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Discussion Paper

Direct Access to Climate Finance: experiences and lessons learned

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ENVIRONMENT AND ENERGY

1. Introduction

The volume, sources, and type of climate finance has grown significantly over the past decade. Such growth is an extremely positive development and is critical to support developing countries pursue low-emission, climate-resilient development. However, while the scale of finance is increasing it is essential that due attention is paid to the mechanisms and modalities that are used to access and deliver that financing. Within the context of the United Nations Framework Convention on Climate Change (UNFCCC) governments have been negotiating various options that will facilitate the effective, equitable, and efficient delivery of finance. This process has reinforced the importance of strong national climate strategies as well as in-country institutional structures. A major theme within these discussions has been "direct access". However, while significant political attention is paid to this concept, there is a pressing need to undertake a thorough substantive and technical assessment of what true direct access means and how it can be put to work in the context of climate change.

This paper provides an overview of the concept of direct access to funding for climate change actions in developing countries. It focuses on the institutional arrangements that are necessary to facilitate and support direct access and is intended to inform the current and future discussions on direct access modalities, including within the design process for the Green Climate Fund (GCF). The paper begins by looking at what the term 'direct access' implies, what it is seeking to achieve, and how it has been defined to-date. The experience with this financing modality in other global funds is then reviewed. Based on this, a number of lessons learned are highlighted and several possible future arrangements for directly accessing international climate change-related funding are outlined.

While the paper recognises the wide applications of direct access across both multilateral and bilateral, as well as public and private, financing modalities, the discussion here is restricted to only multilateral public financing—i.e. that sourced from international public funds.

2. What is direct access?

Whereas developed countries have internal resources to respond to climate change (both in monetary terms and a wide skills base), in many developing countries the response is undermined by a scarcity of such resources and capacity. These limitations are heightened for vulnerable groups, such as the poor and women, who often face increased political, social and economic barriers to accessing and benefiting from the limited financial resources which currently exist. It is now widely recognised that removing such barriers would widen the effectiveness and equity of climate finance, promote the Millennium Development Goals, and drive sustainable development.

With direct access, the facilitation function normally played by multilateral, international and bilateral entities in accessing international public finance is taken on by a national entity.

Accordingly, the international community has paid much attention to the need for new and additional finance to support developing countries' respond to climate change. It is expected that considerable sums will be needed, and Annex II governments[1] have already made significant commitments of both 'Fast Start Finance' of $30bn between 2010 and 2012, and long-term finance of $100bn per year by 2020. The institutional arrangements that are evolving to channel this finance need to contribute towards a

[1] Annex II countries of the UNFCCC are required to provide financial resources to enable developing countries undertake emissions reduction activities under the Convention and to help them adapt to the adverse effects of climate change.

long-term architecture, which will include how internationally-raised finance can be accessed by developing countries in ways that are country-driven, catalytic at the national level, and that promote equity and therefore sustainable development.

'Direct access' is a concept that has evolved from this international discourse. Direct access is widely understood as a short-hand term for developing countries directly accessing international public financing in order to implement national and local actions to address climate change. Direct access implies that the facilitation and project management function played by multilateral, international, and bilateral entities is not used to access international public finance, and instead this function is taken on by a national entity. Direct access to finance as a concept is applicable across both multilateral and bilateral financing; moreover, direct access to finance can be considered in terms of both public and private finance. Direct access to private finance, for example, is illustrated by the Clean Development Mechanism. However, for the purposes of this paper, the discussion is limited only to public finance from multilateral sources. In this context, the change in institutional roles implied by direct access—and the associated discussion on direct access—exists in the context of a wider dialogue on responsibilities, vulnerabilities, and capabilities. All of these issues alter the terms on which climate finance is discussed and negotiated.

Direct access reflects a wide transfer of scaled-up financial resources for developing countries while also transferring capacities and building national systems to access, manage and be accountable for those resources.

