify these issues, providing information on the extent, modalities and implications of private sector leveraging and mobilization through support provided by the GCF.

### **A. Potential private sector involvement in Green Climate Fund activities**

82. There is general consensus that the principal goal of mobilizing the private sector to expand the availability and reach of climate change financing is to maximize the effectiveness of public finance, not to reduce the level of commitment of public funding. Members have highlighted the need for the private sector to engage actively with national and international public and private partners and to avoid crowding out existing national and local private sector investment.

83. Private sector activities can complement public sector initiatives to help countries achieve the goals of climate resilience and low-emission growth. While private sector involvement may sometimes require unique processes and procedures to maximize the potential impact, private sector activities would be embedded into, and subject to the overall policies and governance structures of the GCF.

84. Private sector financing could occur at different levels of GCF operations:

- Private sector investment directly into the GCF (likely to be limited to philanthropic sources);
- Private sector investment into a specific window or facility of the GCF;
- Private sector investment into specific programs/projects (such investments could include financing from co-financiers/sponsors, e.g., from banks, funds, local corporations, developers,, farmers and consumers).

85. In addition to such actions and partners, private sector entities could also be called upon to deliver and execute projects based on fixed revenue procurement contracts (e.g., as contractors or advisors).

86. Private sector investors only commit themselves to operations with an expected return commensurate with the risks taken (including sovereign, counterparty, co-financing, project risks, etc). When risks and expected rewards are unbalanced or too uncertain, the private sector will not invest. However, GCF financing and associated government actions could be used to potentially rebalance the risk/reward profile for investors to the minimum extent needed to mobilize private financing at scale for climate change programs or projects at local, national and international levels.

### **B. Potential benefits of private sector involvement in Green Climate Fund**

87. TC members have noted that where appropriate, the GCF should aim to maximize the potential amount of private capital that can be leveraged with available public financing. Private sector involvement in the GCF could help to achieve:

- Potential for scale, in terms of both financing and implementation;
- Provision of efficient and transparent operational modalities;
- Development of domestic private sector markets;

- Co-benefits such as increased jobs, enhanced technology transfer and economic growth;
- Additional sources of funding to developing countries (carbon market instruments, institutional investors, pension funds, etc.);
- Consistency with the social, environmental and fiduciary standards of the Fund;
- Technical and financial knowledge, networking to engage with both public and private partners, of national and international scope, and an ability to execute investments/programmes rapidly;
- Value for money if properly regulated and monitored.

88. To maximize private capital mobilization, however, would require special attention to the structuring of the GCF and the establishment of its policies and procedures to ensure an alignment of interests. Options for how to maximize private sector benefits while addressing such challenges are outlined below.

### **C. Key aspects for engaging the private sector in Green Climate Fund operations**

89. Engagement of the private sector in GCF operations would have implications on the Fund's structure, policies and procedures. The implications could vary, depending on the level at which the private sector is engaged:

#### **1. Engagement of private capital at each level of GCF operations**

- (a) At the GCF-wide level (if this is to occur):
  - Clear alignment of interests would be required between the GCF and investors (in terms of scope, strategy, size, operational modalities, risk exposure, etc of target investments);
  - Clear contractual agreements would be required between the GCF and the investor;
  - The involvement of private investors in the governance structure of the GCF could probably be required (eg. If a window or sub-structure would be agreed and be responsible for the decisions on private sector projects/programs).
- (b) At the Sub-GCF level (e.g., a public private investment fund financed in part by the GCF): The conditions listed above would need to be met, but only at the sub-fund level. Particular attention would be needed for:
  - Adequate risk / revenue sharing arrangements among all investors, including the GCF;
  - Sufficient flexibility for intermediaries in structuring financial outflows to address barriers (regardless of the form of financing);
  - Efficient and predictable decision and implementation processes and procedures;
  - Effective aggregators of multiple sub-projects (national, regional, global private or public entities);
  - Careful attention to the risk/reward profile of projects to ensure that they are adequate to attract investors (e.g., farmers, small and medium enterprises (SMEs), developers, manufacturing companies, etc.).

#### **2. Institutions eligible to access the Fund**

- Public and private financial intermediaries and funds that can coordinate, implement and supervise multi-project interventions.

**3. Eligible interventions**

- Programmatic approaches (multi-project interventions) with potential for market scale-up;
- Demonstration projects with significant potential to lead to market scale-up;
- Broad market incentive programmes, such as advanced market commitments and feed-in tariffs, to stimulate technology development, transfer and diffusion;
- Technical assistance to support public and private sector capacity building needs, including through educational institutions and other market players;
- Regional and global programmes which can address cross border barriers and/or scale/risk diversification needs of international investors (such programmes which supplement national programmes and attract investments into smaller markets);
- Grant financing for assisting and incentivising private sector interventions in LDCs, given their need for larger subsidies and weak abilities to manage foreign exchange rate risks;
- As GCF funds invested in private sector interventions are non-sovereign (through non-government intermediaries), they do not constitute a debt burden for the government;
- Monitoring and evaluation of regional/global programmes will need to be performed at the GCF/secretariat level.

**4. Governance of private sector proposals**

- Need for special skills to assess potential effectiveness of private sector strategies, policies and proposals (financial structuring, broad sectoral/technology knowledge and experience, etc.).

