

The Adaptation Fund: a model for the future?

With millions of the poor already facing the impacts of a changing climate, adaptation is a globally urgent – and costly – issue. The Adaptation Fund, created under the Kyoto Protocol, has unique features that could herald a new era of international cooperation on adaptation. Its governance structure, for instance, offers a fresh approach to fund management under the UN climate convention. The Fund's Board has also developed a constructive working atmosphere, and further progress is expected before the 2009 climate summit in Copenhagen. But developing countries' demand for adaptation funding is huge: conservative estimates put it at US\$50 billion a year. The Fund's current structure and funding base are clearly only a first step towards filling that gap. And despite its significant progress over the last 18 months, many countries, particularly in the developed world, remain sceptical about this approach. Looking in detail at the Fund's evolution offers insight into its future potential as a model for adaptation finance.

Policy pointers

- **Adaptation to climate change** requires a vast amount of money, capacity and effective governance structures.
- **The Adaptation Fund of the UN Framework Convention on Climate Change** is still being shaped, but with its innovative features, is well suited to deal with adaptation challenges in the most vulnerable countries and communities.
- **The Fund needs more resources** to assist with adaptation.
- **A successful agreement** at the Copenhagen climate summit in 2009 could strengthen its functioning and funding base.

Beginnings: launch and aims of the Fund

For many of the world's poorer countries, adaptation to climate change is now an essential priority rather than an option. It is a task demanding vast amount of money and capacity, and effective governance systems to ensure good management of existing and future funds.

The Adaptation Fund (AF) was established under the Kyoto Protocol of the UN Framework Convention on Climate Change (UNFCCC) to finance concrete adaptation projects and programmes in vulnerable developing countries that are Party to the Protocol. While it was launched in 2001 at the 7th Conference of the Parties (COP) to the UNFCCC in 2001 in Marrakech, Morocco, some important provisions were not adopted until 2007. The legal framework of the Fund was established when its key documents were adopted at the 2008 climate summit in Poznań, Poland.

At Poznań, the Parties agreed that the AF should begin to operate as soon as possible. One of the AF's key principles is direct access by developing countries. The Parties also decided to give its Board legal status. Broadly, the Fund will assist countries on

a needs basis according to priorities identified through country-driven processes.

The Fund's innovative features

The AF has several unique features to do with the way it is owned, funded and governed. Together, these give it the potential to contribute significantly to international cooperation on adaptation.

The principle of ownership For the first time in the history of the international climate change regime, the AF clearly embodies the principle of ownership by developing countries, giving them a majority on its Board (see below). This ensures that the countries most affected by climate change impacts can participate more fully in decision making, and remain assured that funds will be dispersed effectively and transparently. The fact that developing countries have direct access to Fund resources also enhances this sense of ownership.

The funding mechanism Fund revenues are obtained primarily from a 2 per cent share in the proceeds from the Kyoto Protocol's Clean Development Mechanism (CDM) project activities. This means that the Fund is self-financed through the carbon market, independently from and in addition to contributions from developed

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countries. The first credits from CDM projects (CERs, for 'certified emission reductions') have now been monetised, and have generated US\$18.33 million.¹

By 2012, the Fund is likely to contain at least US\$500 million, but very probably much more.² This makes available funding predictable, dependent only on the development of the

carbon market. The revenue raised, however, will not be enough to cover the deficit in adaptation funding. Current estimates for adaptation in developing countries vary, but research by the charity Oxfam suggests this will cost a minimum of US\$50 billion each year. There is a clear need for a major boost in adaptation funding.

Governance The AF is supervised and managed by the Adaptation Fund Board (AFB). This Board works under the authority of, and is accountable to, the Meeting of the Parties to the Kyoto Protocol. The Board has 16 members (and 16 alternates): two represent each of the five UN regional groups, one represents Small Island Developing States (SIDS), one represents the Least Developed Countries (LDCs), two represent the Annex 1 (developed) countries and two represent the Non-Annex 1 (developing) countries. This representation enshrines the UNFCCC principle of equitable and balanced representation of all Parties in the governance structure.

Currently, the Global Environment Facility (GEF) provides secretariat services to the AFB on an interim basis. However, the secretariat dedicated exclusively to the AF is very small compared to those for other Funds (such as the Climate Investment Funds under the World Bank), and will likely need to be expanded once funding proposals by Parties are on the table. The World Bank serves as the AF's trustee, also on an interim basis. These institutional arrangements will be reviewed in 2011.

The Board's functions include the supervision and management of the Fund; the development of related strategies, policies and guidelines; setting operational parameters; and monitoring and reviewing the Fund's implementation. Every decision taken by the Board should be reached by consensus. Where consensus cannot be reached, a two-thirds majority of members present is sufficient, with a single vote per representative.

