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DISCUSSION PAPER:

UNDERSTANDING THE GREEN CLIMATE FUND: IMPLICATIONS FOR THE EVOLVING ARCHITECTURE OF DIRECT ACCESS TO CLIMATE FINANCE

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Discussion Paper

Understanding the Green Climate Fund: Implications for the Evolving Architecture of Direct Access to Climate Finance

Ornsaran Pomme Manuamorn[1] and Robert Dobias[2]

Introduction

This discussion paper was prepared for the Regional Clinic on the Design and Management of National Climate Funds (NCFs) on 6-8 September 2012 in Bangkok, Thailand. The Regional Clinic is jointly organized by the United Nations Development Programme (UNDP) and the United States Agency for International Development (USAID) through its ADAPT Asia-Pacific project. The event brings together practitioners in the Asia-Pacific region who are fund managers of well established and recently established national funds, as well as those who are considering establishing new funds, to discuss technical aspects of NCFs and share practical experience from implementation. The objective of this paper is to situate the discussion on NCFs in the context of the evolving landscape of international climate finance. Since many NCFs are expected to play an instrumental role in accessing international funds for national climate change projects and programs, it is essential that managers of NCFs understand the requirements for accessing the funds using the direct access modality. The paper focuses on the early considerations in the design of the Green Climate Fund (GCF) and what it implies in terms of the emerging architecture of international climate finance in the coming decade. The paper concludes by outlining key considerations which should be taken into account in the design and operation of NCFs to enhance their readiness to directly access international climate finance.

I. Evolution of the Green Climate Fund (GCF) and its Current Status

Climate change has emerged as a top priority on the international development agenda in the past decade. A key catalyst was the findings of the fourth assessment report (AR4) of the Intergovernmental Panel on Climate Change (IPCC) released in 2007. The AR4 made clear that climate change is man-made and happening, and developing countries, especially the poorest ones, are the most vulnerable. To deal adequately with the challenges of climate change, developing countries need significant financial resources both to reduce greenhouse gas emissions and to adapt to the consequences of climate change.

Several cost estimates of potential climate change impacts as well as projected costs of adaptation and mitigation have been produced in recent years. Sachs and Someshwar (2012) reviewed the estimates and found that they vary significantly and carry great uncertainty due to different assumptions, models and methodologies used in the analyses. For example, the UNFCCC (2007) and the World Bank's Economics of Adaptation to Climate Change Study (2009) broadly provide similar estimates of USD 30–90 billion per year in adaptation costs for developing countries by 2030 (UNFCCC 2010 and World Bank 2009). The World Bank's estimates were later revised to project the costs of USD 70-100 billion a year between 2010 and

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2050 for developing countries to adapt to a world approximately 2 degrees *Celsius* (^{o}C) warmer, of which USD 40 billion annually will come from the Asia-Pacific region (World Bank 2010). As for mitigation, the IPCC review (2007) suggested mitigation costs by 2030 to range from -0.6%-3% of GDP, relative to the baseline emissions scenarios, depending on the global average temperature stabilization target (Sachs and Someshwar 2012).

How to finance the high costs of climate change is a key topic in ongoing international climate negotiations. Guided by the principles of common but differentiated responsibilities and respective capabilities, the United Nations Framework Convention on Climate Change (UNFCCC) articulated the need for developed countries both to reduce their own emissions and to help developing countries address climate change mitigation and adaptation challenges through financing and technology transfer. In 2009, developed country parties to the UNFCCC agreed as part of the Copenhagen Accord to provide developing countries with USD 30 billion in "fast start" finance for 2010-2012. In addition, an agreement was reached on the "long term" goal to mobilize climate finance of USD 100 billion per year by 2020. These commitments are "new and additional" to pre-Copenhagen official development assistance (ODA) flows and to be met by both public and private resources (though some developing countries are of the view that the commitment figures should only apply to public resources). The Copenhagen commitments also called for balanced allocations of climate finance between adaptation and mitigation.

Gaining a comprehensive picture of the current climate finance landscape is complicated due to the absence of a common definition of what constitutes climate finance, inconsistent reporting and tracking methodologies, and parallel financial flows for climate purposes outside the fast start framework. Efforts to track fast start commitments[3] suggest that as of August 2012 a large portion of the fast start finance coming mostly from public sources (with the exception of Japan which counts private sector finance) has been channeled from developed to developing countries through multilateral institutions, bilateral assistance programs and a pool of dedicated international climate funds, though the actual disbursement to individual programmes and projects are hard to track.

A study conducted by the Climate Policy Initiative (Buchner et. al 2011) estimated that **at least USD 97 billion per annum of climate finance** is currently being provided globally, out of which the amount of private finance is almost three times greater than public finance. While the USD 97 billion per annum figure is close to the ambitious Copenhagen goal of 100 billion per annum by 2020, the CPI study observed that not all of the USD 97 billion is necessarily additional to climate finance available prior to the Copenhagen Accord. In terms of distribution, the large majority of climate finance --USD 93 billion out of USD 97 billion-- is used for mitigation measures; a mere 5% goes to adaptation efforts. This suggests that inadequate considerations have been give to development of effective mechanisms to promote adaptation financing. At the same time, the imbalance may also reflect the lack of quality proposals for climate change adaptation projects (Figure 1).

