VIII. FINANCIAL COOPERATION UNDER THE CONVENTION AND ITS KYOTO PROTOCOL

8.1. INTRODUCTION

673. The Convention and its Protocol foresee financial assistance from developed country Parties to developing country Parties. Developed country Parties (Annex II Parties) shall provide new and additional financial resources to assist developing country Parties implement the Convention (Article 4.3)109 and its Protocol (Article 11). This assistance may be through bilateral or multilateral channels or through a financial mechanism defined in Article 11 of the Convention and referred to in Article 11 of the Kyoto Protocol.

674. Financial assistance through bilateral and multilateral channels is addressed in chapter III. Annex II Parties are to provide details of measures taken to give effect to their commitments under Articles 4.3, 4.4, and 4.5 of the Convention as part of their national communications. Owing to gaps and inconsistencies in reporting approaches in the third and fourth national communications from Annex II Parties, it is difficult to reach specific funding figures. However, it is possible to discover trends. The analysis of bilateral and multilateral funding in this paper therefore corresponds mainly to information relating to ODA.

675. The GEF was assigned as an operating entity of the financial mechanism of the Convention on an on-going basis, subject to review every four years. The financial mechanism is accountable to the COP, which decides on its climate change policies, programme priorities and eligibility criteria for funding, based on advice from the SBI.

676. In addition to the guidance to the financial mechanism, Parties have established two special funds[110]: the Special Climate Change Fund (SCCF) and the Least Developed Countries Fund (LDCF), under the Convention. These two funds are managed by the GEF.

677. The Adaptation Fund, under the Kyoto Protocol, was also established[111] by Parties in order to finance concrete adaptation projects and programmes in developing countries that are Parties to the Kyoto Protocol.

678. Chapter VIII.2 below provides an overview of the funding available under the financial mechanism of the Convention (through the GEF, SCCF and LDCF). Chapter VIII.3 provides an overview of the Adaptation Fund under the Kyoto Protocol.

8.2. FINANCIAL MECHANISM UNDER THE CONVENTION

679. As an operating entity of the financial mechanism of the Convention, the GEF receives guidance from the COP on policy, programme priorities, and eligibility criteria related to the Convention. The COP has provided general guidance with regard to operation of the financial mechanism, and has also provided specific guidance in the following areas:

- Support to national communications of non-Annex I Parties;
- Capacity-building;
- Public awareness and outreach (Article 6 activities);
- Development and transfer of technologies;
- Support for adaptation;
- Support for activities referred to in Article 4, paragraph 8(h) of the Convention;
- Support for mitigation.

680. The GEF has responded to COP guidance through the climate change focal area[112] of the GEF Trust Fund (in support of enabling activities, operational programmes relating to mitigation and the strategic priority on adaptation), the SCCF and the LDCF.

681. Article 11, paragraph 3(d) of the Convention calls for arrangements to determine in a predictable and identifiable manner the amount of funding necessary and available for the implementation of the Convention. In accordance with decision 11/CP.1, "in mobilizing funds, the operating entity or entities should provide all relevant information to developed country Parties and other Parties included in Annex II to the Convention, to assist them to take into full account the need for adequacy and predictability in the flow of funds. The entity or entities entrusted with the operation of the financial mechanism should take full account of the arrangements agreed with the Conference of the Parties, which, inter alia, shall include determination in a predictable and identifiable manner of the amount of funding necessary and available for the implementation of the Convention, as provided for in Article 11.3(d) of the Convention".

682. In accordance with the annex[113] to the memorandum of understanding (MOU) between the COP and the GEF (decision 12/CP.3), "in anticipation of a replenishment of the GEF, the COP will make an assessment of the amount of funds that are necessary to assist developing countries, in accordance with guidance provided by the COP, in fulfilling their commitments under the Convention over the next GEF replenishment cycle, taking into account":

- The information communicated to the COP under Article 12 of the Convention;
- National programmes formulated under Article 4, paragraph 1(b) of the Convention and progress made by Parties in the implementation of such national programmes and towards the achievement of the Convention's objective;
- Information communicated to the COP from the GEF on the number of eligible programmes and projects that were submitted to the GEF, the number that were approved for funding, and the number that were turned down owing to lack of resources;
- The GEF replenishment negotiations should take into account the assessment by the COP.