For example, questions of responsibility are important parameters in terms of international public climate finance and, by extension, who has authority to access and manage it. The answer to this question depends in part on the source of the finance. There is already an appreciation that finance for climate change actions will be drawn from multiple sources, as outlined by the 2010 UN high-level advisory group on climate change financing (AGF). The AGF report identified four potential sources of finance: public sources, development bank instruments, carbon market finance and private capital. Much of the early attention has focused on the first of these sources, namely public funds. Many developing countries perceive this revenue source as a payment made by polluting countries along the lines of the polluter pays principle. In making such payments, the ownership of the finance is transferred to the recipient country and hence the control for such resources becomes a national rather than an international concern. In contrast, many developed countries provide international funding on a different basis, particularly for mitigation, seeing this additional finance as a payment to developing countries in return for stabilisation and/or reduction of GHG emissions, where the ownership of the funding remains with the donor country.

These two perspectives represent very different starting points to a discussion over access to finance. From the first perspective, financial resources, as the entitlement of developing countries, should be available to national systems within those countries. From the second perspective, direct access to climate finance is less about a transfer of ownership and stewardship and more about accelerating the pace and effectiveness of delivery. In this second perspective, direct access is not by default a preferred option. Indeed, it is the juxtaposition of these different perspectives that perhaps underlies some of the initial lessons and experiences of operationalising direct access, and sets the scene for the discussion in this paper on possible models moving forward.

Issues of capabilities also provide an important context for considering direct access. Discussions over different levels and forms of responsibility and vulnerability must be complemented by acknowledging differing levels of capacity to mitigate and adapt, which has a direct bearing on how countries access and then manage internationally-sourced finance. In this respect, regardless of whether the term implies a transfer of ownership over resources or not, direct access is not simply a financial term. It reflects a wider transfer of scaled-up financial resources for developing countries whilst also transferring capacities and building national systems to access, manage, and be accountable for those resources. This includes capacities to identify the best national partners to execute projects, capabilities to develop bankable projects and programmes, and abilities to undertake financial management and good fiduciary practices.

3. Definitions of direct access

In this political context, and despite the attention given to the issue over recent years by governments, the term direct access is poorly defined in a formal manner. In terms of multilateral public climate finance, it was mentioned within the decision to establish the Adaptation Fund (AF) at the Third Conference of Parties serving as the Meetings of the Parties to the Kyoto Protocol (CMP): *'Eligible parties shall be able to submit their project proposals **directly** to the Adaptation Fund Board and implementing or executing entities chosen by governments that are able to implement the projects funded by the Adaptation Fund may also approach the Adaptation Fund Board **directly**;'* Paragraph 29, Decision 1/CMP.3, UNFCCC, 2007. However, practice under the AF has not followed the first part of this definition in a strict way, as all national proposals for funding are currently submitted by accredited national implementing entities rather than governments per se, after having received the endorsement of the country's Designated Authority (in most cases within the government Ministry of Environment).

This form of direct access allows for the implementation and execution of finance from the AF to be delegated to the national level, whilst the oversight function is retained at the international level by a Board with the legal capacity of the Adaptation Fund. The Board is accountable to the CMP, being under its guidance and authority, and it is the Board that instructs the trustee to disburse funds and signs the associated grant agreements with recipients. Under this arrangement, ownership of the financial resources of the Fund appears to rest with the Board at a day-to-day level but ultimately with the CMP.

Another reference to direct access appeared in the discussion paper on the governance of climate finance that the governments of the UK, Mexico, Norway and Australia circulated at COP15 in Copenhagen in 2009: *'There should be **direct access** to international finance where fiduciary standards allow and country level trust funds should be considered, among other alternatives, where **direct access** is not possible.'* In this presentation country level trust funds were not considered as being synonymous with direct access.

Direct access is also fleetingly mentioned within the terms of reference for the Transitional Committee appointed for the design of the GCF, as set out under the Cancun Agreements at COP 16: *'The Transitional Committee shall recommend to the Conference of the Parties for its approval at its seventeenth session and shall develop operational documents that address, inter alia:'... '(c) Methods to manage the large scale of financial resources from a number of sources and deliver through a variety of financial instruments, funding windows and access modalities, including **direct access**, with the objective of achieving balanced allocation between adaptation and mitigation;'* Appendix III, Decision 1/CP.16, UNFCCC, 2010.

These three references are among the very few statements that refer to direct access by official sources. A more detailed mapping of the governance arrangements underpinning direct access is needed to help clarify some of the potential for variation among direct access modalities. In particular, one fundamental issue is whether direct access should be limited to national government agencies or, as the AF allows, extend to national implementing entities that are not necessarily part of the government administration (but that have the government's endorsement). This question takes on greater significance as the range of financial instruments widens beyond grant finance.