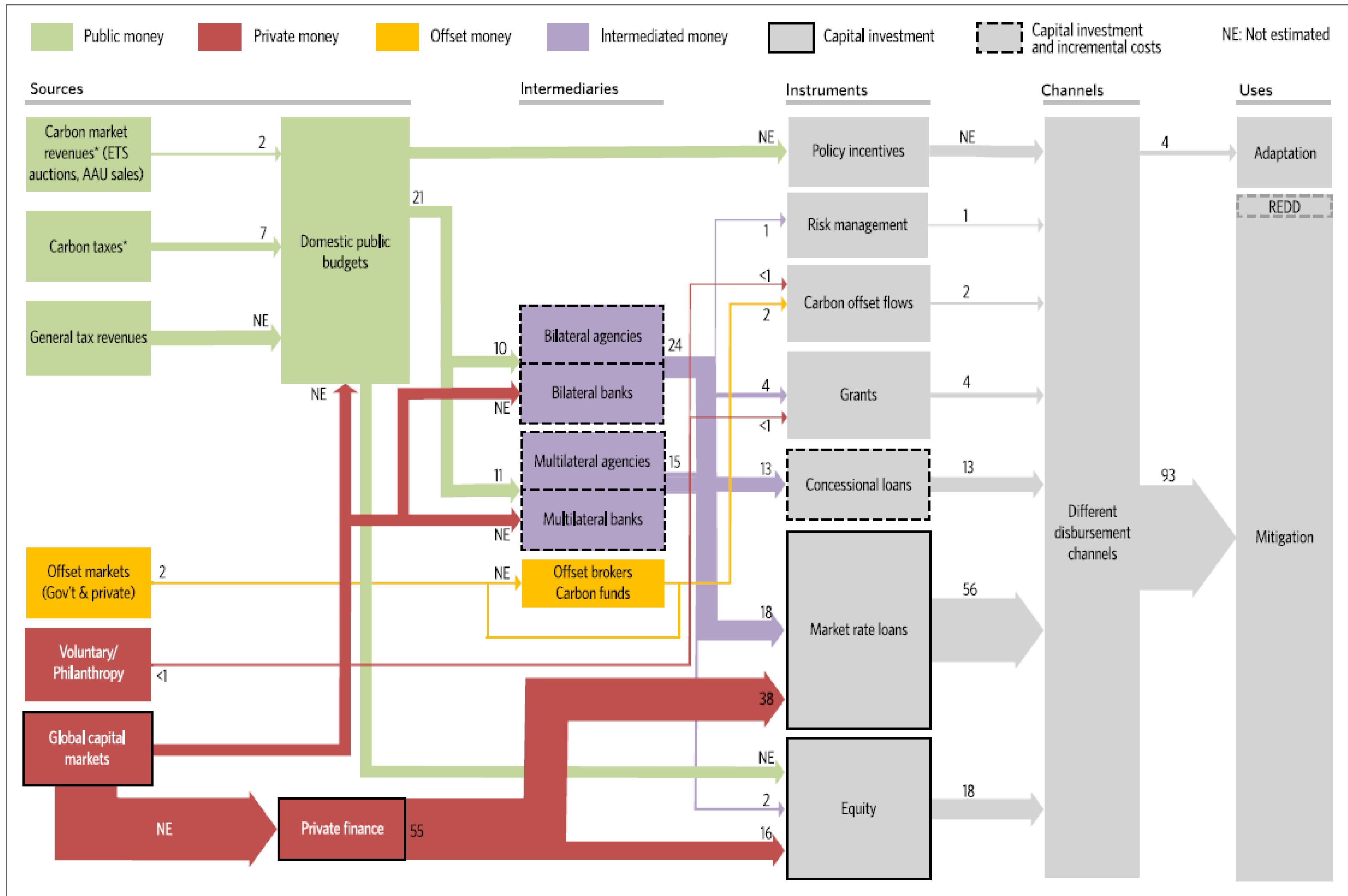
The CPI study also found that intermediaries such as bilateral and multilateral financial institutions play a key role in distributing climate finance. Dedicated climate funds, typically managed by bilateral and multilateral institutions, channel a small but growing portion of finance (Buchner et.al 2011). The two most important multilateral funds in terms of financing volume are

[3] See for example, World Resources Institute (WRI) http://www.wri.org/publication/summary-of-developed-country-fast-start-climate-finance-pledges

the Global Environment Facility (GEF) and **the Climate Investment Funds (CIF).** As the longest standing fund for climate change under the UNFCCC, the GEF primarily funds mitigation and adaptation activities in developing countries through two specialized funds: the Least Developed Countries Fund (LDCF) and the Special Climate Change Fund (SCCF). As of February 2012, the LDCF and SCCP have received a combined amount of USD 775 million in pledges and allocated over USD 370 million to climate change projects.[4] In 2008, the CIF was established as a joint undertaking of five multilateral development banks (MDBs), with an administrative unit housed at the World Bank. With over USD 6.5 billion of pledges to its sub-programmes, the CIF is the largest multilateral climate change fund that exists today.[5] Contrary to prior expectations, **the Kyoto Protocol's Adaptation Fund,** which was established at the UNFCCC Conference of the Parties (COP) in Marrakech in 2001 and became operational in 2009**,** plays a relatively small role in providing adaptation finance for developing countries due to its modest size (USD 200 million is estimated to be available between now and the end of 2012).[6]

4 Data provided by the GEF quoted in Manuamorn (2012)
5 See www.climateinvestmentfunds.org/cif/
6 Data provided by the Adaptation Fund Secretariat quoted in Manuamorn (2012)

Figure 1 Current Annual Climate Finance Volume



Source: Climate Policy Initiative (Buchner et. al 2011)

The Green Climate Fund

The GCF is the most important unfolding development with potentially transformational impact on the global climate finance architecture. This section provides historical context for the establishment of the GCF and discusses key design considerations. Information in this section is drawn from public documents from the GCF website[7], briefing notes, and background discussions on design issues considered by members of the Transitional Committee (TC) for the design of the GCF.