683. The replenishments of funds in the GEF depend on voluntary contributions from donors. The trust fund contributions follow a pre-defined "basic" burden share (GEF, 2005a). The amount of funding under the GEF after 2010 will depend on negotiations on the fifth replenishment of the GEF (GEF 5). The trustee will probably need to start making arrangements for the fift replenishment in 2008. Negotiations and conclusion of the GEF 5 should occur in 2009.

684. The fourth review of the financial mechanism should start at COP 13 (December 2007) and it is expected that the COP will make an assessment of the amount of funds that are necessary to assist developing countries and provide an input to GEF 5.

[109] Article 4.3 stipulates that developed country Parties shall provide new and additional financial resources to meet the agreed full costs incurred by developing country Parties to prepare national communications and to meet the agreed full incremental costs of implementing measures that are covered by paragraph 4.1 of the Convention. Article 4.4 further stipulates that developed country Parties shall assist particularly vulnerable developing country Parties to meet the costs of adaptation and Article 4.5 stipulates that developed country Parties shall take all practicable steps to promote, facilitate and finance the transfer to, or access to, environmentally sound technologies and know how.

[110] Decision 7/CP.7.

[111] Decisions 10/CP.7 and 28/CMP.1.

[112] The GEF's climate change programme is one of six focal areas managed by the entity, and is the second largest after its biodiversity focal area. Most of the GEF's climate change activities are financed by a trust fund (GEF Trust Fund). The LDCF and SCCF were established by decision 7/CP.7 and are managed by the GEF.

[113] FCCC/CP/1996/9.

8.2.1. GEF TRUST FUND

8.2.1.1. LEVEL OF FUNDING

685. As of July 2007 the GEF had allocated (since its inception)[114] a total of just over USD 3.3 billion to climate change projects from the GEF Trust Fund. Further co-financing in excess of USD 14 billion has been leveraged for these GEF projects, or USD 4.2 per dollar of GEF grant.[115] However, in the last reporting period (from September 2005 to August 2006), this ratio was higher – USD 6.4 per GEF dollar.[116] Six project proposals approved in the recent Work Programme (June 2007) leveraged an exceptionally high amount of co financing, making this ratio USD 21.6 per GEF dollar.

686. The total GEF climate change funding allocations (including enabling activities[117]) and co financing amounts are shown below for the different replenishment periods (TABLE VIII-56).

687. The proposed programming for GEF 4 (for the period 2006 – 2010) climate change activities amounts to USD 990 million. Most of the resources will go to mitigation activities. The balance will be allocated to the remainder of the strategic priority on adaptation (Piloting an Operational Approach to Adaptation or SPA, the Small Grants Programme (SGP), cross-cutting capacity-building activities and support to LDCs and SIDS (GEF, 2006).[119] A revised climate change strategy and climate change programming framework (GEF, 2007) is being discussed currently by the GEF Council and provides for a set of links between the GEF's mission, its strategic approach, priorities, operational programmes and project areas (see more detail in the discussions on the climate change portfolio below).

688. As shown in TABLE VIII-57, GEF funding represented 1.6 per cent of funds from bilateral and multilateral sources for energy projects during the period 1997 – 2005 (Tirpak and Adams, 2007).

689. As noted in CHAPTER IV.4.7.3, even if not focused on climate change, the forestry activities financed through the biodiversity focal areas of the GEF account for an important part of financing of forestry mitigation activities and acts as an important catalyst for additional resources (see TABLE 12-ANNEX V). The focal areas for biodiversity, land degradation and international water are also important catalysts of financing for adaptation, as acknowledged in different sectors analysed in CHAPTER V.

[114] Not all of these funds have been fully disbursed as projects are in various stages of implementation.

[115] GEF/C.31/10, annex 2, "Climate Change Focal Area Strategy and Strategic Programming for GEF-4".

[116] Total allocations were USD 355 million, with leveraged funds more than USD 2.3 billion (FCCC/CP/2006/3).

[117] Excludes project development facility (PDF) grants. A total of USD 14.7 million has been approved for PDF-Bs, for the information gathering necessary to complete full project proposals and the essential supporting documentation.

[118] FCCC/CP/2006/3.

[119] See CHAPTER VIII.2.1.3 for more detail on allocations across sectors.