Recent progress by the Board

The AFB made significant progress in 2008. It adopted rules of procedure, legal arrangements for the AFB Secretariat and strategic priorities, policies and guidelines. The Board has developed a constructive working atmosphere, in stark contrast to the sometimes controversial and politicised negotiations under the UNFCCC. In 2009, the Board has also made considerable progress with developing an institutional mechanism to allow direct access to funds, establishing legal capacity and taking steps to set up fiduciary standards.

Applying for funding The AFB intends to provide rapid delivery of resources to developing countries and to avoid the often burdensome provisions existing in other international finance institutions.³ It has already agreed the process countries will follow to apply for funding (see 'The project cycle'), and it is expected that it will invite vulnerable developing countries to submit proposals before the climate summit in Copenhagen.

The project cycle

- 1 submission of the project /programmes to the AFB secretariat using templates to be approved by the AFB
- 2 screening for consistency by the secretariat. Technical summary for small-size projects
- 3 all proposals made public via the website before adoption
- 4 review by the Committee on Project and Programme Review. Can use services of independent experts
- 5 decision-making by the AFB (can approve or reject with a clear explanation); disbursement of funds by the trustee upon written instruction by the AFB (only in cases of fully fledged projects)
- 6 all projects: annual status reports and terminal evaluation reports.

Procedures are simpler for smaller projects below US\$1 million. No upper limit has yet been set for single projects or country programmes, but it is acknowledged that resources currently available will not be sufficient to cover the needs of all eligible developing countries. The Board has developed relevant criteria (see 'Criteria for the allocation of resources'), but there is not yet a clear picture of how this will be done.

Unfortunately, the Board could not agree to give priority to certain country groups like LDCs or SIDS, even though these groups are widely known to be particularly vulnerable.

Working towards direct access to funding The principle of direct access aims to simplify and accelerate the process by which resources for adaptation flow to developing countries. But what does this mean in practice?

The AF offers eligible Parties two access options:⁴ (a) direct access via National Implementing Entities (NIEs) in that country, or (b) via Multilateral Implementing Entities (MIEs), such as national offices of the UN Development Programme or regional banks. In both cases the implementing entities have to meet criteria and fiduciary standards set by the Board.⁵ These include issues like the ability to demonstrate financial integrity and management, and monitoring and evaluation. The

Criteria for the allocation of resources

- 1 level of vulnerability
- 2 level of urgency and risks arising from delay
- 3 ensuring access to the Fund in a balanced and equitable manner
- 4 lessons learned in project and programme design and implementation to be captured
- 5 securing co-benefits to the extent possible, where applicable
- 6 maximising multi-sectoral or cross-sectoral benefits
- 7 adaptive capacity to adverse effects of climate change.

Note: *In developing projects and programmes, special attention shall be given by eligible Parties to the particular needs of the most vulnerable communities.*

MIEs and NIEs will oversee project implementation and be accountable to the Board. Projects and programmes will be executed by so-called Executing Entities (EEs), such as government agencies and NGOs.

Allowing direct access meets the principle of ownership by recipient countries, but it also increases their responsibility in ensuring that resources are used for their intended purpose. Where required, building institutional capacity in vulnerable countries should be an integral task of the AF or its partner organisations.

An issue related to direct access is where the AF will be hosted. After controversial discussions at Poznań in 2008, legal capacity was conferred to the AFB – a precondition to fully implementing direct access. Two countries offered to provide this capacity: Germany, which already hosts the UNFCCC Secretariat, and Barbados. The Board plans to make its decision in September 2009.

The Barbados option would have a symbolic value by locating the Fund in one of the most vulnerable countries; and it would probably result in swifter implementation of direct access. However, the country's relative remoteness from other AFB member countries would saddle the Fund with higher mobility costs (both in value and time),⁶ and consume resources that could otherwise be spent on adaptation. Basing the Fund in Bonn would also allow closer exchange with the UNFCCC Secretariat as well as the opportunity to hold meetings back to back with UNFCCC negotiating sessions – a useful situation to date.

Helping the most vulnerable countries All countries have a human rights obligation to help the most climate-vulnerable people adapt. So the AF's Strategic Priorities,

Policies and Guidelines expect developing countries to 'give special attention to the particular needs of the most vulnerable communities'.

Closely linked to this aspect is the role of civil society. Many local and international NGOs work closely with communities at risk and have considerable experience with adaptation. Their active participation in decision-making on the disbursement, implementation and evaluation of funds for adaptation will be crucial. In the current institutional structure of the AF, civil society organisations can perform the following functions:

- promote dialogue between NIEs and national AF focal points before project submission. This could help ensure processes are transparent and inclusive from their early stages. Civil society organisations could also advise and monitor the work of the NIE, and help build its capacity on adaptation in practice
- be an EE if recognised by the NIE, monitor performance of other EEs and inform EEs about adaptation practices
- observe the overall performance of the AFB and the AF and, where necessary, lobby for certain improvements. This could involve informing AFB members about adaptation in practice; informing the outside world about AFB performance; and examining and commenting on project proposals published on the AF website.