4. The institutional architecture associated with direct access

There are three main components of the public architecture used to deliver international public finance from global funds. While the terms used to describe the different components vary by institution, clarity over the role of each element associated with the flow of public international funds is important to an understanding of the direct access arrangement:

- The first of these elements is a *fund manager or strategic oversight body* (usually a Board) that has the authority to make funding decisions and to instruct the trustee to transfer funds to finance selected proposals. In the case of direct access, such a body must have a legal identity to fulfil these functions so that it can enter into legal financial agreements with the recipient national entity[2].
- The second element is an *implementing body* (sometimes referred to as a supervisory body). It is this body's responsibility to identify, propose, oversee and appraise programmes/projects for the Board. The implementing body would normally be expected to hold the funds released by the trustee.
- The third architectural element is an *executing body*. Executing bodies receive funding to undertake programmes of work and may utilise sub-contracting arrangements to complete these activities.

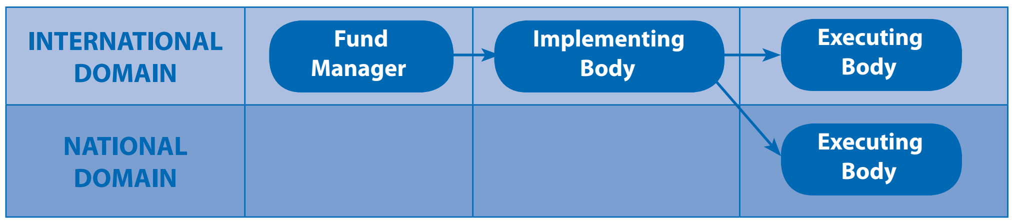
FUND MANAGER FUNCTIONS (SOME FUNCTIONS CARRIED OUT BY FUND SECRETARIAT)	IMPLEMENTING BODY FUNCTIONS	EXECUTING BODY FUNCTIONS
• Develops strategies, policies and guidelines of Fund • Reviews proposals submitted to Fund • Decides who receives funding • Instructs trustee to transfer funds to eligible implementing bodies • Monitors implementation progress • Accountable to donors on fund expenditures	• Identification of projects • Preparation of Project concepts • Appraisal of Project concepts • Preparation of project documents • Approvals and start-ups of projects • Supervision of projects • Evaluation of projects • Accountable to Fund on use of funds	• Management and administration of day-to-day project activities • Undertakes procurement and contracting of goods and services • Accountable to implementing body for use of funds

[2] In the case of multilaterally-implemented funds the trustee has traditionally provided this function, meaning the strategic oversight body does not require legal status. However, in the case of existing direct access modalities the trustee has not entered into agreements directly with national entities, hence the need for legal personality at the strategic oversight level.

The three main elements of this architecture give rise to three main access arrangements:

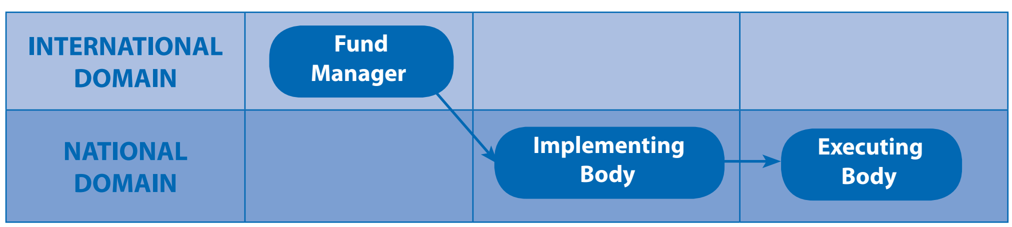
(i) ***Multilateral access:*** here fund oversight, management, and implementation are undertaken at the international level within a multilateral or international institution. Execution may take place at the national level (through national execution modalities within multilateral institutions) or may be managed from within the multilateral institution. Under this arrangement there is use of multilateral rather than country systems, with expenditure being channelled largely outside the national budgetary system.

a. ***Example:*** many international public climate funds use this model, including the Global Environment Facility (GEF) and Climate Investment Funds (CIFs).



