



Email: twnet@po.jaring.my

Website: www.twinside.org.sg

Address: 131 Jalan Macalister, 10400 Penang, MALAYSIA

Tel: 60-4-2266728/2266159 Fax: 60-4-2264505

Third World Network

World Bank's Climate Funds Will Undermine Global Climate Action*

Celine Tan, Third World Network
10 April 2008

The World Bank will be holding a key two-day meeting in Washington DC next week to move forward plans to establish its proposed portfolio of climate investment funds (CIFs) projected at in time for the G8 summit in Japan in July. According to a statement on the Bank's website by Kathy Sierra, the Bank's vice-president of Sustainable Development, the aim of next week's meeting 'is to work out details of how, when, and where to funnel new donor financing to projects that will have a transformational impact, at scale, in developing countries struggling with climate change'.

The proposed funds have come under fire from developing countries and civil society since details of the proposal to establish the funds were leaked in February this year. Developing countries under the Group of 77 and China attacked the Bank's initiative at last week's Bangkok meeting of the UN Convention on Climate Change (UNFCCC). The group argued that the proposed funds, especially in such significant amounts, should come under the direction of the UNFCCC, instead of being diverted to the Bank, and that the Bank's initiative could undermine ongoing UNFCCC negotiations on financial resources.

The Bank's proposal is also heavily criticised by civil society groups, which see it as a move to wrestle control of billions of dollars of funds in an attempt to reinvent itself, at the expense of other more suitable institutions. These proposed funds are also criticised for the significant speed at which they have been designed, promoted and implemented without due consultation with wider stakeholders. Although plans for the funds have been in the pipeline since last year and proposed documents have been circulating internally at the Bank and within donor governments since early this year, the proposals were only made public by the Bank last week

The stated aims of these funds are to 'scale up financing available for policy reforms and investments that achieve sustainable development goals through a transition to a low-carbon path and climate

* This paper is an abridged and updated version of the paper 'No Additionality, New Conditionality: A Critique of the World Bank's Proposed Climate Investment Funds', *TWN Briefing Paper No 5 for the Bangkok Climate Change Talks, 31 March - 4 April 2008*. The full paper is available at <http://www.twinside.org.sg/bangkok.briefings.htm> but please note that the original paper was based on earlier drafts of the Bank proposals.

resilient economy'. They will finance public and private activities ranging from 'clean technology' to 'sustainable forest management' to 'piloting the integration of climate resilience into development plans and budgets'.

Although the recent documents on the funds address some of the criticisms directed at the CIFs, they do not address the fundamental problems with the establishment of this portfolio of funds under the auspices of the World Bank and through what remains an essentially donor-led process outside ongoing multilateral negotiations on climate change.

1. New Mission for the Bank

Initially, the World Bank had proposed the creation of three specific funds – a Clean Technology Fund (CTF) (with a target size of between US\$5 – 10 billion), a Forest Investment Fund (US\$300 – 500 million) and an Adaptation Pilot Fund (US\$300 – 500 million) – along with a Strategic Climate Fund (SCF) which would be established as an umbrella vehicle for the receipt of donor funds and disbursements to specific funds and programmes aimed at piloting new development approaches or scaling up activities aimed a specific climate change challenge or sectoral response.

Currently, plans have moved towards the immediate establishment of the CTF and the SCF with the possibility of creating a Forest Investment Fund in late 2008 or early 2009. The Adaptation Pilot Fund, renamed the Climate Resilience Pilot Programme, will be established as a programme under the SCF framework at the outset although it will have a separate oversight committee.

The climate investment funds are to be established as trust funds through the World Bank's Multilateral Trusteeship and Innovative Financing Department (MTIF) under its Concessional Finance and Global Partnerships Vice-Presidency and the Bank will act as 'overall coordinator for the CIF partnership'.

The CIFs will serve as the central instruments through which donor resources are collected and disbursed for climate-related financing to the various multilateral development banks (MDBs), including the World Bank Group. Resources from the CIFs will, in effect, subsidise the financing made by the MDBs to developing countries for climate-related activities, including co-financing arrangements with the MDBs and buying down of interest and repayments on MDB loans to increase the concessionality of financing for the projects.

