UNITED
NATIONS

Framework Convention
on Climate Change

Distr.
GENERAL

FCCC/SBI/2008/INF.4
30 May 2008

ENGLISH ONLY

SUBSIDIARY BODY FOR IMPLEMENTATION
Twenty-eighth session
Bonn, 4–13 June 2008

Item 4 of the provisional agenda
Financial mechanism of the Convention: fourth review of the financial mechanism

Synthesis report on submissions from Parties on the review of the financial mechanism

Note by the secretariat

Summary

This document presents a synthesis of nine submissions from Parties relating to: (a) two documents presented at the twenty-seventh session of the Subsidiary Body for Implementation (SBI) – a technical paper reviewing the experience of international funds, multilateral financial institutions and other sources of funding relevant to the current and future investment and financial needs of developing countries, and a report on the assessment of the funding necessary to assist developing countries to meet their commitments relating to the Global Environment Facility (GEF) replenishment cycle; (b) the report on the analysis of existing and potential investment and financial flows relevant to the development of an effective and appropriate international response to climate change, prepared by the secretariat; and (c) options for scaling up the international financial response to climate change, based on national experiences and on available relevant documents. It also provides summaries of the documents presented at SBI 27 and the financial and investment flows report.

GE.08-70442

CONTENTS

I. Introduction

A. Mandate

1. The Conference of the Parties (COP), by its decision 3/CP.4, decided, in accordance with Article 11, paragraph 4, of the Convention, to review the financial mechanism every four years. By its decision 2/CP.12, the COP requested the Subsidiary Body for Implementation (SBI) to initiate the fourth review of the financial mechanism at its twenty-seventh session in accordance with the criteria contained in the guidelines annexed to decision 3/CP.4, or as they may be subsequently amended, and to take appropriate measures and report on the outcome to the COP no later than at its sixteenth session.

2. In response to decision 2/CP.12, the secretariat prepared the following documents for consideration at SBI 27, to facilitate the fourth review of the financial mechanism:

(a) A technical paper reviewing the experience of international funds, multilateral financial institutions and other sources of funding relevant to the current and future investment and financial needs of developing countries (FCCC/TP/2007/4 and Corr.1);

(b) A report on the assessment of the funding necessary to assist developing countries to meet their commitments relating to the Global Environment Facility (GEF) replenishment cycle (FCCC/SBI/2007/21).

3. The COP, by its decision 6/CP.13, invited Parties to submit to the secretariat, by 21 March 2008, their views on the documents mentioned in paragraph 2 above, on the report on the analysis of existing and potential investment and financial flows relevant to the development of an effective and appropriate international response to climate change[1] and on options for scaling up the international financial response to climate change, based on national experiences and on available relevant documents. The COP requested the secretariat to compile the views submitted by Parties and to prepare a synthesis report for consideration by the SBI at its twenty-eighth session.

B. Scope of the report

4. The secretariat based this report on submissions received from nine Parties[2] in response to the request of the COP referred to in paragraph 3 above.

C. Possible action by the Subsidiary Body for Implementation

5. The SBI may wish to take account of information provided in its deliberations on the fourth review of the financial mechanism and in assessing the funding necessary to assist developing countries in fulfilling their commitments under the Convention, for consideration by the GEF in its negotiations on the fifth replenishment of the GEF.

II. Background

6. Under Article 21, paragraph 3, of the Convention the GEF was initially designated to be the international entity entrusted with the operation of the financial mechanism referred to in Article 11 of

---

[1] Dialogue on long-term cooperative action to address climate change by enhancing implementation of the Convention working paper 8. 2007. Available at: <http://unfccc.int/files/cooperation_and_support/financial_mechanism/financial_mechanism_gef/application/pdf/dialogue_working_paper_8.pdf>.

[2] Brazil, Indonesia, Japan, Nigeria, Philippines, Slovenia on behalf of the European Community and its member States, Uruguay, Uzbekistan and United States of America.

the Convention, on an interim basis (decision 9/CP.1). A memorandum of understanding (MOU) between the COP and the Council of the GEF (decision 12/CP.2) and its annex on the determination of funding necessary and available for the implementation of the Convention (decision 13/CP.2) were adopted at COP 2.

