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The Time is Right!

Devolution of funding decisions to designated national/regional climate change funding entities

by Benito Müller[1]

The Issues

At the heart of any financial architecture debate is the question: ***who decides who gets how much and for what purpose?*** In the context of climate finance for developing countries, this can be interpreted at a macro- and a micro-level. The macro decision is about how much each country gets, and for what specialized theme.[2] The micro decision is about approving of specific activities to be funded. As it is useful to distinguish the two, this Comment uses the term '***financing***' for the macro-level decisions and '***funding***' for micro-level ones.[3] Whereas *financing* in the climate change context is mainly an issue of distributive justice between countries[4] and of thematic balance,[5] *funding* is more about appropriateness, effectiveness, accountability, and efficiency.

This Comment discusses the need to ***devolve funding decisions to national*** (or, if more appropriate, regional) ***designated funding entities***. It is about the rationale for devolving funding decisions to the recipients, as well as the need for joined-up decision-making at the recipient end.

The most straight-forward argument in favour of devolving funding decisions to the recipient countries is based on the fact that the amount of (public sector) money required is in the upper tens of billions of €/$, and that the final processing – i.e. the evaluation and approval of projects/programmes etc. – of this amount of funding will require ***many thousands of people***. It would be immensely inefficient to build or bolster the necessary infrastructure for taking these decisions at the international level, irrespective of whether the decisions are taken by one central (new) entity or a handful of existing ones. Indeed, given the prevailing pay scales, the tax payers in contributing countries might also reject the idea of hiring yet more civil servants at home if the job can be done much more cost-effectively in the recipient countries. In short, there is a ***transaction cost argument*** against retaining funding decisions either at the bilateral or multilateral payer end which, given the total size of the transactions becomes compelling. But it is by no means the only argument for the devolution of funding decisions.

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Autonomous Development Funds

The idea of devolving decision-making related to international funding to national hubs is by no means new. Over a decade ago, a similar idea was put forward by two civil society organizations in the context of ODA. It is illuminating to review the benefits of such devolution that were put forward by them.

The Swedish Dag Hammarskjöld Foundation and African Association for Public Administration and Management proposed the idea of African ***Autonomous Development Funds*** (ADF) in 1995. The model envisaged a public but politically independent institution, catering for both government and civil society. ADFs were meant to be ***funding, not implementing, entities*** with a national scope, aggregating finance from a variety of sources. The ADFs were proposed in response to the following concerns and conclusions:

- The delivery mode and a relationship of trust are *a critical variable*[s] *in determining the effectiveness of foreign aid*.
- Donors need to give up the idea *that the more control they have over the preparation of a given project the more likely it is that the project will yield positive results. What is needed is a modification of this process so that donor coordination takes place in response to the demands of recipient institutions.*
- [D]*evelopment funding must be available not only at the central level of government but also at lower levels. The central control of decision-making, information flow and resource allocation can be broken if local institutions, including local government, are able to enhance their financial autonomy vis-à-vis central government.*

Established as national institutions with a specific sectoral mandate, the ADFs were meant to dispense money within the context of national policy to organisations applying for their resources on a competitive basis. They were to be run by boards of trustees, including representatives of government, donors and civil society. To secure their operational autonomy, the ADFs were to have their own capital base, raised from external donor sources as well as domestically through donations and fund-raising activities. The overall aim of the ADFs was *to encourage greater innovativeness and **effectiveness** in the use of development resources*, by complementing existing transfer mechanisms (such as *direct resource transfer to governments or non-governmental organisations*).

The idea of ADFs failed to generate the necessary support and interest, with the last major workshop on the topic held in Tanzania in February 1997.[6]

The Emergence of National Climate Change Trust Funds

Over the past decade, the times have clearly changed. While the idea of national funding entities was initially proposed by some enlightened CSOs, they are now emerging as government-backed realities on the ground in the context of climate change funding and finance. Bangladesh and Indonesia, for example, have put forward plans for establishing such national trust funds.

In September 2008, the Government of Bangladesh (GOB) launched its *Climate Change Strategy and Action Plan* (CCSAP). To scale up financing to meet the needs of this Strategy, GOB is now establishing a national ***Multi-Donor Trust Fund for Climate Change*** (MDTF). The MDTF is designed to be a 'one-stop' mechanism for large scale climate change funding in Bangladesh. The benefits of having such a mechanism are seen to be *high-level coordination, elimination of overlaps,*

donor harmonization, flexibility in fund management, transparency, and the possibility of attracting additional funds from both local and external sources.

The MDTF is to have two windows: an ***on-budget window*** for funding public sector projects ('budget support'); and, an ***off-budget window*** for funding projects from civil society. All projects funded through the MDTF will be rigorously reviewed to ensure consistency with the priorities laid out in the CCSAP. (For more on the institutional arrangements of the MDTF, see Müller and Echeverri 2009,[7] Section 7.2)

The Government of Indonesia (GOI) is currently developing a 20 year *Climate Change Sectoral Roadmap* (CCSR), and is in the process of establishing a dedicated funding vehicle known as ***Indonesia Climate Change Trust Fund*** (ICCTF) to address the emerging and immediate needs of CCSR program investments. The ICCTF in designed to link the international architecture for climate change with national investment strategies, with the aim of becoming a showcase of innovative climate change financing owned by government, in an efficient, transparent and accountable manner.