The GCF was conceived at the Copenhagen COP in 2009 as the main multilateral financing mechanism to support climate change actions in developing countries (Schalatek, Nakhooda, and Bird 2012). Once operational, it is expected to become the primary multilateral channel for large-scale financing both for mitigation and adaptation actions (Schalatek 2012). It is envisioned that the Fund will "promote the paradigm shift towards low-emission and climate-resilient development pathways by providing support to developing countries to limit or reduce their greenhouse gas emissions and to adapt to the impacts of climate change, taking into account the needs of those developing countries particularly vulnerable to the adverse effects of climate change." [8]

The decision to establish the GCF (Decision 1/CP.16) was taken by the Parties to the COP16 in Cancun, Mexico in 2010 as part of the Cancun Agreements. The decision states that the GCF will "manage 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."[9]

The architecture of the GCF was designed by a Transitional Committee (TC) which was established by the same decision (Decision 1/CP.16) at the COP16 in Cancun. The TC comprised 40 members, 15 from developed country Parties and 25 from developing country Parties. In accordance with its terms of reference (Annex III of decision 1/CP.16), the TC met four times during 2011 to work out design recommendations of the GCF and presented them to the COP17 in Durban, South Africa for its consideration and approval.[10] The GCF was formally launched in the COP17 by "Decision 3/CP.17, which approved the Governing instrument for the Fund annexed to that decision."[11] The adoption of the GCF's Governing instrument, along with a transitional process for its operationalization by 2014, was a key component of the "Durban Package" (Schalatek, Nakhooda, and Bird 2012).

The full design of the GCF is far from being settled. The approved Governing instrument only outlines the broad framework and general direction for operationalizing the GCF. Many details are left to be decided by the GCF Board. Key design parameters outlined in the GCF's Governing instrument document (FCCC/CP/2011/6)[12] are:

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7 http://gcfund.net/home.html
8 Ibid.
9 1/CP.16, Appendix III, Para 1(c) and 1/CP.16 paragraph 99.
10 http://gcfund.net/home.html
11 Ibid.
12 Report of the Transitional Committee for the design of the Green Climate Fund (FCCC/CP/2011/6). Available at http://unfccc.int/resource/docs/2011/cop17/eng/06.pdf

Objectives

- The GCF will "make a significant and ambitious contribution to the global efforts to combat climate change" by "channeling new, additional, adequate and predictable financial resources to developing countries and will catalyze climate finance, both public and private, and at the international and national levels."
- "The Fund will pursue a country-driven approach and promote and strengthen engagement at the country level through effective involvement of relevant institutions and stakeholders."
- "The Fund will strive to maximize the impact of its funding for adaptation and mitigation, and seek a balance between the two, while promoting environmental, social, economic and development co-benefits and taking a gender-sensitive approach."

Governance and institutional arrangements

- "The Fund will possess juridical personality and will have such legal capacity as is necessary for the exercise of its functions and the protection of its interests."
- "The Fund is accountable to and functions under the guidance of the COP" under an arrangement to be concluded between the COP and the Fund.
- The Fund's Board will "have 24 members, composed of an equal number of members from developing and developed country Parties."
- "The Fund will establish a secretariat, which will be fully independent. The secretariat will service and be accountable to the Board. It will have effective management capabilities to execute the day-to-day operations of the Fund."
- The Fund will have a trustee with administrative competence to manage the financial assets of the Fund."

Operational modalities

- "The Fund will provide simplified and improved access to funding, including direct access."
- "All developing country Parties to the Convention are eligible to receive resources from the Fund."
- "The Fund will have thematic funding windows. Initially the Fund will have windows for adaptation and mitigation" and "the Board will balance the allocation of resources between adaptation and mitigation activities."
- The Board will have the authority to add, modify and remove additional windows and substructures or facilities as appropriate."
- "The Fund will finance agreed full and agreed incremental costs for activities."
- "The Fund will have a private sector facility that enables it to directly and indirectly finance private sector mitigation and adaptation activities at the national, regional and international levels."

Access modalities and accreditation

- "Access to Fund resources will be through national, regional and international implementing entities accredited by the Board."
- For direct access by national institutions, "recipient countries will nominate competent subnational, national and regional implementing entities for accreditation to receive funding. The Board will consider additional modalities that further enhance direct access, including through funding entities with a view to enhancing country ownership of projects and programmes."

- For international access, “recipient countries will also be able to access the Fund through accredited international entities, including United Nations agencies, multilateral development banks, international financial institutions and regional institutions.”
- “The Board will develop, manage and oversee an accreditation process for all implementing entities based on specific accreditation criteria that reflect the Fund’s fiduciary principles and standards and environmental and social safeguards.”

Stakeholder input and participation

- “The Board will develop mechanisms to promote the input and participation of stakeholders, including private-sector actors, civil society organizations, vulnerable groups, women and indigenous peoples, in the design, development and implementation of the strategies and activities to be financed by the Fund.”