7. The COP, having completed the first review of the financial mechanism, decided that the restructured GEF shall be an operating entity of the financial mechanism of the Convention subject to review every four years (decision 3/CP.4).

8. As a result of the second review of the financial mechanism, the COP at its eighth session requested the GEF:

(a) To review, in cooperation with the implementing and executing agencies as well as national focal points, its project cycle, with a view to making it simpler and more efficient, taking into account the lessons learned and the findings of the GEF Monitoring and Evaluation Unit;

(b) To continue its efforts to increase the administrative efficiency and cost-effectiveness of its operations in line with the recommendations of the Second Overall Performance Study of the GEF (OPS 2)[3] and the Beijing Declaration;[4]

(c) To continue to make the concept of agreed incremental costs and global benefits more understandable, recognizing that the process for determining incremental costs should be transparent, flexible and pragmatic, consistent with the Beijing Declaration;

(d) To strengthen efforts to promote consistency of GEF activities with national priorities and to integrate them into national planning frameworks, such as national sustainable development strategies and poverty reduction strategies.

9. The COP also requested the GEF to report on how it responded to the recommendations of OPS 2, on how it considered the recommendations of the second review and on the outcome of the dialogue on long-term cooperative action to address climate change by enhancing implementation of the Convention (the Dialogue) in order to implement more effectively the guidance provided by the COP to the GEF. The COP further requested the secretariat to prepare, for consideration at SBI 20, a report on the determination of funding necessary and available for the implementation of the Convention.

10. The COP, at its tenth session, considered the report[5] and decided that it should constitute an input of the COP to the fourth replenishment negotiations of the GEF Trust Fund. The COP also requested the secretariat to compile information relevant to address future investment needs of developing countries for the purposes of fulfilling their commitments under the Convention. A report was prepared for consideration at SBI 23.[6]

11. At SBI 23, Parties agreed[7] to use the two reports mentioned in paragraph 10 above as inputs to the third review of the financial mechanism. The third review of the financial mechanism was initiated at SBI 21 in accordance with the guidelines annexed to decision 3/CP.4 and the SBI agreed to take appropriate measures and report on the outcome to the COP at its twelfth session.

---

[3] "The first decade of the GEF – Second Overall Performance Study". GEF.2002.
[4] "Beijing declaration of the second GEF Assembly". GEF.2002.
[5] FCCC/SBI/2004/18.
[6] FCCC/SBI/2005/INF.7.
[7] FCCC/SBI/2005/23, paragraphs 56 and 57.

12. The COP, at its twelfth session, requested the GEF to respond to the recommendations of the third overall performance study of the GEF and to report on how it has taken into consideration the recommendations of the third review of the financial mechanism. The COP also decided that the fourth review of the financial mechanism should assess and review the GEF funding for mitigation and its response to the adaptation needs of developing countries in accordance with the guidance by the COP.

III. Synthesis of submissions

A. Fourth review of the financial mechanism

13. Some Parties indicated that the fourth review of the financial mechanism is closely linked with the discussions on finance and investments taking place in the context of the Ad Hoc Working Group on Long-term Cooperative Action under the Convention (AWG-LCA). Thus, outcomes of the discussions relating to the fourth review of the financial mechanism will serve as useful contributions to the AWG-LCA process.

14. One group of Parties outlined the requirements for addressing finance and investment, which include scaling up and mobilizing the financial and investment flows required, developing effective ways to allocate and access the resources, and stimulating the redirecting of particular types of present and future flows – especially those from the private sector – towards low-carbon technologies and investments and measures that reduce vulnerability and increase the resilience of countries, livelihoods and ecosystems.

15. One Party proposed that the COP should review the outstanding issues of the financial mechanism, identify policies and strategies and develop options for a new financial mechanism of the Convention and on how to access funds outside the Convention. The review should explore the methods of innovative financing and ways to increase the present level of funding available and to improve access to these funds.

16. Some Parties noted the important role that the Convention will continue to play in supporting the implementation of programmes and measures to address climate change through the provision of a framework of action, incentives and the financial mechanism. One group of Parties proposed that the fourth review of the financial mechanism should be used to assess how to improve the mechanism, including the administrative procedures and collaboration between GEF implementing agencies. In addition, the following should be examined: the effectiveness of the GEF in contributing to the efforts of Parties to address climate change and in scaling up efforts in relation to a post-2012 agreement; how the work of the GEF complements current and future financing instruments; and the role of the GEF as a catalyst for low-carbon and climate-resilient finance and private-sector investments.