Table VIII-56. **GEF Trust Fund allocations and co-financing (millions of United States Dollars)**

GEF phase	GEF grant[118]	Co-financing amount
Pilot phase	280.60	2,402.89
GEF 1	507.00	2,322.10
GEF 2	667.20	3,403.40
GEF 3	881.80	4,609.69
GEF 4	990.00	–
From which in 2007	76.35	1,651.82
Total	3,326.60	14,389.90

Source: GEF secretariat (2007).

8.2.1.2. RESOURCE ALLOCATION FRAMEWORK

690. A major element of the GEF 3 replenishment reform agenda was the establishment of a framework for allocation to countries based on global environmental priorities and performance.

691. The resource allocation framework (RAF) was adopted by the GEF Council in September 2005. The RAF is designed to increase the predictability and transparency in the way the GEF allocates resources. The resources each eligible country can expect from the GEF will be specified for the four years of the replenishment period, and initial allocations will be updated in the middle of the replenishment period. The RAF began implementation in GEF 4. Each eligible country can expect to receive a minimum allocation of USD 1 million. The total amount that a country receives from the GEF climate change focal area cannot exceed a ceiling of 15 per cent of the resources available. Two indices, the GEF Benefits Index and the GEF Performance Index, will be used in combination to determine the share of resources that each country is allocated. The GEF Benefits Index measures the potential of a country to generate global environmental benefits,[120] and the GEF Performance Index measures a country's capacity, policies and practices relevant to successful implementation of GEF programmes and projects. The GEF Performance Index relies on World Bank Country Policy and Institutional Assessment data.

692. The RAF does not change the GEF project cycle. Each country still needs to work with a GEF implementing/executing agency to develop and prepare concepts for review, pipeline entry and inclusion in a work programme.

693. China, India and the Russian Federation are likely to receive the most under the RAF formula, followed by Brazil, Mexico and South Africa, followed by a group of countries that includes Argentina, Egypt, Indonesia, Islamic Republic of Iran, Kazakhstan, Malaysia, Pakistan, Romania, Thailand, Turkey, Ukraine and Venezuela (GEF, 2005b). In the past, the GEF tended to provide a higher level of resources to those countries with a greater potential for GHG emission reduction. This trend continues in GEF 4.

694. There will be an independent mid-term review of the RAF to be considered by the GEF Council in November/December 2008.

695. The COP, by its decision 5/CP.11, requested the GEF to include in its regular annual reporting information on the initial application of the RAF in the allocation of resources in the fourth replenishment period and inform the COP as to how the RAF is likely to affect funding available to developing countries for the implementation of their commitments under the Convention.

696. The COP, by its decision 3/CP.12, also requested the GEF to give a detailed report on the resources available to each developing country Party in the initial implementation of the resource allocation framework, including a list of activities funded with these resources during this initial period in the climate change focal area.

[120] For climate change, the global environmental benefit index (GBI) weights the baseline emissions of a country with the carbon intensity adjustment factor. GHG emissions from land-use change and forestry are not included in this calculation.

Table VIII-57. **Multilateral and bilateral funding for energy during the period 1997 – 2005 (millions of United States dollars)**

Type of funding	Total 1997 – 2005	Percentage of Total Multilateral and Bilateral Funding
Bilateral Development Assistance	20,104	31.0
World Bank Group	24,898	38.4
EBRD	5,158	8.0
GEF	1,054	1.6
Asian Development Bank	6,593	10.2
Inter-American Development Bank	6,987	10.8
Total	64,794	100.00

Abbreviation: EBRD = European Bank for Reconstruction and Development
Source: Tirpak and Adams, 2007

8.2.1.3. CLIMATE CHANGE PORTFOLIO

697. The largest share of GEF climate change resources has been assigned to long-term mitigation projects. These were envisaged by the GEF to have "much greater impact because the projects would drive down costs, build capacity, and start to put in place the technologies that can ultimately avoid GHG emissions".[121] A key element of the GEF Trust Fund is its requirement that projects meet agreed incremental costs for delivering global environmental benefits. Climate change mitigation projects fell so far within four operational programmes (OP) approved by the GEF Council:

- Removal of barriers to energy conservation and efficiency (OP5);
- Promotion of the adoption of renewable energy by removing barriers and reducing implementation costs (OP6);
- Reduction of the long-term costs of low-GHG-emitting energy technologies (OP7);
- Promotion of environmentally sustainable transport (OP11).

