

# Oxford Energy and Environment Comment

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## One Step Forward, Two Steps Back?

### The Governance of the World Bank Climate Investment Funds

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On the 2<sup>nd</sup> of March 2005 over one-hundred countries, as well as representative from the World Bank, the Regional Development Banks (RDBs), and the OECD Development Assistance Committee (DAC) committed themselves “to a practical blueprint to provide aid in more streamlined ways that better meet the needs of developing countries”<sup>iii</sup> by issuing the

*Paris Declaration on Aid Effectiveness:*

Ownership, Harmonisation, Alignment, Results and mutual Accountability<sup>iv</sup>

The Declaration has some 50 commitments by both OECD (‘donor’) and developing (‘partner’) countries to improve the quality and effectiveness of Official Development Assistance (ODA), mainly through ‘mainstreaming’ ODA into domestic development strategies. And the key message of the Declaration is that this can only be done if the recipient partner countries can exercise genuine ownership over the process. Among the only two people mentioned in the press release on the Declaration was then World Bank president James Wolfensohn, who was quoted as having said that “we know what needs to be done. With the Paris Declaration, we have the blueprint to do it.”

Three years later, the World Bank – together with the RDBs – has begun a process of consultation to establish a ‘portfolio of strategic Climate Investment Funds [CIFs]. The overall objectives of the funds will be to provide concessional finance for policy reforms and investments that achieve development goals through a transition to a low carbon development path and climate-resilient economy’<sup>v</sup>

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The proposed portfolio is initially meant to include three new investment funds: a *Clean Technology Fund* (Target size US\$5-10bn); a \$1bn *Forest Investment Fund*, and a \$1bn *Adaptation Pilot Fund*, to be replenished either directly or through another new ‘transformation’ fund. Among the aims of the CIFs is to ‘pilot innovative approaches and ideas ... through learning-by-doing that could inform and support a successful outcome to the post-2012 framework negotiations.

Notwithstanding the fact that most developing countries would reject the idea that the post-2012 deliberations are ‘framework negotiations’ – for them, the framework is, and is meant to remain, the UN Framework Convention on Climate Change – this World Bank initiative would seem to be very much in line with the thinking of many of the envisaged recipient countries of these funds. After all, ‘learning-by-doing’ activities has been a long standing demand of most developing countries, particularly in the context of the *Clean Development Mechanism* and the *Nairobi work programme on impacts, vulnerability and adaptation to climate change*.<sup>vi</sup>

This initiative could, in particular, be the beginning of the long-awaited serious collaboration between developed and developing countries to fight climate change through new and additional funding in the spirit of Art 4.7 of the Convention as reflected in the twin-aims of Para. 1.b.ii of the Bali Road Map of combining measurable, reportable, and verifiable mitigation actions by developing countries with measurable, reportable, and verifiable financing and technology transfer from developed ones.

Both the Paris declaration and the WB initiative are ultimately aimed at mainstreaming certain policies in developing countries. The rationales put forward for all three CIFs are quite explicit on this:

- ***Clean Technology Fund***: “There is a gap in the international ODA architecture for finance to developing countries at more concessional rates than the standard MDB terms and at the scale necessary to help provide them incentives to integrate low-carbon strategies into their development plans and investment decisions”
- ***Forest Investment Fund*** “mitigation and adaptation strategies need to become an integral part of national forest policies and international efforts addressing climate change”
- ***Adaptation Pilot Fund***: “We need to transform the way adaptation is approached and financed in developing countries, from being a standalone issue to being one which is fully integrated with core development planning and budgeting.”

The problem, in our opinion is that the World Bank tries to do so with complete disregard of the lessons reflected in the Paris Declaration. This is not only apparent in what does come across as a somewhat paternalistic tone in the blueprint (‘We need to transform ... developing countries’) but much more seriously in the proposed governance structure for the CIFs. We feel that the many elements of the blueprint which are worthy of success will be unnecessarily doomed to failure if these governance shortcomings are not rectified speedily and whole-heartedly.

Indeed, our fears are grounded not just in our belief that the spirit of the Paris Declaration – with its emphasis on partnership and mutual ownership of the process – is the only way to achieve the desired mainstreaming of ODA, but in the fact that the sort of climate change funding envisaged by the World Bank funds are generally not considered to be ODA. They are meant to be additional to ODA, reflecting the principle of common but differentiated responsibility. Accordingly, many, if not most developing countries, regard themselves as entitled to receive this sort of assistance, which is why it is even more important than in the case of ODA that they should take ownership of the respective

funding processes. As a matter of fact, the recently completed negotiations on the Kyoto Protocol's Adaptation Fund are a good example of what can happen in the context of climate change financing when this ownership is missing.