17. Another Party proposed that the fourth review of the financial mechanism should take into account progress made by the GEF in responding to decision 4/CP.13 and the performance of the GEF in responding to the guidance by Parties relating to financial support for the preparation of national communications of Parties not included in Annex I to the Convention (non-Annex I Parties), particularly in relation to decision 8/CP.11.

18. A group of Parties noted that other processes under the Convention, such as the analysis by the Expert Group on Technology Transfer of financial resources to support technology transfer, the GEF strategic programme on technology transfer and the reviews of the framework for capacity-building in developing countries, as well as further considerations on the functioning of the Least Developed Countries Fund (LDCF) in accordance with decision 3/CP.11, may provide useful information to the fourth review of the financial mechanism.

B. Views relating to the experience of international funds, multilateral financial institutions and other sources of funding relevant to the current and future investment and financial needs of developing countries

1. Background

19. The technical paper on the review of the experience of international funds, multilateral financial institutions and other sources of funding relevant to the current and future investment and financial needs of developing countries (FCCC/TP/2007/4 and Corr.1) provides an overview of the practices of multilateral development banks (MDBs) in supporting climate-relevant sectors. Among them the World Bank has the largest resources, providing loans and grants of almost the same amount as that provided by the Asian Development Bank, the African Development Bank, the European Bank for Reconstruction and Development (EBRD) and the Inter-American Development Bank combined.

20. The aim of the MDBs is to facilitate social and economic progress in their member countries. In the period 1995–2005, most of their investment went to infrastructure projects in sectors such as energy, transport, agriculture, forestry and fisheries, and to policy reform activities, all of which are closely related to addressing climate change. Total lending by the MDBs relevant to mitigation amounted to about USD 127 billion over the period 1995–2005; lending relevant to adaptation amounted to about USD 204 billion over the same period. The contribution made by official development assistance (ODA) in supporting the mitigation effort in developing countries is also substantial and in many cases is directed to countries that are not receiving much private investment.

21. All the MDBs analysed recognize the importance of supporting mitigation of, and adaptation to, climate change. The joint efforts by MDBs on the Clean Energy and Development Investment Framework should help to develop a more comprehensive strategy to address climate change within each MDB. With regard to adaptation**,** the greater part of relevant lending by the MDBs goes to long-term infrastructure projects that are likely to be adversely affected by climate change. Only a small portion of lending relevant to adaptation is used directly by adaptation projects. Most of the programmes and projects on adaptation so far have focused on analytical work, capacity-building and impact assessments. The work of the MDBs in climate change adaptation is mostly at the pilot stage. There has been an increase in MDB assistance for disaster relief, reconstruction and emergency response.

22. The multilateral and bilateral public funding sources, although small in comparison to private financial flows, continue to provide crucial external financing for developing countries, typically being used by governments to finance economic and social infrastructure. The MDBs could play a key role in mainstreaming, optimizing and mobilizing adequate resources from public and private sources to support climate-resilient and low-carbon investments in developing countries. They have also started various adaptation initiatives to assess vulnerability and to include climate change programmes in the assistance strategies of their member countries.

23. Given the data gaps and the inconsistencies identified in the time-series analysis of MDB lending, further research could be undertaken to extend the scope of this compilation to cover more institutions and to identify within the climate-relevant investments the direction, positive or negative, and the magnitude of their effect on climate mitigation and adaptation.

2. Views from Parties

24. One Party noted the increasing role that MDBs play in supporting efforts by developing countries to address climate change, such as the assistance provided by the EBRD to the private sector in these countries through renewable energy and energy efficiency projects in the form of carbon financing, renewable energy funds and funding through energy service companies.

25. Some Parties noted that most of the investments go to mitigation-related projects and programmes and that projects on adaptation have so far focused on analytical work, capacity-building and impact assessments, but with little attention being given to practical implementation of adaptation measures. International funds, multilateral financial institutions and other sources of funding must be ready and adequately equipped to assist developing countries, in particular least developed countries, in their current and future efforts to address climate change.