**D. Options for Green Climate Fund governance to enable private sector leveraging and mobilization**

**1. Option A**

90. If the private sector activities would be organized within a window established as a stand-alone facility with separate private sector policies and governance through a Board panel or committee, following GCF fiduciary standards.

- Sub-option: Could use the same governance as other windows, but ensure access to private sector expertise;
- Sub-option: Could use a dedicated governance structure that includes private sector representation.

*Implications of Option A:*

- A separate window could leverage financial inputs from dedicated non-government sources and attract additional funds from donor countries wishing to specifically target private sector;
- It could improve the efficient delivery of dedicated, supplementary funding for private sector activities without drawing finance from national allocations, especially in smaller countries with less developed financial markets like SIDS and LDCs;
- It could allow for a sub-committee that includes private sector stakeholders, which is important for attracting private philanthropic money to the Fund;
- A separate window could potentially reduce synergies with other activities.

**2. Option B**

91. Private sector activities fall under the overall GCF governance (investment decisions) and policies.

- Sub-option: GCF Board could establish a private sector policy or strategy;
- Sub-option: GCF Board could establish dedicated operational modalities for private sector programmes/projects (for example proposal, review, contracting and oversight processes);
- Sub-option: Private sector input to the Board;
- GCF board could include active private sector observers;
- GCF could establish a private sector advisory committee;
- Focal points could be established in-country to coordinate private sector engagement.

*Implications of Option B:*

- Integrated operations could potentially improve synergies with other windows;
- It could reduce, typically non-government led, private sector initiatives that address the risk/reward imbalance for early investors, a key intervention to unlock private capital at scale (eg. from pension funds, developers, SMEs, farmers...).

**E. Transformational impact through private sector interventions**

92. Transformational impact could be achieved through radical shifts away from business as usual. In adaptation, this means encouraging countries and companies to be proactive instead of reactive to climate impacts; in mitigation this means moving markets towards a low emission growth trajectory. To achieve true transformation of a country's private sector, change must occur at scale (wide spread actions/interventions under a new business as usual scenario).

93. Such a transformation may be induced by many factors including the following:

- (a) Regulatory changes that introduce a "carrot" or "stick" approach for private sector action (for example government subsidies, building standards and/or emissions controls);
- (b) The introduction of game changing highly in-demanded technologies (for example next generation electronics such as in the cell phone industry); and
- (c) Access to information (for example through the Internet). Market growth has always depended on early market entrants who take risks which promise great rewards. Once these early entrants "prove a venture successful", other private sector players enter a market more quickly.

94. GCF could play a role in catalyzing and fast tracking private sector transformation by:

- (a) Supporting government interventions which promote private sector action; and
- (b) Addressing the risk/reward profile of early market entrants and investors to encourage movement into desired sectors.

## **Chapter VII Gender**

95. In its introductory remarks in Decision 1/CP.16 refers to the resolution 10/4 of the United Nations Human Rights Council which recognizes the adverse effects of climate change on segments of the population that are already vulnerable owing inter alia to gender. Furthermore, in Paragraph 7 of the same decision, the COP recognizes that gender equality and the effective participation of women is important for effective action on all aspects of climate change. It reaffirms gender-sensitivity as one aspect to be considered when taking action on adaptation (Paragraph 12). Developing country parties are requested to address, inter alia, gender considerations when developing and implementing their national strategies or action plans (Paragraph 72). Also, in Paragraph 130, it is highlighted that gender aspects shall be taken into account when providing capacity-building support to developing country Parties.

96. At the second meeting of the TC in Tokyo, numerous interventions made by TC members underlined the importance of gender equality as a cross-cutting issue.

### **A. Gender mainstreaming**

97. Climate change will fundamentally affect the way societies and communities sustain their livelihoods. These changes, as well as the direct impacts of climate-related events such as drought or flooding, will have gendered impacts – short- and long- term implications for adaptation<sup>15</sup>. Moreover, climate mitigation will have implications on consumer patterns, require behavioral changes, and will necessitate women and men adapting to technical innovations. Therefore climate change requires gender responsiveness and gender sensitivity when designing and planning strategies and when implementing specific activities.

98. Existing climate financing mechanisms have been able to design specific climate change gender issues in their policy framework and funding guidelines to a limited extent. The GCF has an opportunity to be transformational when developing guidelines on operationalizing a gender responsive climate finance mechanism. In practice this could lead to the development of a ‘gender climate footprint’.

### **B. Options for incorporating the gender dimension in to the design of the Green Climate Fund**

99. Mainstreaming gender could be done at three different levels in the fund design document: firstly, gender equality should be an integral part of the principles of the GCF; secondly, gender balance and gender expertise could be addressed in the governance of the Fund; and thirdly gender responsiveness and sensitivity could be reflected in the operational modalities. If the TC decides to address the subject of mainstreaming gender, it may consider the following options:

100. Inclusion of a specific Principle

‘The GCF will operate in alignment with the guiding principle of gender equity.’

101. Governance

‘The GCF will strive for a balanced gender representation and relevant gender expertise on the GCF Board and in the Secretariat.’

102. Operation modalities

‘When developing funding guidelines, the GCF Board will ensure, inter alia, gender-sensitive and gender responsiveness in accordance with the specificities of the respective window and/or facility.’

‘The GCF will establish a clear framework for measuring and reporting results, including gender indicators as defined in the funding guidelines.’

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<sup>15</sup> Linking Gender issues with climate change impact, internal presentation at UNFCCC, Valerie Aphie Solomon, 2011