698. A further programme, integrated ecosystem management (OP12), also encompasses climate change objectives, such as removals by sinks. Most of the GEF climate change funds have been spent on OP5 and OP6 (FIGURE VIII-40). To date, a smaller proportion of the GEF's resources have been allocated to adaptation activities, through the SPA.

699. The GEF Council is revising the GEF focal priorities under the fourth replenishment period. A proposal for focal area strategies and strategic programming for GEF 4 has been prepared by the GEF secretariat and is under consideration. The following priorities for climate change mitigation are proposed in the paper (GEF, 2007a):

- Promoting energy efficiency in residential and commercial buildings;
- Promoting energy efficiency in the industrial sector;
- Promoting market approaches for renewable energy;
- Promoting sustainable energy production from biomass;
- Promoting sustainable innovative systems for urban transport.

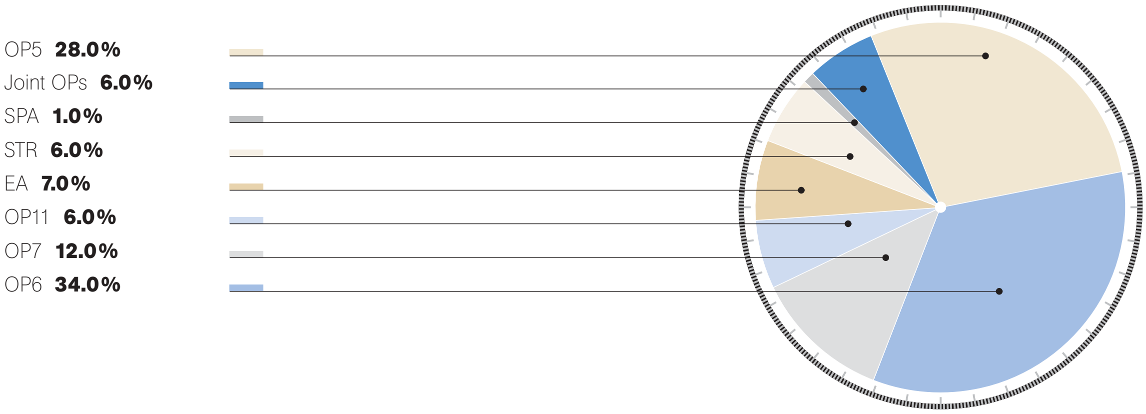
700. The proposal also outlines priorities and issues relating to enabling activities and adaptation. The GEF Council is considering the inclusion of another priority focusing on LULUCF.

701. The largest number of projects has been in the renewable energy portfolio. Although fewer projects have been approved in energy efficiency, these projects have tended to be larger and hence the overall amount allocated for energy efficiency is only slightly less than that allocated for renewable energy. An almost equivalent amount has been allocated for a small number of large projects on solar thermal electricity, power production and fuel cells. Within the energy efficiency portfolio, projects have concentrated on energy efficient buildings, appliances and industry. A relatively new focus has been projects that aim to increase the efficiency of power plants. Within the renewable energy portfolio, there has been a marked shift away from photovoltaic projects (although these have not entirely disappeared) and a greater emphasis on a range of resource and technology options, including biomass, hydropower and wind. Although there are some grid-connected renewable energy projects, most of the portfolio is oriented towards rural energy services. There are fewer isolated, one-off rural interventions, and more emphasis on integrated, sustainable national programmes.

702. FIGURE VIII-40 provides a breakdown of GEF resources allocated to climate change activities by OPs from the pilot phase through the three replenishment periods and including six projects approved under GEF 4 so far (as at June 2007). One third of the resources (USD 861.1 million) has been allocated to support renewable energy (OP6). A comparable amount (USD 719.8 million) has been approved for energy efficiency (OP5). Funding for low GHG-emitting energy technologies (OP7) equalled USD 318.2 million, whereas support for sustainable transport activities (OP11) – a relatively new but rapidly growing operational programme – came to USD 160.6 million. To date, 1 per cent of GEF resources has been allocated to adaptation activities, through the SPA.