26. Multilateral financial institutions will also play an important role in catalysing greater international and domestic private-sector involvement, in enhancing enabling environments and in strengthening the capacities of developing countries to cope with the impacts of climate change in order to enable them to use market-based instruments and other financial instruments and sources and to promote the introduction of low-carbon technologies. One Party noted that the multilateral fund currently being discussed by some Parties included in Annex I to the Convention (Annex I Parties) and the World Bank would have a considerable effect on mitigation and adaptation measures.

27. One group of Parties welcomed the efforts of the MDBs to integrate climate change across their portfolios and to increase the priority given to energy efficiency and renewable energy as a starting point. The integration of adaptation and mitigation measures into development strategies implies adoption of a low-carbon, climate-resilient development path. In this vein, these Parties encouraged all countries to integrate climate change into their overall national strategies at an early stage as action later will be more expensive.

28. One Party suggested that multilateral and regional financial institutions should consider and use the outcomes and information available to the Convention, such as national communications, national adaptation programmes of action (NAPAs) and technology needs assessments, in financing programmes and projects on adaptation and mitigation.

29. One Party noted that loans can be considered part of the financial mechanism of the Convention only if they are concessional and respond to guidance by the COP. It proposed that the secretariat should collect information from multilateral and regional financial institutions on activities implemented under Articles 4, paragraph 1, and 12 of the Convention and examine who determines, and using what criteria, whether these activities are relevant to climate change. It also proposed an assessment of whether these activities support the implementation by developing countries of commitments under Article 4, paragraph 1, of the Convention and whether conditions for the financial support were given. It further proposed to an assessment of whether new forms of conditionalities were introduced and whether they are consistent with policies, programme priorities, eligibility criteria and decisions of the COP.

30. One Party proposed that coordination between multilateral funds and the various bilateral initiatives for climate change be improved to make the most effective use of limited financial resources.

C. Views relating to the assessment of the funding necessary to assist developing countries in meeting their commitments under the Convention

1. Background

31. The report on the assessment of the funding necessary to assist developing countries in meeting their commitments relating to the GEF replenishment cycle (FCCC/SBI/2007/21) presents an overview of the evolution of the GEF Trust Fund from its pilot phase to its most recent replenishment period and of the different climate change funds managed by the GEF. It also presents a brief assessment of the current and necessary funding to assist developing countries in implementing adaptation, mitigation, development and transfer of technologies, capacity-building, enabling activities, public awareness and outreach, and activities referred to in Article 4, paragraph 8(h), of the Convention. This paper should be considered in conjunction with the Dialogue working paper referred to in paragraph 3 above.

32. As at September 2007, the GEF had raised more than USD 3.3 billion for the climate change focal area for the different replenishment periods. Projects financed with GEF grants are typically co-financed by other sources and over USD 14 billion has been leveraged for these GEF projects. Replenishments of the GEF depend on voluntary contributions from donors, which follow a predefined basic burden-sharing framework. The proposed programming for the fourth replenishment of the GEF (GEF 4) climate change activities targets USD 990 million in allocations. The amount of funding under the GEF after 2010 will depend on negotiations on GEF 5.

33. The LDCF and the Special Climate Change Fund (SCCF) are also voluntary funds but are managed separately and have different arrangements for replenishment from those of the GEF Trust Fund. The role of the financial mechanism as a source of funding has been mainly as a catalyst for leveraging finance and investments to adaptation and mitigation activities. Under its current reform, the GEF has been focusing on the creation of enabling environments, testing new and innovative approaches and facilitating private investments, including those with components relevant to the carbon market.

34. While private sources of funding can be expected to cover a portion of the additional mitigation and adaptation costs in some sectors, additional external public financial support will be needed. If the funding available under the financial mechanism of the Convention remains at its current level and continues to rely mainly on voluntary contributions, it will not be sufficient to address the future financial flows needed for mitigation and adaptation. The funding projected to be available to the Adaptation Fund will not be sufficient to fill the gap; it is likely that new sources of funding will be required. The Adaptation Fund may have the potential to cover part of the needs for financial flows for adaptation, but it would not be sufficient.

