

**The African Development Bank congratulates the Parties on the creation of the Paris Agreement and reaffirms its commitment to work with African Parties to assist them in the achievement of the NDCs and Sustainable Development Goals.**

African Development Bank (AfDB) wishes to submit a suggestion to the Parties to consider the creation of an Adaptation Benefit Mechanism under Article 6.8 as a non-market mechanism to support the implementation of adaptation activities in developing countries. Whilst is not an official position of AfDB, we wish to invite Parties to consider whether such a mechanism could run in parallel to the CDM, and an eventual mitigation market mechanism under Article 6.4 of the Paris Agreement using much of the existing infrastructure. AfDB would like to suggest that the proposal aligns with the concept of a non-market mechanism because, although buyers and sellers are involved, the units transacted would not be commoditized and would not be fungible with one-another or with any compliance obligation. As a result, there may be little or no scope for speculation or secondary trading. AfDB submits this contribution to the Parties in order to stimulate discussion around the possibility of using Adaptation Benefit Units as a financing mechanism for the Paris Agreement.

The purpose of an **Adaptation Benefit Mechanism** would be to create a business model to encourage private sector investment in adaptation. Under an Adaptation Benefit Mechanism (ABM) project developers would change their behavior from business as usual to invest in technologies and services which deliver adaptation benefits to developing countries. The benefits would be quantified, verified, issued and then could be monetized through an **Adaptation Benefit Offtake Agreement**. It is suggested that like Emission Reduction Purchase Agreements, Adaptation Benefit Offtake Agreements (ABOAs) could be bankable and, subject to due diligence, could be used to raise equity or debt to finance the projects.

**What are Adaptation Benefit Units?** ABUs may be non-fungible non-commoditized units which represent the verified results of adaptation projects. Since they are not considered to be fungible, the units in which they may be denominated may be irrelevant. For example, any activity which makes households more resilient to climate induced shocks could constitute an adaptation benefit. Clean cooking stoves, flood prevention and access to electricity all help to make households economically stronger by among other things, improving health, reducing women's workloads, improving access to information, protecting assets etc. ABUs associated with these projects could be denominated in number of households using clean cooking stoves per year; number of villages protected from flooding per decade; and number of houses connected to a grid.

**How are they priced?** ABUs could be priced on the basis of cost of generation plus a profit margin set by the project developer to reflect their own assessment of the risks. These data could be presented in the **ABU Project Design Document** and could be verified by an independent accredited verifier (third party, DOE in CDM terms). ABUs from different projects may have different prices reflecting the costs of technology, the scale of the benefits, the geographical location and the developer's assessment of the risks and expected returns. Over time verifiers may develop databases of the costs in order assess value for money from individual projects.

**Surely buyers will simply buy the cheapest units available?** Not necessarily. Because these units have no compliance value, buyers may buy ABUs based on **the story behind the unit**. Some buyers may

simply like cook-stoves and the benefits associated with them whilst others may believe that flooding of villages and farmlands has a devastating impact upon humans' lives. Some may associate with Africa, other may associate with Pacific Islands or Least Developed Countries. Alternatively buyers may adopt a portfolio approach. What may be more important is the proportion of turnover or profit or GDP which they allocate rather than the number of ABUs they buy.

**Who would buy an ABU and why?** Donors as well as corporate social responsibility buyers, philanthropists and impact investors may buy these units because they may consider that ABUs are a smarter way of distributing climate finance compared to buying emission reductions. Whilst it may seem irrational to buy a unit that has no compliance value, it may be no different from what is happening in the carbon market today. Buyers of Certified Emission Reductions (CERs) and Verified Emission Reductions (VERs) today tend to buy them for voluntary cancellation. Many of those buyers may emit GHGs within an already regulated market and voluntary cancellation may not be counted towards any kind of global target. Furthermore, they may buy them through bespoke tendering processes through which they may pick very specific technologies and project types and they may negotiate a project specific price. So buyers of Emission Reductions today may buy a highly qualified commodity designed for a compliance market but they may treat it as a non-fungible non-compliance voluntary instrument.

In addition, there may be challenges to the environmental and social integrity of transferring emission reductions under the terms of the Paris Agreement which have yet to be resolved, meanwhile many developing countries may be in need of help to cope with changing climate today.

**Why might buying an ABU be a smarter way of distributing climate finance than buying emission reductions?** Unlike the Kyoto Protocol in which only developed countries had emissions reduction commitments, under the Paris Agreement, both developed and developing countries have commitments, as set out in their NDCs, to reduce GHG emissions. This fundamentally changes the incentive structures of a market mechanism for emission reductions, creating a moral hazard in which countries may deliberately lower their mitigation ambition in order to raise funding through the sale of emission reductions. Under the Paris Agreement, when emission reductions are exported from the host country, they must be counted as emissions in the national inventory – this allows them to be subtracted from the emission inventory of the buying country whilst maintaining environmental integrity. Such transfers of emission reductions may make it harder for the host country to achieve its Nationally Determined Contribution because in practice, project developers may harness the cheapest emission reduction opportunities (the low hanging fruit) crowding out opportunities for domestic action. As a result, the transfer of emission reduction units out of the host country may lead to lowered levels of achievement within host countries, encouraging lower levels of ambition. It could also cause developing countries to fail to fulfil their commitments and it may result in higher demands for donor finance to pay for more expensive abatement opportunities. These outcomes may be contrary to the objective of Article 6, which is to raise ambition.

On the other hand, if buyers were to buy Adaptation Benefit Units there would be no moral hazard as the two instruments are not directly linked. Buyers could declare their contribution to adaptation to climate change to their shareholders and stakeholders and host countries may eventually detect the mitigation benefits in their national inventories which will help to achieve their Nationally Determined Contributions, ultimately leading to higher levels of achievement and higher levels of ambition. Under this scenario, international markets may not interfere with domestic policies and critically, climate

finance and private sector finance could flow to the countries with the most compelling adaptation needs rather than to those countries who have the most emitting technologies.

**How would an ABM work?** The ABM could run in parallel to the existing CDM, using the same Modalities and Procedures, under an ABM Executive Board or an extended remit of the CDM EB, with the support of the UNFCCC Secretariat. It could have its own methodologies, project design document template, monitoring reports and definition of additionality. The scope of accreditation of existing Designated Operational Entities (DOEs) could be extended to serve both mechanisms. There could be a registry for projects and for issued and cancelled ABUs but there may be no speculator-driven secondary market in ABUs since they may not be designed as a compliance instrument. The issues of DOE liability and appeals which have challenged the CDM could disappear because the Adaptation Benefit Offtake Agreement would be a commercial agreement between a buyer and a seller with no compliance or environmental obligations. Disputes could be settled using commercial arbitration. To the extent that the CDM may contribute to the establishment of a mitigation market mechanism in the future, the ABU could also operate alongside a new mechanism.

**AfDB wishes to invite Parties to consider whether an Adaptation Benefit Mechanism has a role to play alongside a mitigation market mechanism and that an ABM could be well suited to Africa's development needs as well as those of SIDS and LDCs. Purchasing ABUs could directly help economies and people adjust to changes in the climate which are already happening and will continue under a 2°C and a 1.5°C ambition. At the same time, the purchase could also help countries achieve their Nationally Determined Contributions under the Paris Agreement and encourage them to be more ambitious, in line with the objective of Article 6.**