The generic language in the approved Governing Instrument reflects an attempted compromise, as well as the unsettled nature, of divergent visions of the Fund. Schalatek, Nakhooda, and Bird (2011) noted that early in the design process it became clear that developed and developing countries held widely different views on the Fund’s mandate, functions, scope and operational capabilities. Key disagreements surrounded the questions of how closely the COP should oversee the GCF, the method and time-lime for the GCF to achieve a judicial personality status, the appropriate process for civil society participation, and whether the private sector should perform a principal or supplementary role to public resources, etc. On the latter issue, developed countries envisioned the use of limited public finance to leverage greater private sector investments, while developing countries advocated for the GCF to be primarily financed by predictable and adequate public contributions by developed countries (Schalatek, Nakhooda, and Bird 2011).

Apart from the role of the private sector, a more fundamental issue considered by the TC was related to choices on the types and forms of financial inputs to the GCF. The choices carry significant implications for the fundamental characteristics of the GCF because the form of finance inputs (grants and non-grants) has an implication on the subsequent form of disbursed resources from the GCF. Since non-grant finance is more likely to target mitigation activities, receiving a significant portion of finance in non-grant forms could bias the distribution of resources between the GCF’s mitigation and adaptation thematic windows. In this context, some TC members underscored the need to keep the balance between mitigation and adaptation in mind when considering the form of contributions. Other members also suggested that significant grant inputs be targeted to ensure appropriate volumes of finance for adaptation activities. In addition, receiving non-grant finance (such as concessional loans, private sector investment, etc.) may require particular banking functions for the GCF to manage a process of receiving loan repayments and repaying contributions to Fund contributors. This in turn carries significant implications for the design of the GCF.

Regarding access to the Fund’s resources, there was an agreement among TC members that access modalities should promote wide and equitable access to the GCF and avoid restricting access for developing countries. Reflecting the agreement, the Governing instrument outlined a range of access options including national, regional and multinational entities, though the specific requirements of each option still have to be worked out by the GCF Board.

After a long delay, the GCF Board assembled on 23-25 August 2012 in Geneva, Switzerland and comprised 24 members –12 from developing and 12 from developed countries. As expected, the meeting agenda was dominated by key organizational issues including important Board procedures, work plan for the Board, observer participation, arrangements for the Interim

Secretariat and appointment of its Head, selection of the host country of the GCF, budget for the GCF's start up phase, finalization of arrangements with the World Bank to serve as an interim trustee, etc. (Schalatek 2012). Key outcomes of the meeting include the election of the Board's Co-Chairs and adoption of a decision on how to conduct the process to select the host country of the Fund.[13] It is hard to predict when the new Board will get through the deliberation of these organizational set-up issues and begin to decide on the substantive questions of the GCF's strategy, capitalization, business model and access conditions.

II. Past Experience in Direct Access to International Climate Finance: Overview of Challenges and Indications for Future Requirements

This section reviews past experience of developing countries in directly accessing international climate funds. The focus is on understanding current requirements of the funds against which developing country institutions must be accredited before gaining direct access. While different funds have specific accreditation criteria, there are generally overlapping requirements among the funds. This reflects a common perception among donors on the kinds of institutional infrastructure and capacities which need to be put in place for accessing international public climate finance. The understanding of the accreditation practice of existing funds is also likely to shed light on how the GCF may handle direct access in the future, and on the implications for NCFs, which will be discussed in section 3.

The concept of direct access has evolved from an international discourse on climate finance, considering how internationally raised finance can be accessed by developing countries in ways that are country-driven, equitable and sustainable (UNDP&ODI 2011). According to the UNDP and ODI (2011), "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". More broadly, direct access responds to demand from developing countries to take more control of aid resources. It also represents a paradigm shift towards using country systems instead of parallel donor systems in line with the Paris Declaration on Aid Effectiveness.

In reality, direct access is an exception rather than the norm in current international climate finance. For the CIF and GEF funds, countries access the resources by using the services of one of the multilateral institutions to prepare and submit project proposals. Once the project is approved, funding is administered by the multilateral institution on behalf of the recipient country using the institution's fiduciary standards and safeguards. And while these multilateral funds provide grant financing, developing country recipients are often required to leverage investments by MDBs to co-finance projects with the grants, thus significantly tying the use of climate finance to MDBs' existing country programs in practice.

An exception to the use of intermediaries is the Adaptation Fund which is the only multilateral climate change fund with fully operationalized direct access. The Fund reserves 50% of its resources for direct access by accredited national implementing entities (NIEs), while the rest can be accessed by multilateral implementing entities (MIEs). Recently, the GEF has also begun to test accreditation of national institutions for direct access, but this process is still in its

[13] Green Climate Fund Press Release, 25 August 2012.

initial pilot stage.[14] As for bilateral funds, there is currently no practice of accrediting national recipients, but budget support is used by some donors (such as the European Union) as a form of granting direct access to climate finance by developing country institutions. In these cases, budget support could be provided as a direct transfer between ministries of finance in a donor and recipient country, or as a bilateral contribution to a NCF within a recipient country's budgetary system.[15]

Accreditation of national implementing entities (NIEs)

The rationale for accreditation stems from the need to ensure that internationally raised climate finance, especially from public sources, is used in an effective, transparent and accountable manner. This requires that recipient country institutions demonstrate capacity to manage the funding using internationally acceptable systems and standards. A review of recent experience from the Adaptation Fund's NIE application process, as well as the progress of the GEF pilot on direct access, suggests gaining accreditation is a daunting task, and developing countries are facing challenges in the accreditation process.