35. While considering the level of funding needed to support developing countries in meeting their commitments under the Convention, the COP may wish to consider priority areas for funding under GEF 5 and practical ways for scaling up the level of resources and making the most efficient use of available resources under the financial mechanism. The GEF may wish to consider the complementarities and potential overlap between various funds for adaptation in view of the three adaptation funding windows that are currently operational under the GEF and the Adaptation Fund. Overlap also exists in GEF support for mitigation activities, for development and transfer of technologies and for activities addressing impacts of response measures under the GEF Trust Fund and the SCCF. Ways to improve the complementarity of the financial mechanism with other sources of investment and financial flows for mitigation and adaptation to climate change could also be considered.

36. Other issues that may be highlighted as part of the review of the financial mechanism and for possible appraisal by the GEF could include:

(a) Progress made in strengthening the GEF adaptation portfolio in view of growing needs for adaptation support expressed by Parties, and progress made in fully adhering to GEF guidance on this issue;

(b) The impact of the new focal area strategies on leveraging private-sector investment to address adaptation and mitigation needs of non-Annex I Parties;

(c) The effectiveness and sustainability of different approaches and efforts to support technology development and transfer, capacity-building, and public awareness and outreach;

(d) Efforts towards programmatic and sectoral approaches by the GEF, in particular the relationship in practice of programmatic and sectoral approaches to country needs and priorities and the effects that these approaches could have on the effectiveness and efficiency of the operation of the financial mechanism;

(e) Impacts of the Resource Allocation Framework (RAF) on the prioritization of and synergy between actions at the national and regional levels (including synergy with the national communication processes);

(f) Progress made in the implementation of reforms of operational matters and how the financial mechanism has responded to gaps and to criticisms voiced in OPS 3 and by Parties.

2. Views from Parties

37. One group of Parties considered the important contribution made by the GEF, as an operating entity of the financial mechanism of the Convention, to achieving the overall objective of the Convention by supporting Parties in implementing programmes and measures that will address climate change and transforming the market towards low-greenhouse-gas-emitting technologies. These Parties also noted the importance of achieving greater mainstreaming of GEF activities into national planning frameworks to bring policy change in its areas of intervention. Three Parties also supported the reform agenda of the GEF to improve its operation, and acknowledged the progress made in such areas as the project cycle and consultations with recipient countries and the need to continue to move forward on this reform agenda. Two Parties noted the ability of the GEF to catalyse finance and investments for adaptation and mitigation activities through co-financing the GEF grants.

38. Four Parties noted the difficulties they encountered in accessing GEF funds, such as the imposition of conditionalities and the lengthy procedures in the project approval process. Three Parties also noted that funding available in the climate change focal area of the GEF is inadequate to enable developing countries to undertake action to achieve the objective of the Convention. The SCCF has failed to fund the action plans of developing countries, particularly on adaptation, as it is oversubscribed. Most priority adaptation activities identified under the NAPAs have not been translated into actual projects for financial support under the LDCF.

39. One Party noted that mitigation projects take the largest share of resources from the GEF Trust Fund. Adaptation, which is part of the commitments of Parties to the Convention, is essential to developing countries if they are to cope with the impacts of climate change and develop climate resilient economies.

40. Three Parties noted that according to Article 4, paragraph 3, of the Convention, developed country Parties and other developed Parties included in Annex II to the Convention (Annex II Parties) shall provide new and additional financial resources to meet the agreed full costs incurred by developing country Parties in preparing national communications. One Party also noted the provision in decision 8/CP.11 that Parties should apply for financing of their subsequent national communications at any time between three and five years of the initial disbursement of funds to prepare national communications. The GEF must therefore present a clear funding strategy for subsequent national communications and ensure that measures are in place to allow non-Annex I Parties to prepare project proposals for subsequent national communications in order to avoid discontinuity in project financing.

41. One Party expressed support for the RAF as it ensures a performance-based efficient approach to fund management. However, it noted that it was too early to fully judge the efficiency of the system, and four other Parties expressed concern that its implementation will negatively affect the preparation of national communications by non-Annex I Parties because of competition for allocation of funds for projects.

42. Some Parties proposed that contributions by donors to the climate change focal area in the GEF, to the SCCF and to the LDCF should be increased, citing the provision of Article 4, paragraph 3, of the Convention that requires developed country Parties and Annex II Parties to provide “such financial

resources, including the transfer of technology, needed by the developing country Parties to meet the agreed full incremental costs" of implementing Article 4, paragraph 1, in particular Article 4, paragraph 1(e). These funds must be new and additional and not diverted ODA funds.

