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Financial mechanism (Kyoto Protocol)
Adaptation Fund**

Report on the workshop on the Adaptation Fund

Note by the secretariat*

Summary

This note contains the report on the workshop on the Adaptation Fund held in Edmonton, Canada, from 3 to 5 May 2006, in response to the request in decision 28/CMP.1, to promote an exchange of views on further guidance for the operation of the Adaptation Fund.

Following discussions based on submissions from Parties and intergovernmental organizations, presentations and background papers, participants discussed various options in detail in break-out groups focusing on institutional arrangements for the management of the Adaptation Fund, share of proceeds and other funding, eligibility and disbursement requirements, and priority areas.

The Subsidiary Body for Implementation may wish to use the information in this report as input to its deliberations on further guidance for the operation of the Adaptation Fund.

* This document was submitted late due to the timing of the workshop.

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I. Introduction

A. Mandate

1. The Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (COP/MOP), by its decision 28/CMP.1, requested the secretariat to organize, before the twenty-fourth session of the Subsidiary Body for Implementation (SBI), a workshop to promote an exchange of views on further guidance for the operation of the Adaptation Fund.

B. Possible action by the Subsidiary Body for Implementation

2. The SBI may wish to use the information in this report as input to its deliberations on further guidance for the operation of the Adaptation Fund.

II. Organization of the workshop

3. The Adaptation Fund workshop was held in Edmonton, Canada, from 3 to 5 May 2006. It was hosted by Environment Canada and organized by the UNFCCC secretariat. Thirty-seven participants representing 31 countries, together with representatives of several intergovernmental organizations (IGOs) and non-governmental organizations, attended the workshop.

III. Workshop proceedings

4. The Chair of the SBI, Mr. Thomas Becker, chaired the workshop. He was assisted by Ms. Marcia Levaggi, Argentina, and Mr. Karsten Sach, Germany, acting as co-chairs. An inaugural statement was made by Mr. Stephen Mandel, Mayor of Edmonton. Welcoming and opening remarks were also made by Mr. Thomas Becker and a representative of the UNFCCC secretariat. Ms. Rona Ambrose, Minister of the Environment, Canada, and current President of the Conference of the Parties and COP/MOP, hosted a breakfast for the workshop participants.

5. Participants had before them submissions from Parties (FCCC/SBI/2006/MISC.7 and Add.1) and from IGOs (FCCC/SBI/2006/MISC.5).

6. In addition, participants were provided with the following four background papers:

- (a) Summary of submissions on specific policies, programme priorities, eligibility criteria and possible arrangements for management of the Adaptation Fund
- (b) Share of proceeds to assist in meeting the costs of adaptation
- (c) Overview of possible institutional options for the management of the Adaptation Fund
- (d) Overview of existing programmes and policies to assist adaptation activities (including an overview of existing decisions relating to assistance for adaptation).

7. The workshop included presentations by representatives of institutions that might be capable of managing the Adaptation Fund, as identified in submissions by Parties: the Global Environment Facility, the World Bank, the United Nations Development Programme, the United Nations Environment Programme and the United Nations Multilateral Fund for the Implementation of the Montreal Protocol.

8. Following discussions based on submissions from Parties and IGOs, presentations and background papers, participants discussed various options in detail in four break-out groups focusing on criteria for institutional arrangements to manage the Adaptation Fund, share of proceeds and other

funding, eligibility and disbursement requirements, and priority areas. The specific topics discussed in the break-out groups are listed below:

- (a) Institutional arrangements to manage the Adaptation Fund:
 - (i) Institutional principles and criteria to be followed by an institution managing the Adaptation Fund
 - (ii) Relation of the governing body with the COP/MOP
 - (iii) Membership of the governing body
 - (iv) Institution to manage the Adaptation Fund
- (b) Share of proceeds and other funding:
 - (i) Sources of funding for the Adaptation Fund
 - (ii) Options relating to monetizing the share of proceeds
- (c) Modalities for operations
- (d) Eligibility criteria
- (e) Priority areas:
 - (i) Project activities
 - (ii) Priority sectors
 - (iii) Identification of priority project activities
 - (iv) Complementarities of fund activities.