The Adaptation Fund

An organization must meet the Fiduciary Standard established by the Adaptation Fund Board (AFB) in order to become a NIE. The Adaptation Fund defines the Fiduciary Standard as "a reference framework of policies, systems and practices which are required by an organization to effectively manage funds and projects on a sustainable basis". To be accredited, an NIE applicant must meet the Adaptation Fund's Fiduciary Standard in three areas:

1. Financial Management and Integrity
2. Institutional Capacity
3. Transparency, Self-investigative Powers, and Anti-corruption Measures

The AF accreditation process is essentially a process of exchange of information between the NIE applicant and the Accreditation Panel on all of the assessment criteria. It is important to note that the Adaptation Fund does not mandate any particular way, system, or approach by which an organization can meet the Fiduciary Standard; what is important is the ability of an organization to demonstrate that its current system and practices are sufficient in all the three areas. In the application package, an NIE applicant is required to provide adequate documentary evidence to the Adaptation Fund of both the framework and implementation of all the key parameters of the Fiduciary Standard. The Adaptation Fund also considers experience in handling large projects, especially those relating to climate change. Annex I summarizes individual assessment criteria associated with each of the three areas, as well as back-up documents required to substantiate the capabilities.

Past experience suggests that the time it takes for an NIE to get accredited can vary greatly. Centre de Suivi Ecologique (CSE) in Senegal was the first accredited NIE in 2010 and the process then took only three months. On the other hand, the Ministry of Planning and International Cooperation of Jordan, which has been recently accredited, took over one year, a timeframe which is more in line with most cases. This may reflect that the standards of the Accreditation Panel have become more rigorous and additional requirements put in place as the

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[14] http://www.thegef.org/gef/sites/thegef.org/files/documents/document/Accreditation.pdf .

[15] This is not always the case in every country which has established an NCF. In some countries NCF resources are considered off-budget.

Panel gains more experience in reviewing applications. It also leads to a widely held expectation that conditions in gaining direct access to the GEF and to the future GCF will get even tougher.

Several common reasons contribute to countries experiencing difficulties or delays in attaining accreditation.[16] Before submitting an application, some countries have reported difficulties in establishing a robust process for undertaking the selection of appropriate NIEs. Key reasons are:

- The Fiduciary Standard was not given adequate consideration during the selection process;
- Inadequate due diligence was conducted when reviewing existing institutional capacity of the potential NIEs; and
- Too much focus was given to the institution's experience in handling international loan and donor funds, with low priority given to project management capabilities.

After submitting an application, many NIE applicants cannot provide adequate supporting documents to accompany the applications. The reasons are that the documents do not exist, could not be identified, and/or need to be reorganized or upgraded before submitting. Specifically:

- Translation of documents from a local language to English is a delaying factor. Given the amount of supporting documents required, translations required substantial time and resources. In order to facilitate the process, the Accreditation Panel advised that only the relevant parts of a document should be translated;
- The Accreditation Panel experienced a lot of no-responses when reverting to the NIE applicants with clarification questions. This reflects the fact that some organizations submitted applications simply at the request of national governments but lack the real interest and enthusiasm needed to engage in the accreditation process; and
- Several applicants did not have an adequate system and/or capabilities to become NIEs. The most common areas of weakness were the internal control framework, auditing and the anti-corruption framework.[17] When these weaknesses are identified by the Accreditation Panel, the applicant needs to put in place a new mechanism or capability to address the gaps and demonstrate that the new system has worked before presenting the new evidence to the Panel. This process itself could take longer than a year.

In many cases, "conditional accreditation" is granted to an NIE. Conditional accreditation refers to a situation when the AFB approves that accreditation can go ahead based on an understanding that an agreed set of improvements must take place before money is disbursed to the NIE for the first project. Conditional accreditation is often used when the remaining capability gaps relate to the anti-corruption framework.[18]

The stringent accreditation requirements are reflected in the low success rate of developing country applicants. The UNDP & ODI conducted a review of the Adaptation Fund's accreditation process and found that there are a significant number of national institutions that have failed accreditation (UNDP & ODI 2011). As of September 2011, only six out of the 23 NIE applicants were accredited. As of June 2012, the number of accredited NIEs increased to 12 (Table 1). In terms of accessing actual project funding, 22 projects prepared by MIEs have been funded by

[16] Summary based on the Author's discussions with staff of the AFB Secretariat, members of the Adaptation Fund Accreditation Panel, and country representatives at the Workshop on the Process and Requirements for the Accreditation of National Implementing Entities for Direct Access under the Adaptation Fund for Asia and Eastern Europe, Manila, March 19-21, 2012.

[17] Ibid.

[18] Ibid.

the Adaptation Fund to date as opposed to only three funded projects prepared by NIEs.[19] This suggests that many NIEs are still facing challenges in preparing actual project proposals after gaining accreditation.

Table 1: Adaptation Fund's Accredited Implementing Entities

National Implementing Entities (NIEs)	Multilateral Implementing Entities (MIEs)	Regional Implementing Entities (RIEs)
• Centre de Suivi Ecologique (Senegal) • Planning Institute of Jamaica (Jamaica) • Agencia Nacional de Investigación e Innovación (Uruguay) • Fonds national pour l'environnement (Benin) • South African National Institute for Biodiversity (South Africa) • Protected Areas Conservation Trust (Belize) • Ministry of Natural Resources (Rwanda) • Ministry of Planning and International Cooperation (Jordan) • Mexican Institute of Water Technology (Mexico) • Unidad para Cambio Rural (Unit for Rural Change) (Argentina) • National Environment Management Authority (Kenya) • National Bank for Agriculture and Rural Development (India)	• The World Bank • ADB • AfDB • IADB • UNDP • UNEP • IFAD • WFP • WMO • UNESCO	• Banque Ouest Africaine de Développement (BOAD) (West African Development Bank)