43. One Party noted that the fourth review of the financial mechanism should consider eliminating co-financing to ensure accessibility to funds for mitigation projects, but another Party highly commended the GEF for its co-financing requirement and the mobilization of external funding, and recommended that the requirement be maintained. Another Party proposed that the review should assess whether co-financing is tied up with loans and how many of the GEF projects are linked with loans from multilateral or regional financing institutions because of the requirement for co-financing. The same Party also proposed that the review should examine how loans affect a country's ability to pursue its development plans, and how the requirements of co-financing affect the ability of developing countries, especially least developed countries, to access GEF funds. It further proposed that the review should examine how much of counterpart funds from host countries are used to meet the co-financing requirements of the GEF and what proportion of GEF leveraged funds are co-financing funds.

44. Some Parties proposed that the preparation of national communications by non-Annex I Parties should be excluded from the RAF to ensure that funds are allocated on an agreed full-cost basis to implement Article 12, paragraph 1, of the Convention.

45. Another Party suggested that the GEF should comply with the decisions of the COP, particularly in improving the project approval process, to ensure effective access to funds for, inter alia, the preparation of national communications. The GEF should also consider a differentiated approach in allocating resources, such as for national communications. The same Party also recommended that the GEF guidelines and expedited procedures for the Strategic Priority on Adaptation be improved, to better support developing countries in their adaptation activities.

46. One Party noted that any assessment of funding necessary and available for the implementation of the Convention should cover details of the amount of available funds, including the counterpart funds that countries have to raise to access the GEF funds. The same Party proposed that the GEF, in its report to the COP, should provide details of how information provided by Parties was taken into account in the GEF replenishment negotiations, as stated in paragraph 2 of the annex to the MOU between the COP and the Council of the GEF (FCCC/CP/1996/9, annex, page 7, as adopted by decision 12/CP.3).

D. Views relating to the analysis of existing and potential investment and financial flows relevant to the development of an effective and appropriate international response to climate change

1. Background

47. Parties used the Dialogue working paper referred to in paragraph 3 above as input to the deliberations on the fourth review of the financial mechanism when it was launched at COP 13. The report underlines that the additional estimated amount of investment and financial flows needed in 2030 to address climate change is large compared with the funding currently available under the Convention and its Kyoto Protocol, but is only a small proportion of estimated global gross domestic product (0.3–0.5 per cent) or global investment (1.1–1.7 per cent) in 2030.

48. It is estimated that global additional investment and financial flows of USD 200 to 210 billion will be necessary in 2030 to reduce global greenhouse gas (GHG) emissions to 25 per cent below 2000 level. While investment flows in non-Annex I Parties are estimated at about 46 per cent of the total needed in 2030, the emission reductions achieved by the countries amount to 68 per cent of global emission reductions, making mitigation in non-Annex I Parties particularly cost-effective. The investment involves the energy, industry, building, waste, agriculture and forestry sectors. The analysis also presents clearly that a large amount of new and additional investment and financial flows will be

needed to address climate change adaptation needs in 2030 with an order of magnitude of several tens of billions of United States dollars.

49. When considering means to enhance investment and financial flows to address climate change in the future, it is important to focus on the role of private-sector investments as they currently constitute the largest share of investment and financial flows (86 per cent). Although ODA funds are currently less than 1 per cent of investment globally, they represent a larger share of the total investments in some countries, such as least developed countries (6 per cent). Particular attention will need to be given to developing countries, because although they currently account for only 20–25 per cent of global investments, their expected rapid economic growth means that they will require a large share of investment and financial flows.

50. Creating a secure future vis-à-vis climate change will require shifts in investment patterns in a range of sectors, in addition to the need for scaling up funding and optimizing the allocation of existing funds. With appropriate policies and/or incentives, a substantial part of the additional investment and financial flows needed could be covered by the currently available sources. However, improvement in, and an optimal combination of, mechanisms, such as the carbon markets, the financial mechanism of the Convention, ODA, national policies and, in some cases, new and additional resources, will be needed to mobilize the investment and financial flows necessary to address climate change. The carbon market, which is already playing an important role in shifting private investment flows, would have to be greatly expanded to address needs for additional investment and financial flows.