### **One step forward ...**

The Adaptation Fund is based on a levy on the Clean Development Mechanism (CDM) established under the Kyoto Protocol in 1997. However, the negotiations of how this fund was to be operationalised and governed had to wait until the first Session of Kyoto Protocol governing body (CMP.1<sup>vii</sup>) in Montreal, after the entry into force of the Kyoto Protocol in 2005, by which time two other funds had been created (2000) under the financial mechanism of the UN Framework Convention on Climate Change, both operated by the Global Environment Facility (GEF), located in Washington as it was originally “established in the International Bank for Reconstruction and Development (IBRD or World Bank) as a pilot program in order to assist in the protection of the global environment”<sup>viii</sup>.

At Montreal, many (particularly industrialised) countries thought that the most natural candidate for running the AF would again be the GEF, given its track record and a reluctance to proliferate organisational entities. And yet, it was that track record, particularly with respect to the two Convention funds, which in the eyes of many developing countries was not satisfactory, that led the debate on operationalising the AF to be a debate on the merits and demerits of the GEF and its governance structure.

Many developing countries felt very little if any ownership over the GEF, which they saw as dominated by donor concerns, and disregarding guidance by the UNFCCC Conference of Parties (COP). This dissatisfaction led, in a first instance, to the rather unusual revision of a decision by the CMP at its second meeting in Nairobi which was only adopted at the preceding Montreal session, namely the explicit inclusion or the requirement that the AF should be under the ‘authority’ of the CMP, in addition to the traditional ‘being under the guidance of and accountable to’. The Nairobi decision also adopted “a one-country-one-vote” rule and a majority representation for developing countries on the governing body.<sup>ix</sup> This was a fundamental departure from the previous arrangements for climate change funds, where donors – due to the GEF mixed voting system – had an implicit veto.<sup>x</sup>

At the most recent Session of the CMP in Bali/Indonesia (November 2007), this dissatisfaction was re-confirmed, not least in a Statement by Marthinus Van Schalkwyk, the Minister of Environmental Affairs and Tourism of South Africa, who led the AF negotiations on behalf of the G77+China:

“Our cabinet mandate was to establish a transparent and fair governance regime under an Adaptation Fund Board [...] Our aim was also to ensure that this fund will be exempt from the decision-making procedures of the GEF, to give developing countries a more direct and equitable voice in how funds are prioritised and spent.

The possibility of direct access to the Adaptation Fund by eligible parties was of major concern for the Group of 77. The G77 did not want to continue a process where they would be forced to use implementing agencies. After agreeing to include criteria relating to financial responsibility and the ability to deliver the projects, it was agreed that eligible countries will have direct access to the Fund.

The appointment of a secretariat and trustee was of the most contentious aspects of the decision, given the negative experiences that most developing countries have with their interaction with the GEF and the World Bank in respect of the funding of climate related projects.”

In the end, the CMP actually did decide in Bali to create a completely new operating entity – in addition to the GEF – called the *Adaptation Fund Board* (AFB), with a majority of members/alternates from developing countries, and designated representation from the two main recipient interest groups, the Group of Least Developed Countries, and the Alliance of Small Island States. Moreover, it was decided that Parties should have direct access, and the involvement of the GEF and the World Bank in the running of the AF was reduced to an interim provision of secretariat and trustee services, respectively. Indeed, to avoid any possible confusion with the other operating entity of the UN financial mechanisms for climate change, it was also decided that AFB is to meet at the seat of the UNFCCC Secretariat in Bonn/Germany.

Not surprisingly, therefore, the assessment of Minister Van Schalkwyk of the Bali Adaptation Fund Decision: “The decision constitutes a major victory for the developing world in setting in place a new governance system for funding of adaptation activities.” What is surprising is that news of this does not seem to have reached 1818 H Street in Washington (headquarters of both the World Bank and the GEF).

### **... two steps back?**

One, if not *the* key problem with the current blueprint for the World Bank Climate Investment Funds – not only from a developing country perspective – is the proposed governance structure, which makes that of the GEF look positively progressive.<sup>xi</sup> Indeed, compared to that of the Adaptation Fund, it is a huge leap backwards.

According to the 22 January version of the blueprint, each investment fund would have an independent governance structure which has ultimate control over that fund [§6]. The governance of each fund would be exercised through a dedicated Trust Fund Committee (TFC), *comprised of donors to the particular fund*, who decide on who will represent them [§§6, 17]. § 17 also posits a minimum contribution, the level of which is “to be decided”, meaning that small donor countries could well be kept out of the governance of the funds.