Source: AFB Secretariat

The GEF

The GEF Council approved in May 2011 a pilot to accredit new institutions to serve as GEF project implementing partners. Accredited institutions will be called "GEF Project Agencies". According to the GEF's website, "upon accreditation, GEF Project Agencies will be entitled to work directly with the GEF Secretariat and Trustee to assist recipient countries in the preparation and implementation of GEF-financed projects, which will enable them to access resources from GEF-managed trust funds directly."[20] The GEF will be able to accredit up to 10 institutions under the pilot, with the goal of accrediting at least five national institutions. The first round of application was closed in December 2011. Applications from 16 agencies (six national entities, four regional entities, and four international NGOs) were received.[21] Applicants have to undergo a three-stage process:

[19] http://www.adaptation-fund.org/funded_projects accessed on 22 August 2012
[20] http://www.thegef.org/gef/agencies_accreditation
[21] Author's conversation with the GEF secretariat staff, May 2012.

- **Stage 1: Core value-added review.** There are six criteria for evaluation of applicants:
    - Relevance to the GEF
    - Demonstration of environmental or climate change adaptation results
    - Scale of engagement
    - Capacity to leverage co-financing
    - Institutional efficiency
    - Networks and contacts

The stage-one review is conducted internally by the GEF Council to determine whether the applicant would be a suitable GEF project partner. Institutions which qualify should have existed for more than five years. Applicants should provide documentary evidence supporting their answers in most cases in relation to each criterion. Applicants may do so by including the link to a document(s) on a publicly available website or by including a copy of the document(s) with the application form.

- **Stage 2: Assessment of fiduciary standards, safeguards, and compliance**

If approved by the Council, applicants will move forward to Stage 2 of the accreditation process which is conducted by the GEF's Independent (External) Accreditation Panel Review. At this stage, applicants will be assessed against criteria in five areas:

1. Audit, Financial Management and Control Framework
2. Project/Activity Processes and Oversight
3. Investigations of Allegations of Fraudulent and Corrupt Practices and of Possible Agency Staff Misconduct
4. Minimum Standards on Environmental and Social Safeguards
5. Gender Mainstreaming

- **Stage 3: Conclusion of memorandum of understanding and financial procedures agreement**

The GEF Council at its June 2012 meeting decided to approve 11 agencies to progress onto Stage 2 of the accreditation process and invited them to submit their Stage 2 applications to the GEF Secretariat for review by the GEF Accreditation Panel. The 11 agencies are listed below.[22] The Council further decided to postpone the consideration of a next round of accreditation until its November 2012 meeting.[23]

- The Development Bank of Southern Africa (DBSA)
- Fundo Brasileiro para a Biodiversidade- Brazil (FUNBIO)
- Foreign Economic Cooperation Office – China (FECO)
- National Environment Fund – Peru (FONAM)
- VTB Bank – Russian Federation (VTB)
- Banco de Desarrollo de America Latina (CAF)
- Banque Ouest Africaine de Dévelopment (BOAD)
- World Wide Fund (WWF)
- Conservation International (CI)

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[22] http://www.thegef.org/gef/sites/thegef.org/files/docuents/C.42.09.Rev_.01_Secretariat%20Recommendations%20of%20Project%20Agencies%20for%20Accreditation.pdf

[23] http://www.thegef.org/gef/agencies_accreditation

- International Union for Conservation of Nature (IUCN)
- International Federation of Red Cross (IFRC)

Reflecting the stringent criteria used, the Stage 2 application form contains 140 individual questions, for most of which applicants are required to provide back-up evidence to the responses. At this stage, applicants will also need to pay an accreditation fee of USD 25,000. This fee will not be refunded if the applicant fails to be accredited. It is unclear how long the Stage 2 process will take, but the amount of information required in the application form suggests that substantial capacity, resources, and time will be required for the applicants to pass this stage.

Comparison of the accreditation criteria of the Adaptation Fund and the GEF indicates that both funds pay high attention to three similar issues: financial management, project management and transparency measures. However, the additional inclusion of social, environmental and gender criteria by the GEF suggests a more demanding accreditation process, and one from which several new challenges and lessons learned will emerge. While the accreditation requirements for the GCF are as yet unclear, the language of the Governing instrument suggests that the GCF may adopt an expanded set of accreditation criteria similar to that of the GEF. In the meantime, developing countries may see the accreditation process of the two funds as providing useful indications of what needs to be put in place in preparation for direct access to the GCF.

III. Evolving Architecture of Direct Access to International Climate Finance: Considerations for National Climate Funds

This section discusses key considerations for NCFs in the context of the evolving architecture of direct access to climate finance. It outlines steps which may be taken by NCFs not only in expectation of the GCF but also in enhancing national climate finance readiness more broadly.

Many countries in the Asia-Pacific region have recently established NCFs as an implementation tool to manage climate finance. NCFs vary in terms of their mission, funding sources, operations, trustee arrangements, capitalization and beneficiaries. However, they generally share common functions in attracting climate finance from a variety of sources and coordinating, blending, and channeling them while attempting to ensure accountability and transparency. In many cases, NCFs are established so that they will be able to tap into the billions of dollars expected to be channeled toward climate change actions in the region.

The GEF accreditation process and the design discussions of the GCF point to the possible nature of international climate finance in the coming decade as well as what it means to be ready for climate finance at the national level. While the momentum for expanded direct access is clear, donors will also insist that international climate funds adopt rigorous standards and safeguards covering all national entities and activities involved. The standards and safeguards may constitute serious impediments to developing countries in accessing the funds if NIE candidates do not fully understand accreditation requirements, or lack resources and technical assistance needed to build the required systems and capabilities. As many countries in the Asia-Pacific region are implementing new NCFs or in the process of designing ones, there are important issues to be considered if these NCFs are expected to play an important role in directly accessing international climate finance in the future.