2. Views from Parties

51. Some Parties noted the key message in the financial and investment flows paper of the need to considerably increase and redirect investments toward low-carbon economies to address short- and long-term challenges of climate change. Private-sector engagement will be crucial in responding to the bulk of investments, because resources within the Convention process are limited.

52. One Party pointed out that climate-friendly investment is considered key to enhancing implementation of the Convention, and is appropriately a core topic in the discussion of a post-2012 agreement on climate change. Just as different countries have different circumstances with respect to mitigation, so different countries will have different approaches to funding, and the discussion should cover a range of useful actions and avenues. The same Party stressed that any discussion relating to financing must begin with a discussion of the measures that countries can take domestically to promote investment in clean technologies, and must explore actions that are in line with sustainable development policies and measures. There are many examples of actions that can be taken to reduce costs of investment that would contribute to countries' sustainable development; the reduction of tariffs and investment risk reduction tools such as loan guarantees are two examples. The Party also noted that capital flows now emanate not just from North to South but from all parts of the globe

53. Three Parties noted that improving enabling environments, including governance, is critical to attracting private-sector investments. The public sector will also play an important role in mobilizing external funding, in formulating policy framework, and in promoting the introduction of low carbon technology.

54. One Party noted that, as developing countries increasingly experience the impacts of climate change, developed country Parties should take a lead in addressing climate change and support the efforts of developing countries to achieve the objective of the Convention while meeting their sustainable development needs.

55. One group of Parties proposed that the secretariat update its paper on investment and financial flows and elaborate a more ambitious emission reduction scenario that, in 2030, would bring global GHG emissions back to 1990 levels.

56. Another Party proposed that information of assistance to less developed countries by countries outside the Organisation for Economic Co-operation and Development should be brought forward and examined. The same Party also proposed that in planning further work, consideration should be given, inter alia, to success stories and lessons learned in improving developing country enabling environments for clean energy technology investments; to domestic savings in major emerging economies and other developing countries; to success stories, barriers and incentives for its mobilization for clean energy technology investment; to mobilization of foreign direct investment in clean energy technologies; and to patterns of foreign direct investments.

57. One Party suggested that coordination between multilateral funds and various bilateral initiatives should be improved to make the most effective use of limited financial resources.

E. Views relating to options for scaling up the international financial response to climate change

1. Background

58. The report referred to in paragraph 3 above recognized that substantial additional funding will be required to support effective action aimed at adaptation. Discussions under the Dialogue highlighted the need to identify new and innovative sources of funding and the need for existing funding to be used most effectively. The report also underlined the importance of domestic policies, expansion of carbon markets, increase in ODA and concessional financing for mitigation action by developing countries. The workshop on investment and financial flows to address climate change, organized by the secretariat on 31 October 2007, also examined various proposals made over the past few years to facilitate the scaling up and the better allocation of available resources for climate change mitigation and adaptation.

59. The Bali Action Plan (decision 1/CP.13) called for enhanced action on the provision of financial resources and investment to support action on mitigation, adaptation and technology cooperation, including consideration of improved access to adequate, predictable and sustainable financial resources and financial and technical support, and on the provision of new and additional resources, including official and concessional funding for developing country Parties. If the funding available under the financial mechanism of the Convention remains at its current level and continues to be provided mainly by voluntary contributions, it will not be sufficient to address the future financial flows estimated to be needed for mitigation and adaptation. Several other options for generating additional funds have been suggested, such as the expansion of the carbon market and the auction of allowances for emissions which could generate revenues commensurate with the additional needs. Any of these options would require further analysis and agreement at the intergovernmental level.

2. Views from Parties

60. Four Parties noted that resources presently available within the Convention process are inadequate to respond to the global challenge of climate change and to achieving the objective of the Convention. The discussions of financial flows and investments in the context of the Bali Action Plan is therefore an important process for designing a future financial architecture that takes into account the resources within and outside the Convention process, the need for improved access to adequate, predictable and sustainable financial resources and financial and technical support, and the provision of new and additional resources.