The reason for choosing the national trust fund model for these purposes was that it is viewed as the ***most suitable instrument to reduce transaction costs*** by reducing the number of free-standing projects and programs, and by harmonizing the financing into "basket funds". Owned and managed by the government, the creation of this fund is fully consistent with the government efforts to strengthen the effectiveness of ***national ownership over development*** as outlined under the Jakarta Commitment of 2008.

The design of the ICCTF is guided by a number of principles. The ICCTF is to ***mainstream*** not only ***sustainable development***, but ***good governance***, as well as ***civil society participation*** and ***local community empowerment***. It is to ensure that all eligible Indonesian institutions have ***access in a balanced and equitable manner***. The funding of activities is to be ***country-driven***, taking in particular account of ***national development plans***. The governance is to be ***transparent*** and ***open***, with independent monitoring, evaluation and financial audits (including the use of ***international fiduciary standards***).

The ICCTF is likely to cover two funding mechanisms. The first is an ***Innovation Fund***, to be replenished through bi- and multilateral non-refundable contributions. It is to be used for activities with indirect economic and social benefits that will not provide any direct financial return to the participants.

In a second stage, a ***Transformation Fund*** may be introduced where funding sources such as domestic funds, loans, all the international funds under the UNFCCC, and the world capital market would generate direct financial revenues and support stakeholders including both the government and private sectors, in mobilizing investment in a low-carbon economic development path.

Conclusions and Way Forward

The idea has been around for some time that if funding is ***to be mainstreamed effectively*** into recipient country policy, then it must be handled through dedicated national funding entities. However, it is only now − in the context of climate change − that it is being implemented (on developing country initiative). Recipient countries are realizing that they will not be able to provide the financial support for the domestic climate change activities in an ***adequate, efficient***, and ***effective*** manner without such national funding entities. As far as they are concerned, the time is clearly right for the idea of consolidated national funding, quite independently of the degree of consolidation of the

international climate finance regime.[8] What is needed now is the support of the international community, and, in particular, of the financial regime of the UNFCCC, as envisaged in the language submitted to the AWG-LCA by India.[9]

It should be stressed that countries should not be coerced into establishing national trust funds, and that consequently the international regime should be able to accommodate those who are unable or unwilling to do so.[10] What it must do is ***encourage countries to establish such designated national*** (or, where more appropriate, regional[11]) ***climate change funding bodies***, by assuring that they will be adequately provided for under the international finance regime. And it must acknowledge that these bodies will have the authority ***not only to make plans, but to spend the funds*** thus provided.

As concerns institutional and governance arrangements, the RFM model, for example, envisages that the Executive Board of the (Reformed) Financial Mechanism of the Convention would develop (i) ***criteria for disbursing funds*** to the national/regional funding bodies for each of the thematic windows, (ii) ***accreditation criteria*** for designated funding bodies, and (iii) ***international fiduciary standards*** (as envisaged in the Indonesia Climate Change Trust Fund). To address the latter two, one could simply adopt the criteria and standards adopted by the Adaptation Fund Board. Indeed, by introducing ***National Implementing Entities***, the Adaptation Fund Board may well have paved the way for the idea of designated funding entities even ***at the international level***. In other words, the time may actually be doubly right! It is now up to the international community in the shape of the UNFCCC COP to seize the day by following the Indian lead and create an ***overall architecture*** for climate change funding and finance, which is ***fit for purpose***.

Endnotes

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2. Climate change 'themes', such as mitigation, adaptation, technology transfer, and capacity building.
3. In other words, 'funding decisions' are meant to be the sort of decisions typically involved in approving and managing activities (projects/programmes).
4. Ensuring that no one has to contribute more than, and everyone receives their fair share.
5. Ensuring that there is not an inordinate imbalance in financing between the themes.
6. A "Donor Seminar" which was to follow that meeting never materialized because of the participating four African country teams "encountered considerable problems" in formulating their proposals.
7. Benito Müller and Luis Gomez-Echeverri, *The Reformed Financial Mechanism of the UNFCCC. Part I: Architecture and Governance*, Oxford Institute for Energy Studies Background Paper EV45, April 2009. Avaialble at http://www.oxfordclimatepolicy.org/publications/mueller.html
8. The time is right whether or not the future international regime becomes more consolidated or remains in its current fragmented state. The main rationale for introducing these national funding hubs is their domestic effectiveness, particularly in mainstreaming climate change into national policies.
9. *x.9 The national entities, designated by the developing country Parties, shall approve funding for projects, programs, actions, subject to the guidelines and procedures established by the specialized thematic assessment units duly approved by the Executive Board. The thematic assessment units under the Executive Board shall carry out the relevant assessments for disbursement of funds to the designated national entities under their respective specialized funding windows.*
   x.12 The designated national funding entities could also accept contributions directly, as per guidelines agreed in the COP, from and facilitate linkages with other private or official national, regional, subregional, international bodies and/or stakeholders that may seek to implement actions relating to mitigation, adaptation and technology transfer and related activities directly.[FCCC/AWGLCA/2009/INF.1:p.159]
10. On how this might be achieved, see Benito Müller, *Is There Room for Compromise? The debate on institutional arrangements for climate finance*. Oxford Energy and Environment Comment, October 2009.
11. The fact is that for some very small countries, it might make more sense to have a 'regional' designated funding entity, rather than a national one for each.