The envisaged interaction with recipients and stakeholders is described [§11] as the possibility that “donors of all funds could convene an annual outreach forum to bring together donors, recipients and stakeholders. The outreach forum would provide an opportunity to exchange views on policy issues affecting the investment funds and other activities.” In other words, developing countries and NGO, if they are lucky, might get invited once a year to find out what is going on.

The remaining articles on how these CIFs would be governed/managed begin with the proposal that the World Bank would host a secretariat for these funds [§12], and that it would serve as the trustee [§13]. Decision making would essentially be by consensus [§18], that the TFCs “would meet at a senior level once or twice a year, depending on business needs”[§20]. Towards the end, the blueprint discusses the fees for the Secretariat and the Trustee (to be “based on cost rather than a percentage of the resources held in the fund” [§28], before turning to ‘issues that will require further elaboration’ [§29]. The third issue listed – just after “(ii) who should Chair the meetings of the Trust Fund Committee?” is:

- “(iii) who would be invited as observers to the Trust Fund Committee? Voice of recipient countries in the governance structure?”

It should be encouraging to see that the issue of giving the recipient countries a voice in the governance structure of these new World Bank funds is still seen as requiring further elaboration, although the signs that this will be given the prominence needed for this initiative to succeed are unfortunately not auspicious.

Will the World Bank, or rather the key donors thus far consulted (Japan, UK, US) be able and willing to leap forward in their proposal for the governance of the envisaged funds by including developing countries as equal partners in the spirit of the OECD Paris Declaration?

We are not asking the World Bank and the other initiators of this potentially valuable initiative to perform a 'great leap forward' – all we hope is that there is still time to prevent a leap in the opposite direction that would be unhelpful to absolutely everybody. After all it stands to reason that the funding channelled through these funds, particularly the Clean Technology Fund, will benefit their own industries at least as much as they will benefit the participating developing countries.

In particular, will the UK and Japan, and perhaps even the US under a new administration, be able to embrace the partnership that has been established in the Kyoto Protocol Adaptation Fund? For one, the overall rationale for the proposed CIF Adaptation Pilot Fund – namely to integrate adaptation as 'an integral part of national and sectoral development plans' – is not incompatible with the remit of the Adaptation Fund, but could easily be integrated as a 'Policy Adaptation Programme,' particularly if donors are willing to fund these sorts of activities. As such it would complement the project based activities of the Adaptation Fund funded through the CDEM levy, thus enabling it to take a truly 360° view of adaptation.

The question is therefore whether the donor community is willing to provide the start-up money for such a Programme under the Adaptation Fund? Or will they choose to further erode trust by contributing to an unnecessary proliferation of adaptation funds under a governance structure wholly unacceptable to the large majority of countries in the world?

## Endnotes

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<sup>iii</sup> OECD, "International community holds itself accountable for better use of aid" Press release, Paris: 2 March 2005, <http://www.oecd.org/dataoecd/11/23/34570799.pdf>

<sup>iv</sup> <http://www.oecd.org/dataoecd/11/41/34428351.pdf>

<sup>v</sup> World Bank, *Consultation Draft on Climate Investment Funds*, 22 January 2008. All quotes in this article, unless otherwise indicated, are from this document.

<sup>vi</sup> [http://unfccc.int/adaptation/sbsta\\_agenda\\_item\\_adaptation/items/3633.php](http://unfccc.int/adaptation/sbsta_agenda_item_adaptation/items/3633.php)

<sup>vii</sup> Conference of Parties serving as Meeting of the Parties to the Kyoto Protocol.

<sup>viii</sup> GEF, *Instrument for the Establishment of the Restructured, Global Environment Facility*, Preamble.

<sup>ix</sup> Decision 5/CMP.2, para. 3.

<sup>x</sup> The GEF voting procedures requires a dual majority of 60% of countries and 60% of donations for a vote to pass, which would have provided the group of largest donors with a *de facto* veto. However, there never has been a vote in the history of the GEF since its inception in 1991, arguably at least in part due to the implicit veto power inherent in this sort of money vote.

<sup>xi</sup> To be sure, there are likely to be other issues that, given the recent debate on the operationalisation of the Adaptation Fund, are likely to prove controversial, not least the fact that (i) funds are meant to 'focus on countries with the greatest potential for transformation towards low carbon or climate-resilient development'

which – together with the “list of current GHG emissions and trends” (§ 31.iv) – is strongly reminiscent of the *GEF Resource Allocation Framework*, or that (ii) the funds will rely implementing agencies, such as the Bank’s private sector International Finance Corporation ([www.ifc.org](http://www.ifc.org)). But our main concern in this context is primarily with the proposed structure of governance.