703. As for trends, TABLE VIII-58 illustrates that from the pilot phase to GEF-3, the share of the energy efficiency portfolio (OP5) in the GEF climate change focal area saw a steady increase from 25 per cent to nearly 34 per cent. The share of the GEF renewable energy portfolio, including OP6 and OP7, also experienced an increase from less than one third to nearly 47 per cent (OP6 saw a decrease from 39 per cent to 34 per cent, whereas OP7 saw an increase from less than 4 per cent to nearly 13 per cent). Short-term response measures (STRMs) were the only area among all GEF climate change activities that saw a sharp decline in financing over time, from 25 per cent during the pilot phase to less than 1 per cent during GEF 3. Among the first the projects approved for funding under GEF 4 in June 2007, three aim at energy efficiency, one at renewables and two at sustainable transport.

Figure VIII-40. **Allocation of funds available through the Global Environment Facility among its operational programs**



Source: GEF, 2007b.[122]
Abbreviations: EA = Enabling Activity, Joint OPs = Joint operational programmes, OP5 = Removal of Barriers to Energy Efficiency and Energy Conservation, OP6 = Promoting the Adoption of Renewable Energy by Removing Barriers and Reducing Implementation Costs, OP7 = Reducing the Long Term Cost of Low Greenhouse Gas-emitting Energy Technologies, OP11 = Sustainable Transport, SPA = Strategic Priority on Adaptation, STRM = Short Term Response Measures.

Table VIII-58. **Allocation of GEF resources to climate change activities for the period 1991 – 2007 (millions of United States dollars)**[123]

	Pilot phase (1991 to 1994)	GEF 1 (1995 to 1998)	GEF 2 (1999 to 2002)	GEF 3 (2003 to 2006)	GEF 4 (June 2007)	Total
OP 5: Energy efficiency	70.6	128.6	200.1	286.7	33.8	719.8
OP 6: Renewable energy	108.8	191.3	251.8	299.2	10	861.1
OP 7: Low GHG-emitting energy technologies	10.1	98.4	98.6	111.1	–	318.2
OP 11: Sustainable transport			46.4	82.2	32	160.6
Enabling activities	20.2	46.5	45.3	73.9		185.9
Short Term Response Measures	70.8	42.2	25.1	3.7	–	141.8
Strategic pilot approach to adaptation	–	–	–	25	–	25.0
Total	280.5	507	667.3	881.8	75.8	2,412.4

Abbreviation: OP5 = Removal of Barriers to Energy Efficiency and Energy Conservation, OP6 = Promoting the Adoption of Renewable Energy by Removing Barriers and Reducing Implementation Costs, OP7 = Reducing the Long Term Cost of Low Greenhouse Gas-emitting Energy Technologies, OP11 = Sustainable Transport.

[a] As of July 2007, six project proposals have been approved under GEF 4.

[121] FCCC/CP/1995/4.

[122] CCC/CP/2006/3.

[123] FCCC/CP/2006/3.

704. *Enabling activities:* Total funding for enabling activities amounted to USD 186 million. The GEF has provided financing to support 139 non-Annex I Parties in preparing their initial national communications.[124] As of July 2007, About 110 countries received assistance to undertake stocktaking in preparation for their second national communications. The National Communication Support Programme, phase II, is currently assisting 106 countries in preparing their second national communications.

705. *Small grants programme:* According to information provided by the GEF secretariat in July, cumulative funding allocations for the SGP since 1992 have amounted to USD 365.8 million. The ratio of projects for climate change is increasing, starting from 15 per cent in the 1990s to more than 20 per cent currently.

706. *Strategic Priority on Adaptation (SPA):* In response to guidance by the COP,[125] the GEF established the strategic priority "Piloting an Operational Approach to Adaptation (SPA)". An allocation to the pilot of USD 50 million was included in the GEF business plan in November 2003. As of June 2007, eleven projects have been approved with financing from the SPA, totalling USD 28 million. The remaining funds of the pilot programme have been carried over to GEF 4. According to information provided by the GEF secretariat, there are now six projects in the pipeline.[126]

8.2.2. SPECIAL CLIMATE CHANGE FUND

707. The SCCF finances activities, programmes and measures relating to climate change that are complementary to those funded by the resources allocated to the climate change focal area of the GEF and by bilateral and multilateral funding, in the following areas: (a) adaptation, (b) transfer of technologies, (c) energy, transport, industry, agriculture, forestry and waste management; and, (d) activities to assist developing countries whose economies are highly dependent on income generated from the production, processing and export, and/or on consumption of fossil fuels and associated energy-intensive products in diversifying their economies (GEF, 2004).