9. Based on the discussions in the break-out groups, participants identified options for the above topics which are contained in the annex to this report.

10. All background papers and presentations, as well as the list of participants and agenda, are posted on the web page “Workshop on Adaptation Fund” on the UNFCCC website (http://unfccc.int/meetings/workshops/other_meetings/items/3672.php).

IV. Conclusions

11. Participants expressed their satisfaction with the workshop and encouraged the use of the outcome contained in the annex to support the SBI, at its twenty-fourth session, in deliberations on the Adaptation Fund.

Annex

Outcome of the workshop on the Adaptation Fund held in Edmonton, Canada, from 3 to 5 May 2006

I. Institutional arrangements to manage the Adaptation Fund

A. Possible principles and criteria to be followed by an institution managing the Adaptation Fund

Country driven-ness:

- 28/CMP.1: A country-driven approach
- Responsiveness to the needs and views of developing countries
- Reflect national priorities or regional priorities.

Accountability and transparency:

Accountability:

- Accountability to the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (COP/MOP)
- Ability to work under the authority of the COP/MOP (this point is also covered in option 2 (a), section B – reflect on this based on discussions on option 2 (a), section B)
- Separation and independence from the management, procedural arrangements and decision-making process of existing funds under the Convention and the Kyoto Protocol
- Separation of accountability and disbursement (separation of quality assurance, implementation and management)
- Independent monitoring and evaluation function
- Independent reviews at regular intervals.

Transparency:

- 28/CMP.1: Sound financial management and transparency
- Transparent reporting on management of the financial resources
- Financial management including independent financial audits and minimum international fiduciary standards.

Fund management:

- 28/CMP.1: Separation from other funding sources
- Autonomy to enable the use of funds in a flexible and fluent manner
- Serve as a catalyst to leverage additional financing
- Maximize means of funding from other sources.

Effectiveness and efficiency:

- Effective management and expeditious operation so that funding is available in a timely manner
- Overall procedures to be flexible, simple and clear
- Low transaction costs and cost-effective management
- Consistency and synergy with activities in related climate change areas
- Ensure the highest standards of professionalism.

Knowledge and networking capacity:

- 28/CMP.1: A learning-by-doing approach
- Have established knowledge and experience on how to manage a fund

- Have established knowledge and experience of adaptation activities
- A wider and/or appropriate base/network of organizations (including regional organizations) to serve as implementing agencies.

B. Relation of the governing body with the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol

Option 1: Keep the functions as outlined in decision 28/CMP.1. (The COP/MOP, by its decision 28/CMP.1, decided that the Adaptation Fund shall function under the guidance of, and be accountable to, the COP/MOP.)

Option 2: Provide the COP/MOP a stronger role to play:

Option 2 (a): In addition, the management of the Adaptation Fund shall be subject to the authority of the COP/MOP;

Option 2 (b): The decisions on how funds are disbursed should be made by the COP/MOP and the entity operating the fund should be bound strictly by the guidance of the COP/MOP.

C. Membership of the governing body

Composed of Kyoto Protocol Parties, with:

Option 1: Balanced representation from developing and developed country Parties (equal representation, one country one vote and equal number of developing and developed country Parties).

Option 2: Balanced representation of developing and developed country Parties.

Option 3: Balanced representation of Parties included in Annex I to the Convention and Parties not included in Annex I to the Convention (non-Annex I Parties).

Option 4: Majority of non-Annex I Parties.

D. Institution to manage the Adaptation Fund

(Note: The options below do not exclude any additional options.)

The selected entity has to demonstrate that it will be able to fulfil specific principles and criteria established for managing the fund.

Option 1: The Global Environment Facility (GEF).

Option 2: The GEF, provided that:

- The fund follows only criteria adopted by the COP/MOP and is not subject to the GEF's existing conditionality and criteria for fund disbursement; or

The fund follows only criteria adopted by the COP/MOP and is not subject to any of the GEF's conditionality and criteria for fund disbursement;

- A separate memorandum of understanding between the GEF Council and the COP/MOP is adopted regarding the operation of the financial mechanism of the Kyoto Protocol, containing guidelines for separate administration and management of the Adaptation Fund.