These funds are the latest efforts on the part of the World Bank to capitalise on current global concerns with climate change and form a key pillar of its larger proposed strategic framework on climate change. In contrast to previous financing initiatives, these proposed funds are expected to attract significant donor support. The combined target size of the CIFs almost exceeds the combined total of funds held in existing trust funds administered by the Bank. In 2006, the total funds held in trust by the Bank were US\$10.3 billion while the target size of the proposed CTF alone is between US\$5 and US\$10 billion.

2. Bank Funds under Fire

The climate investment funds have come under heavy fire from developing countries and civil society, worsened by the speed and stealth in which their process of design took place. At the climate change talks in Bangkok last week, developing countries expressed regret that the funds were

designed without guidance from parties to the UNFCCC, without due transparency and are at risk of undermining efforts and commitments of the international climate change regime.

In particular, developing countries questioned the transparency of the process of designing and implementing the proposals for the funds which took place outside the UNFCCC negotiating framework and expressed concern that the sizeable amount of resources the funds are targeting from donor countries threatens to dwarf and divert away resources available under existing financing mechanisms of the Convention. ‘There is clearly money for climate actions, which is the good news, but the bad news is it is in the hands of institutions that do not necessarily serve the objectives of the Convention,’ said Bernaditas Muller, chief negotiator for the Group of 77 developing countries and China, at the climate talks last week.

In light of significant criticism of the funds since their announcement, the Bank’s latest documents on the CIFs have stressed their consistency with international climate regime principles and deference to the United Nations as the pre-eminent body for agenda-setting for international climate change policy and regulation. The Bank is claiming that the establishment of these funds sit consistently within the long-term cooperative action programme of the Bali Action Plan adopted at the 13th session of the UNFCCC Conference of Parties last year. There has also been some revision to the proposed governance structure of the funds incorporating some developing country participation.

However, in spite of the conciliatory tone of the revised proposals for the climate investment funds, these changes do not resolve the fundamental contradictions and inherent problems associated with their design and proposed implementation. Furthermore, the compressed timeframe in which these funds are being conceptualised and operationalised, especially at a critical juncture where negotiations are ongoing within the UN to develop financial mechanisms within the international climate change regime, raises significant questions as to the motivations of the World Bank and the donor country proponents of the funds.

3. Donor-Driven Process

The design process for these funds has remained a donor-driven endeavour, shaped by the most part by World Bank staff and stemming from the institution’s dialogue with and building upon the early initiatives of a tripartite of G8 countries – the UK, US and Japan. Developing countries and civil society have been marginalised from the design of the CIFs so far and any inclusion of developing countries into the management or governance structure of the funds now will only be ring-fenced around existing operational plans.

While there has been some changes to the proposed governance structure of the CIFs, notably that the Trust Fund Committees which will oversee the funds will now consist of representatives from *both* donor and recipient countries identified through consultation with respective countries, there is no guarantee that this representation will translate into *actual voice (or decision-making powers)* on the committees.

It is still expected that the composition of donor representatives will remain primarily guided by their total contributions. There is no agreement as yet on what the decision-making structure of the CIFs would look like as physical representation at the Board may not necessarily translate into equality in voice on the committees.

Although initially, the Bank had proposed that decision-making will be by ‘consensus’, the new CTF proposal for example note that this is merely the ‘first principle’ for decision-making and suggest that the ‘alternative’ where consensus is not achieved is that a vote is taken ‘in accordance with agreed procedures for voting’ which have yet to be determined. Several options for such voting procedures have been tabled, including one based either on the number of seats at the committee (one seat, one vote), or based on contributions to the fund, or a hybrid system. There remains no provision for the engagement of civil society within the decision-making process.

The fact that the meetings next week are aimed at ‘moving ahead with the creation of these new trust funds’ demonstrates that the Bank is paying little heed to concerns that the funds are being created without adequate consultation with stakeholders and study as to the appropriateness of their design and proposed implementation. The short timeline in which these funds are being pushed forward have limited not only the consultation period but also the actors involved in their design.