708. As of June 2007, the original pledges to the SCCF totalled USD 67 million. Of this sum, USD 57 million was pledged for the SCCF Programme for Adaptation and USD 10 million for the SCCF Programme for Transfer of Technology. The total amount available for allocation was USD 43.67 million.[127]

709. To date, eight projects (four medium size projects and four full size projects) have been approved under the SCCF adaptation programme[128]. TABLE 28- and 29-ANNEX V summarizes the approved projects and the projects currently in the pipeline.

8.2.3. LEAST DEVELOPED COUNTRIES FUND

710. The LDCF is designed to support projects addressing the urgent and immediate adaptation needs of the LDCs as identified by their national adaptation plans of action (NAPAs). The LDCF contributes to the enhancement of adaptive capacity to address the adverse effects of climate change, including, as appropriate, in the context of national strategies for sustainable development. The priority sectors that are expected to receive the most attention under the NAPA are water resources, food security and agriculture, health, disaster preparedness and risk management, infrastructure and natural resources management. Community-level adaptation may also be a cross-cutting area of concern (GEF, 2007b).

711. As of 30 June 2007, the LDCF had received USD 160 million in contributions and investment income. Allocations of USD 20.7 million had been made and USD 139.3 million remained available for allocation[129].

712. According to information provided by the GEF Secretariat, to date, 44 out of 49 eligible LDCs have been allocated funds to prepare their NAPAs, as well as for two global support programmes, for a funding total of USD 9.6 million.

713. As of July 2007, there are 6 approved NAPA implementation projects under LDCF. These projects are country driven, presenting a differentiated range of options to address urgent and immediate risks due to adverse impacts of climate change, and demonstrate links between adaptation and development. The six projects in the pipeline are summarized in TABLE 30A-ANNEX V.

8.3. ADAPTATION FUND

714. The Adaptation Fund, under the Kyoto Protocol was established to finance concrete adaptation projects and programmes in developing country Parties that are Parties to the Kyoto Protocol, in particular those that are particularly vulnerable to the adverse effects of climate change. This fund shall function under the guidance of, and be accountable to, the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP).

715. Although initial guidance from the CMP on principles, modalities and some key governance elements for the operationalisation of the Adaptation Fund was agreed upon in December 2006,[130] negotiations on the details for operationalising the Adaptation Fund, in particular institutional arrangements, are currently ongoing.

716. The Adaptation Fund is to be financed with a share of proceeds from CDM project activities and other sources of funding. The share of proceeds amounts to 2 per cent of CERs issued for a CDM project activity, with exemptions for some project types.[131]

717. The level of funding for the Adaptation Fund depends on the quantity of CERs issued and the price of CERs. Assuming annual sales of 300 – 450 million CERs and a market price of USD 24 (range of USD 14 – 34) the Adaptation Fund would receive USD 80 – 300 million per year for 2008 to 2012.

718. Funding for the Adaptation Fund for post-2012 depends on the continuation of the CDM and the level of demand in the carbon market. Assuming a share of proceeds for adaptation of 2 per cent continues to apply post-2012, the level of funding could be USD 100 – 500 million per year in 2030 for low demand by Annex I Parties for credits from non-Annex I Parties and USD 1 to USD 5 billion per year for high demand. The level of CERs issued in the account from the CDM registry for the Adaptation Fund, as of July 2006, is 1,264,201.[132]

[124] FCCC/CP/2006/3.

[125] Decision 6/CP.7.

[126] Information has been received from personal communication with the GEF Secretariat.

[127] Personal communication with the GEF Secretariat.

[128] "LDCF and SCCF Programming Update", in GEF/LDCF.SCCF.2/Inf.3.

[129] Personal communication with the GEF Secretariat.

[130] Decision 5/CMP.2.

[131] Article 12, paragraph 8 of the Kyoto Protocol and decisions 17/CP.7 and 3/CMP.1.

[132] For updated information on the number of CERs issued in the Adaptation Fund account in the CDM registry please see: <http://cdm.int/Issuance/SOPByProjectsTable.html>.