(Note: Where appropriate, if amendments to the GEF instrument would be needed, they would need to be flagged to the GEF Council, agreed by the GEF Council and further adopted by the GEF Assembly (which meets every four years).)

(Note: Conditions stated in option 2 shall apply, mutatis mutandis, to other options.)

Option 3: United Nations Multilateral Fund for the Implementation of the Montreal Protocol.

(Note: A new governing committee would be needed for the Adaptation Fund (for Parties to the Kyoto Protocol).)

(Note: This option would need to have agreement of the meeting of Parties to the Montreal Protocol (in accordance with Article 10 of the Montreal Protocol on Substances that Deplete the Ozone Layer).)

Option 4: United Nations Development Programme (UNDP).

(Note: Agreement from the UNDP Executive Board, United Nations Economic and Social Council and United Nations General Assembly would be needed.)

Option 5: United Nations Environment Programme (UNEP).

(Note: Agreement from United Nations General Assembly and UNEP Governing Council would be needed.)

Option 6: Arrangements similar to those for the United Nations Multilateral Fund for the Implementation of the Montreal Protocol:

- A new body established under the COP/MOP (new committee/governing body under the direct supervision of the COP/MOP and elected by the COP/MOP);
- An existing institution would be selected to host the secretariat of the fund;
(Note: consider any agency.)
- An existing institution would be selected that would be the trustee of the fund;
(Note: consider any agency.)
- Use the experience in cooperating with country offices and implementing agencies.

(Note: The new committee/governing body would need to be created by the COP/MOP and with agreement from the institutions that will be selected to act as secretariat and/or trustee of the fund.)

II. Share of proceeds and other funding

A. Sources of funding for the Adaptation Fund

Possible sources of funding shall be:

- Share of proceeds from clean development mechanism (CDM) project activities
- Other sources of funding, including:
 - Voluntary contributions by Parties
 - Contributions by other entities such as the private sector, foundations.

(Note: This is without prejudice to governance structure and assumes separate tracking of funding sources.)

B. Options relating to monetizing the share of proceeds

The COP/MOP should decide on principles or guidance for monetization that would be implemented by a designated institution.

Option 1: The COP/MOP decides on principles/guidance for monetization only and leaves implementation to a designated institution (which reports to the COP/MOP).

Possible principles/guidance include:

- Maximize revenue for the fund within risk tolerance
- Predictable revenue flow for the fund
- Operational principles, e.g. transparency, cost-effectiveness.

Selection of an institution, based on criteria set by the COP/MOP, to monetize the certified emission reductions (CERs) would be delegated to:

- The secretariat servicing the CDM Executive Board and the international transaction log under the Kyoto Protocol
- The institution responsible for managing the Adaptation Fund
- Other entity.

Specific monetization options could include:

- Direct sale of share of proceeds of CERs to Parties included in Annex B to the Kyoto Protocol at a premium price
- Periodic auctions of share of proceeds of CERs
- Sale of share of proceeds of CERs on an exchange, if possible
- Use of brokers to sell share of proceeds of CERs
- Some combination of the four preceding options.

Option 2: The COP/MOP specifies the share of proceeds in monetary terms with periodic revision and/or on an interim basis.

III. Modalities for operations

List of possible modalities to guide the management of the fund

Outreach:

- Regular consultations, outside formal processes, to be held between developing countries and the institution managing the fund.

Project cycle:

- Incorporate year-round submission, consideration and approval of proposals
- Use expedited processing system (such as that used by the GEF for medium-sized projects) for all projects
- Provide authority for the implementing agencies to commit the funds for the project following their own approval procedures (have a “simple” process for approval – keeping, however, central approval).

Disbursement modalities:

- Use similar funding principles as those of the Least Developed Countries Fund (LDCF) as a starting point
- Avoid the use of the incremental cost concept
- Draw on sliding scale to simplify calculation of fully funded additional costs of adaptation
- Ensure adequate geographic representation in access to resources.

IV. Eligibility criteria

Option 1: Article 12, paragraph 8, of the Kyoto Protocol.