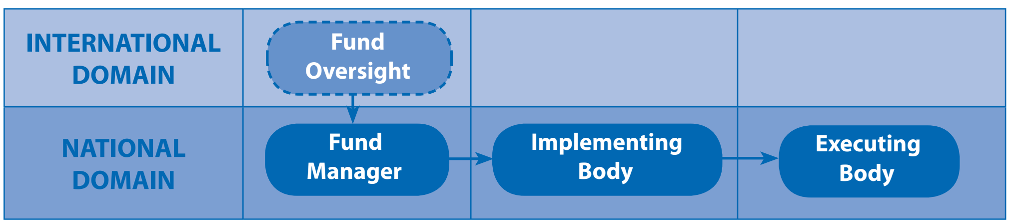
(ii) ***Direct access:*** here only the fund oversight and management function remains at the international level and both fund implementation and execution are delegated to the national level, usually to a national entity. In this case, the administration of funds is carried out by a national entity.

a. ***Example:*** the AF under the Kyoto Protocol has piloted this model on climate finance; however, within the health sector the GAVI Alliance and Global Fund to Fight AIDS, Tuberculosis and Malaria have delivered significant volumes of finance using this model.



(iii) ***Enhanced access:*** here all three functions – oversight and management, implementation, and execution – are delegated by the global fund in question to the national level. The key distinction between enhanced access and direct access (above) is that funding decisions and management of funds take place at the national level. Under such a scenario a country allocation or clearing house mechanism would operate at the international level to guide the level of internationally sourced funding to different countries. Other functions would then be delegated to entities at the national However, even within an enhanced direct access arrangement at least some degree of oversight is maintained at the international level, as the fund manager is required to report on the fund's activities and ensure sound practice among accredited entities[2].

a. ***Example:*** there are no major examples of enhanced direct access within the climate finance architecture. However, the report of the Transitional Committee tasked with the design of the GCF did state that the Board would "consider additional modalities that further enhance direct access, including through funding entities[3]".



[3] Funding entities are defined in a submission from the Least Developed Countries (LDCs) Group to the Transitional Committee as entities that are able to undertake fund management and oversight, implementation, and execution functions.

5. Experience of direct access arrangements within global funds

This section of the paper examines some of the lessons learned from three existing global funds that are channelling international public finance to developing countries: the Kyoto Protocol Adaptation Fund, the Global Alliance for Vaccines and Immunisation (GAVI), and the Global Fund to fight AIDS, tuberculosis and malaria (the Global Fund). Each of these funds uses a variant of the second type of direct access outlined in the previous section. The aim is to identify the key experiences and lessons from these funds' experience in delivering direct access.

5.1. The Kyoto Protocol Adaptation Fund (AF)

Description

The AF has developed direct access arrangements that allow eligible countries to submit funding proposals and receive approved funding through national implementing entities (NIEs) as well as through multilateral implementing entities (MIEs) if they so choose. This arrangement relies on national entities being accredited by the AF Board as having met certain fiduciary standards, related to financial integrity, institutional capacity and transparency of operation. It is important to note here that the standards development by the AF are wide ranging in scope, and include project management capabilities as well as basic fiduciary issues. The work to accredit NIEs for the AF began in January 2010, so there is limited experience to date with this arrangement as a full project cycle has not yet been completed for any NIE projects. Accreditation of multilateral organisations (termed multilateral implementing entities) took place in parallel to NIEs. Table 1 shows that funding to-date has largely flowed through MIEs, despite much political rhetoric in support of direct access.

The Adaptation Fund's initial lessons on direct access demonstrates the difficulty in balancing strong fiduciary principles and standards with the desire to increase the use of national entities for implementation and execution.

It is yet to be seen whether direct access will become a major funding arrangement for the AF without much greater investment to strengthen national capacity and clarify the accreditation process for potential applicants. However, Table 2 suggests a strong and developing demand by national organisations wishing to become NIEs, so the situation may change quite quickly if this demand is translated into effective readiness support. As an early step, Decision 5/CMP.16 mandated the UNFCCC Secretariat to organize three regional or sub-regional workshops on accreditation in order to make the accreditation process clearer to countries. To date, two workshops have taken place, the first in Dakar, Senegal, on 5-6 September 2011 for African countries and the second in Panama, Panama on 10-12 November 2011 for Latin America and the Caribbean. However, this does not directly deal with the critical issue