First, designers of NCFs should pay close attention to the standards and safeguards which donors see as prerequisites for enabling access to their funds. In the case of the GCF, developed countries insist that the GCF Board adopt ‘best practice’ fiduciary standards and ‘best practice’ standards for environmental and social safeguards, which will be applied to all projects and all implementing entities, both national and multilateral, of the GCF (Schalatek, Nakhooda, and Bird 2012). A key issue here is for the GCF Board to come up with a definition of ‘best practice’ which is agreeable by donors, developing countries and other stakeholders. In addition to the standards and safeguards, the GCF’s Governing instrument also made explicit references to accountability mechanisms, stakeholder input and participation, and monitoring and evaluation. These are likely to be fundamental to the NIE accreditation criteria and project approval process of the GCF.

For future NIE applicants, experience from the Adaptation Fund and the GEF illustrates the importance of a strong track record of performance. The Adaptation Fund advises against nominating a new institution with no track record as an NIE candidate, while institutions which qualify to apply for the GEF accreditation should have existed for more than five years. Therefore, NCFs hoping to serve as NIEs or the equivalent for major international climate funds will need to continue to invest in building fiduciary and safeguard systems and developing an inventory of evidence of their effectiveness.

Third, international climate funds are likely to prioritize funding for projects and programs which are mainstreamed into national development plans and processes. For example, the GCF’s Governing instrument clearly states that “The Fund will pursue a country-driven approach and promote and strengthen engagement at the country level through effective involvement of relevant institutions and stakeholders.”[24] In addition, “The Fund will support developing countries in pursuing project-based and programmatic approaches in accordance with climate change strategies and plans, such as low-emission development strategies or plans, nationally appropriate mitigation actions (NAMAs), national adaptation plans of action (NAPAs), national adaptation plans (NAPs) and other related activities.”[25] If a country expects its NCF to be the primary mechanism to access international climate finance and subsequently blend the funding with other domestic resources, then care is needed to ensure that the design of the NCF does not inadvertently work at cross-purpose to mainstreaming climate finance into national and subnational planning and budgeting systems. Such mainstreaming is especially important for climate change adaptation. This is because all current estimates suggest that international resources are inadequate to meet the adaptation needs globally, while private sector finance is also likely to prioritize investments in mitigation activities. Therefore, developing country governments themselves will need to shoulder most of the long term costs of adaptation using national budgets. NCFs should be designed to facilitate not counter this eventual transition.

Mainstreaming is also important for ensuring sustainability of climate change projects and programs themselves. In some countries, NCF funds may be kept “off-budget” and consequently not show up on national ledgers, which in turn can contribute to the marginalization of climate change programs unless early precautions are taken. In other cases, an NCF may be established as an interim measure that provides structure to climate financing while being “off-budget”. To ensure mainstreaming, clear plans should be formulated to transition from the off-budget NCF to an on-budget mechanism at some future date. An approach is to use donor funding channeled through an NCF for demonstration activities.

[24] Report of the Transitional Committee for the design of the Green Climate Fund (FCCC/CP/2011/6). Available at http://unfccc.int/resource/docs/2011/cop17/eng/06.pdf

[25] Ibid.

Subsequently, these activities could be scaled up by national budget as well as domestic private sector financing. The Indonesian Climate Change Trust Fund (ICCTF) is an example of an NCF which adopts this approach in its current operation of the Innovation Fund.

A sufficient volume of high quality project proposals is another key factor for a country's ability to rapidly access international climate funds. In the case of the GEF, applicants for direct access already need to submit preliminary project ideas during the screening stage. While many developing countries already have NAMAs, NAPAs, NAPs or other climate change strategies in place, there is a general lack of readily financeable climate change project proposals. Most project ideas are still at the concept level without specific details on costs and benefits and a plan for implementation. In the interest of mainstreaming climate change into national planning and budgeting as well as preparing for the GCF, GEF and other sources of international climate finance, it is in the interest of developing countries to raise the level of their NAMAs and other climate change programs so that there is an available pipeline of high quality mitigation and adaptation projects. And as a large number of project proposals may be generated from this process, NCFs can play an important role by selecting the best projects for funding. To do so, NCFs need to develop capacity to review project proposals in order to prioritize the most promising projects to match the available sources of funding.

Finally, it is important that NCFs have a strong monitoring and evaluation (M&E) plan and the means to implement it. Donors have increasingly placed emphasis on M&E in the provision of development finance in general, and for climate finance, it is clearly reflected in the GCF's Governing instrument. Whether the NCF is financed through domestic or international sources or both, the people and institutions providing the finance will want to ensure that their funds are achieving results, and therefore, would like to see a robust M&E system in place. While a relatively standard methodology exists for measurement, reporting and verification (MRV) of carbon emissions from non-REDD[26]mitigation projects, there is not yet an equivalent standardized approach for REDD and adaptation activities. In looking forward, NCFs should invest resources in developing an M&E system for both mitigation and adaptation activities. The M&E system development could be carried out in an integrated manner with the strengthening of NCFs' project review capacity, with the criteria used in prioritization of project proposals for funding feeding back into the M&E process and vice versa.