Option 2: Article 12, paragraph 8, of the Kyoto Protocol, and recognizing that low-lying and other small island countries, countries with low-lying coastal, arid and semi-arid areas or areas liable to floods, drought and desertification, and developing countries with fragile mountainous ecosystems are particularly vulnerable to the adverse effects of climate change.

Option 3: All developing country Parties to the Kyoto Protocol are eligible to receive assistance from the fund.

Option 4: In particular, developing country Parties to the Kyoto Protocol particularly vulnerable to adverse effects of climate change:

Option 5: Eligibility restricted to developing country Parties to the Kyoto Protocol particularly vulnerable to adverse effects of climate change:

Option 4/5 (a): Particularly vulnerable is defined as in the Convention.

Option 4/5 (b): Small island developing States (SIDS).

(Note: This could be operationalized as a special window for funding SIDS.)

Option 4/5 (c): Least developed country Parties.

Option 4/5 (d): Developing country Parties with projected higher risks in the near future, in particular those which do not already have a specific fund of their own.

Option 4/5 (e): Developing country Parties and regions where available information indicates that the impacts of climate change are likely to be severe.

Option 4/5 (f): Possible combinations of options (a) to (e).

V. Priority areas

A. Project activities

Option 1: The Adaptation Fund shall finance concrete adaptation projects and programmes in developing country Parties that are Parties to the Kyoto Protocol.

Option 2: The Adaptation Fund shall finance concrete adaptation projects and programmes in developing country Parties that are Parties to the Kyoto Protocol. Concrete adaptation projects and programmes shall:

Option 2 (a): Be stage III activities.

Option 2 (b): Be stage II and III activities.

Option 2 (c): Have a maximum of 15 per cent of the budget for technical assistance and the majority of the budget for “actions in the field”.

B. Priority sectors

Option 1: The Adaptation Fund shall finance activities identified in decision 5/CP.7, paragraph 8.

Option 2: The Adaptation Fund shall finance activities identified in decision 5/CP.7, paragraph 8,

Option 2 (a): as well as areas identified as priorities under relevant decisions, such as 1/CP.10 and 2/CP.11.

Option 2 (b): as well as:

- Forestry
- Sustainable livelihoods
- Integrate adaptation into policy process and planning frameworks for decision-making which require development of tools, methods, modelling for local level and technology for adaptation
- Increase public awareness of the potential impacts of climate change and possible adaptation options and strategies, to enable decision-making at the individual and community levels
- Capacity-building:
 - Disaster-proof communication systems
 - Awareness and training exercises
 - Preparedness for desertification and support for rain enhancement and water harvesting activities under capacity-building in the areas of preparedness and management of disasters relating to climate change
 - Sensitize policymakers to the impacts their decision-making may have on adaptive capacity

- Explore the augmentation of insurance schemes for particularly vulnerable sectors, such as subsistence agriculture
- Economic diversification as a subtheme of the five-year programme of work on adaptation:
 - Promote understanding and development and dissemination of measures, methodologies and tools for economic diversification aimed at increasing economic resilience and reducing reliance on vulnerable economic sectors, especially for relevant categories of countries listed in Article 4, paragraph 8, of the Convention
 - Improve quality of models, in particular those that assess the adverse impacts on social and economic development as a consequence of the responses to climate change, taking into full account the legitimate priority needs of developing countries with specific emphasis on 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.

C. Identification of possible priority project activities

Priority project activities shall be identified:

- As priorities, inter alia, in national adaptation programmes of action, national communications, national sustainable development strategies, poverty reduction strategies and other relevant national plans;
- As thematic priority areas with links to development goals;
- As being of critical importance to human survival and economic sustainability;
- As priorities for addressing specific problems, local capacity-building, technology transfer and the promotion of indigenous technological applications;
- To avoid stand-alone projects;
- To seek projects with multiple benefits;
- To highlight good examples for adaptation.

D. Complementarities of fund activities

The Adaptation Fund shall be complementary to and not duplicate other existing funds and assistance, in particular with funding priorities and allocations for adaptation activities under the Special Climate Change Fund and the LDCF.