61. In view of the needs for investment and financial flows, four Parties noted the important role of the private sector in scaling up investments to address climate change in the future. The channelling of

global investments towards low-carbon energy technologies and adaptation measures should be consistent with the development needs and growth objectives of developing countries. In scaling up and leveraging these investments, international financial institutions and other sources of funding also play an important role. Public-sector investments can be used to leverage domestic and international private-sector finance. Governments may also provide the necessary enabling environments, adequate governance, and incentives at the national, regional and international levels, including regulation and market-based incentives, to attract public and private finance for deploying climate-related technologies and investments in infrastructures for climate-resilient development. According to one Party, it is also necessary to identify areas in which large emission reductions may be expected, as well as the mitigation potential of these areas, in order to promote investment. To this end, the expertise of specialized organizations such as the International Energy Agency should be utilized.

62. One Party noted that the global carbon market will continue to be one of the important drivers of investments in low-carbon technologies and also noted the need to actively engage the private sector in climate-related projects in order to provide predictable and sustainable financial resources. One group of Parties indicated the need to start an in-depth discussion on ways to improve existing mechanisms, and to consider the development of new instruments needed to ensure adequate, cost-effective and predictable finance and investment flows that will support mitigation and adaptation actions under a post-2012 agreement.

63. Another Party cited its experience in a debt conversion programme with Spain, and proposed such a programme as one possible innovative option for scaling up investments in climate change. It also noted that the experience of the Caribbean Catastrophe Risk Insurance Facility, the first disaster insurance facility in the world, may be replicated in other regions to manage country risk financing for hazards relating to climate change. Another Party noted, on the other hand, the need to develop human resources and institutional systems, including the protection of intellectual property rights in developing countries, in order to promote private-sector investments.

64. One Party proposed that a levy should be imposed on the share of proceeds from Joint Implementation and carbon trading activities to increase the resources of the Adaptation Fund. It also proposed the establishment of the following funds to address climate change:

(a) Technology Transfer Fund. As part of the Bali Action Plan, financing of development and transfer of technologies will come from various options because GEF resources will not be sufficient to support its implementation. Financing of technology transfer under the Montreal Protocol on Substances that Deplete the Ozone Layer may be explored as a model for this fund as work under this instrument has successfully reduced ozone depleting substances;

(b) Reduction in Emissions from Deforestation and Forest Degradation (REDD) Fund. The development of methodologies for calculating REDD is expected to increase contributions to its implementation. Contributions made by developed country Parties should be reported under the Convention;

(c) Voluntary Developing Countries Fund. Use of national funds for mitigation and adaptation measures by developing country Parties should be reported and acknowledged as contributions by these Parties to achieving the objective of the Convention.

65. Another Party proposed the creation of a Multilateral Climate Change Fund under the Convention. This would be directly under the authority and guidance of the COP, and its arrangements could be similar to those of the Multilateral Fund for the Implementation of the Montreal Protocol. It would allow developed country and Annex II Parties to fulfil their commitments on the provision of

financial resources under the Convention and ensure consistency and coherence of financing for the implementation of the Convention. The fund would support the implementation of long-term collaborative action under the Convention and allow for such action to be reportable, verifiable and measurable, including through the use of national communications, such as those of Annex I Parties.

66. One Party proposed that the intergovernmental process can stimulate and expand the opportunities for investments by playing an intermediary role in reducing the incremental costs, decreasing risks for investors and adopting enabling policies to support the expansion of the market. To increase the international financial response to climate change, the same Party proposed to further develop the carbon markets, increase investments to research and development of innovative technologies, attract private-sector investments and financial flows, and increase in-country investments in mitigation and adaptation measures, as well as adopting national energy efficiency standards.

67. Another Party suggested that a percentage of loans received by developing countries for infrastructure development should be used to fund projects on adaptation to climate change.

68. A group of Parties noted that the future climate financial architecture under the Bali Action Plan should support the mitigation and adaptation efforts of developing countries in a cost-effective and targeted manner. It is important to ensure that all Parties participate in the development of this financial architecture, and to ensure coherence and consistency with existing instruments and sources, including those under the Convention, in the light of the new climate-related instruments and funding sources.

69. The same group of Parties proposed to consider whether further analysis of some key areas of the investment and financial flows paper could provide a basis for further exploring policy options and implications with a view to accelerating the negotiations under the AWG-LCA.

- - - - -