Discussions around the design of the GCF recognized that both additional resources and technical assistance are needed for building climate finance readiness in developing countries. Main areas of capacity building include establishment and management of NCFs, NIE accreditation, climate change project design and preparation, national-local transfers of climate finance resources, etc. Several donor and multilateral organizations are currently active in providing technical assistance to developing country national climate finance institutions NCFs could benefit substantially from familiarizing themselves with these capacity building programs and tap into their resources and expertise.

[26] REDD - Reducing Emissions from Deforestation and Forest Degradation

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Annex I
Adaptation Fund Accreditation Assessment Criteria and Back-up Evidence

<table>
<tr><th colspan="2">1. Financial Management and Integrity</th></tr>
<tr><th>A. Criteria</th><th>B. Required Supporting Documents</th></tr>
<tr><td>1.1 Legal Status</td><td>1. Documents providing clear demonstration of legal status and mandate:
a. Provide separate letter confirming legal status if necessary
2. List of foreign loan/donor funds handled over the last 2 years
3. Clarity or legal opinion that the applicant by virtue of its enabling legislation has no restriction to do the work of a NIE</td></tr>
<tr><td>1.2 Financial Statements and Audit Requirements</td><td>1. Audited Financial Statements including project account statements
2. External Auditor Reports with management comments and responses
3. Audit Committee's Terms of Reference and minutes of meetings
4. Name and brief description of accounting package used
5. Policy/charter and other published documents (like manuals) that outline the entity's internal auditing function
6. Copies of internal audit plans for last 2 years and the current year
7. List of internal audit reports of last 2 years and sample reports
8. Management response and action taken on internal audit reports</td></tr>
<tr><td>1.3 Internal Control Framework[27]</td><td>1. Policy or other published document that outlines the entity's internal control framework (ICF). Demonstration of an effective ICF must include:
– Documented organisational structure and division of responsibility with reference to internal control</td></tr>
</table>

[27] According to the AF Accreditation Panel, the objective of an Internal Control Framework is to ensure that the organization has in place systems for internal control over operational and financial matters which provide reasonable assurance to all stakeholders that transactions within the organization are:

- Undertaken in accordance with management policy and authority
- Assets are protected against material loss or unauthorized acquisition, use or disposition
- All transactions are properly authorized and recorded
- Environmental and other organizational risks are systematically and regularly identified
- Action to handle the risks is planned, implemented and reviewed.

	– Established policies and procedures undertaken in accordance with management policy and authority – Oversight/audit system that monitors the operation of the internal control system and report findings and recommendations to the top management 2. Procedures describing the payment/ disbursement system with particular reference to project payments/disbursements
1.4 Preparation of Business Plans and Budgets	1. Long Term Strategy/Business plans and/or Financial Projections for the next 3 to 5 years 2. Annual budgets for the organization or entities within it 3. End of calendar year/fiscal year or periodical budget vs actual report with analysis of variations
2. Institutional Capacity	
A. Criteria	*B. Required Supporting Documents*
2.1 Procurement	1. Procurement Policy 2. Detailed procedures or guidelines including composition and role of key decision making committees 3. Provisions for oversight/audit /review of the procurement function with sample oversight/audit/review reports 4. Procedures for handling/controlling procurement in Executing Agencies
2.2 Project Preparation and Approval	1. Detailed project plan documents for at least two projects (including likely impact of technical, financial, economic, social, environmental, and legal aspects of the project at the appraisal stage itself) and assessment study of likely risks and corresponding mitigation plans 2. Details of the project approval process/procedure within the entity along with the formats and approval levels 3. Two samples of project appraisals undertaken in the last 12 to 18 months 4. Policy and/or other published document(s) that outline the risk assessment procedures/framework 5. Two samples of completed project appraisals with identified risks and corresponding mitigation strategies/plans

	The two samples of project documents which demonstrate this capability can be for the same projects for all the aspects of this capability
2.3 Project Implementation Planning and Quality-at-entry Review	1. Operational manual or written procedures for project review system during the design phase 2. Sample documents of actual review done for at least 2 projects 3. Samples of project budgets
2.4 Project Monitoring and Evaluation	1. Policy or other published document that outlines monitoring and evaluation requirements 2. Detailed procedures and formats used for monitoring and evaluation during project implementation 3. Procedures for project-at-risk system or similar process/system to ensure speedy solutions to problems which may interfere with the achievement of the project objectives 4. Sample project monitoring and evaluation reports 5. Sample of project accounts 6. Sample of project audit reports 7. Analysis of project expenditure vs budget
2.5 Project Closure and Final Evaluation	1. Project closure reports or independent evaluation reports containing assessment of the impact/implications of the technical, financial, economic, social, environmental, and legal aspects of projects 2. Independent evaluation reports of completed projects/programmes
3. Transparency, Self-investigative Powers, and Anti-corruption Measures	
A. Criteria	*B. Required Supporting Documents* *C.*
3.1 Handling Financial Mismanagement and other Malpractices	1. A policy of zero tolerance for fraud, financial mismanagement and other forms of malpractice and its dissemination 2. Documented code of conduct/ethics applicable to staff and associates 3. Documentation establishing avenues for reporting non-compliance/violation/misconduct and business conduct concerns 4. An avenue for reporting frauds/corruption/ complaints must also be available from home page on the organization's website 5. Details of policies and procedures relating to managing conflict of interest and whistle blower

	protection 6. The structure and process/procedures within the organization to handle cases of fraud and mismanagement and undertake necessary investigative activities 7. Data on cases of violation of code of conduct/ethics and frauds reported in terms of number of cases, types of violations and summary of status/action taken 8. System for oversight of the ethics function