So far, the AFB has not explicitly defined the role of civil society organisations in the project application and approval process. Nor has it spelled out how countries are expected to show that they are addressing the needs of their most vulnerable communities. Close cooperation with civil society organisations on different levels can help develop partnerships that effectively address this challenge.

The future Fund: assessing the outlook

The AF, with its innovative features, is still being shaped. It has the opportunity and responsibility to show how institutional innovations can rise to the challenge of adaptation.

The AFB has developed a constructive working atmosphere and has managed to meet key milestones. Progress in 2009 shows that it can reach agreement on difficult issues, such as fiduciary management standards. The Board's ability to agree on solid standards, which are also lean and not burdensome, will be crucial for its credibility. Occasional criticism that the process is too slow and the Board too politicised seems unjustified. Such criticism may be strategically motivated by developed countries who may feel that it is not in their interest to develop alternative approaches to the current World Bank/GEF architecture for delivering climate change funding. However, the way funding proposals are decided will be

the true test of how effective the AFB and its provisions are at helping the vulnerable adapt. Given the limited amount of available funding, allocation criteria must prioritise the most vulnerable countries, particularly LDCs and SIDS, and must recognise the needs of the most vulnerable people.

Many developed countries want to see a stronger move towards financing programmes rather than projects. But it is up to developing countries to choose their priorities, and implementing specific projects remains key due to scarce resource delivery in recent years. If resources stay at existing levels, it will also be extremely difficult to fund entire programmes in many vulnerable countries. Increasing available funding is a priority, for example through reliable funding mechanisms such as the auctioning of 'assigned amount units' of

allowed emissions for trade under the Kyoto Protocol – or the generation of resources from international transport, as the LDCs have proposed. This could be done without undermining the innovative features of the AF, which serve the needs of vulnerable developing countries.

The AF could play a more important role in the future climate regime, if its progress continues apace. An agreement in Copenhagen will need to include consideration of how to strengthen its role and funding base still further.

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Jargon buster

CER: 'certified emission reductions'. CERs are generated by 'climate-friendly' sustainable development projects in developing countries, and useable by their governments or companies to meet Kyoto Protocol reduction commitments. A CER amounts to 1 tonne of CO₂ equivalent. CER certificates are issued under the CDM.

Clean Development Mechanism (CDM): an arrangement under the Kyoto Protocol allowing developed countries to invest in emissions-reduction projects in developing countries.

Global Environment Facility (GEF): a worldwide partnership of countries, organisations and business that provides grants for sustainable development initiatives in developing countries, and operates the financial mechanism of the UNFCCC.

Kyoto Protocol: a protocol under the UNFCCC that sets a legally binding commitment for developed countries to reduce emissions of a range of greenhouse gases, and general commitment for all its 183 member countries.

UN Framework Convention on Climate Change (UNFCCC): the global climate treaty, aiming to stabilise atmospheric greenhouse gas concentrations to levels preventing 'dangerous' human-driven interference with the global climate system.

Further reading & websites

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- Simms, A., Magrath, J., and Reid, H. 2004. *Up in Smoke? Threats from, and Responses to, the Impact of Global Warming on Human Development*. First report of the Working Group on Climate Change and Development. nef/IIED, London. See www.climnet.org/pubs/200410_UplnSmoke-report.pdf.
- Adaptation Fund: www.adaptation-fund.org.

Notes

- ¹ Adaptation Fund Board. June 2009. Report of the 6th Meeting. Bonn, Germany.
- ² That assumption is based on a projection that 1.6 billion CERs (each representing a tonne of CO₂ equivalent) would be issued in 2012 from already registered CDM projects. Valued, at a conservative estimate, at US\$15 per tonne, that would equal US\$2.4 billion.
- ³ The Strategic Priorities, Policies and Guidelines and the Draft Provisional Operational Policies and Guidelines for Parties to access resources from the AF are the two key documents guiding the application process.
- ⁴ UNFCCC. 2001. The Marrakesh Accords. Decision 5/CP.7, paragraph 8.
- ⁵ Adaptation Fund Board. 31 March 2009. Draft Provisional Operational Policies and Guidelines for Parties to access Resources from the Fund. AFB/B.5/4 Rev.2, p 8.
- ⁶ Most flights from current AFB member countries to Barbados are over twice as long as flights to Germany, and cost over twice as much.

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