Moreover, the design of the CIFs remain premised on an aid framework for climate change financing which places the parties to the financing in a donor-donee relationship contrary to international climate change principles and obligations. Financial resources for climate change should be provided as part of developed countries’ obligations under the international climate change regimes and should not be considered as donor funds.

Therefore, disbursement of financial resources through a donor-driven facility based on the principle of conditionality is contrary to multilaterally negotiated commitments of the developed country contributors to these funds, particularly if the resources provided to the CIFs by these countries will not constitute any additional resources to funds set aside to meet these or other internationally agreed development obligations.

Civil society groups are particularly concerned that existing resources would be diverted from existing official development assistance (ODA) towards the CIFs thus risking financing of other key development areas, notably those aimed at achieving the Millennium Development Goals (MDGs).

4. Initiative ignores ‘Polluter Pays’ and Other Climate Principles

The climate investment funds will be providing *loans* as well as grants to eligible developing countries. This means that developing countries will have to *pay* for dealing with a problem that has been caused by developed countries while at the same time facing other major developmental challenges. This comes at a time when many developing countries, due to debt relief initiatives and rising commodity prices, are beginning to shake off the shackles of debt which have circumscribed their social and economic development for almost three decades.

The framework of the CIFS would therefore appear to contradict internationally agreed principles on climate change, in particular that of the UNFCCC and Kyoto Protocol regime which state that, as historical polluters and due to their higher technological and economic capabilities, developed countries should shoulder the main burden for resolving the crisis (see UNFCCC, Articles 3 and 4).

While the loans under the CIFs will be provided on a concessional basis, these loans are also expected to be ring-fenced around specific projects and programmes and will have to be repaid in the future by developing countries. Given that many developing countries will continue to be reliant

on external financing for other aspects of development financing, loans will only add to their debt burden in the long run and affect their ability to generate sustainable resources for long-term economic growth and development.

Furthermore, the conditionalities attached to the loans and grants under the CIFs may also have the effect of extracting emissions targets and other commitments from developing countries outside the multilateral framework of negotiations. In order to secure financing, developing countries must demonstrate that they have, among other things, an enabling regulatory framework in place to achieve a low-carbon development path. This is contrary to the UNFCCC regime which emphasises that implementation of commitments by countries is contingent upon the availability of financing and technology and not the other way around.

5. New Conditionality

Access to resources under the CIFs will be contingent upon recipient countries fulfilling the criteria of the respective trust funds, that is, adopting Bank and donor conditions in exchange for financing. Eligible countries will have to submit ‘country investment strategies’ which will be assessed by the respective Trust Fund Committees. Guidelines for accessing financing will be drawn up by the CIF secretariat and will also be based on existing World Bank and/or other MDB policies.

Implementation of the projects and programmes financed by the CIFs will be the responsibility of the implementing MDB, including the World Bank. This means that while the overall oversight committees of the funds (known as trust fund committees) may decide on the programming priorities and financing modalities for the CIFs, the development and management of individual funded projects and programmes will be the responsibility of the MDBs and be reliant on their own policies and procedures for disbursement of resources.

Under the Clean Technology Fund, for example, the MDBs (including the World Bank) involved in financing under a particular country programme will determine the eligibility criteria and priorities for each of the investment operations under its portfolio. In the case of the World Bank, all operations financed by the CTF ‘will follow the Bank’s operational policies and procedures for investment lending’ regardless of whether there is IBRD or IDA co-financing’.

This means that aside from specific climate-related criteria, access to the CIFs may also be based on the Bank’s traditional criteria for financing, including tight fiscal discipline and implementation of economic and other structural and policy reforms. The Bank’s track record in managing other trust funds, including the HIPC Trust Fund demonstrates that it has significant leverage over determining the conditions for access and use of resources by recipient countries, including the imposition of policy conditionalities which may not necessary be relevant to the objectives of the trusts administered.

The same goes for the other MDBs which act as implementing agencies of the resources held by the CIFs who may subject recipient countries to different financing conditionalities, including compliance with the guidelines of the Paris Declaration on Aid Effectiveness, another donor-driven framework for aid disbursement and management. This goes against the principles decided under the UNFCCC which stipulate that any funds established for the purposes of meeting the financial commitments of the Convention must be consistent with the objectives of the Convention and must not impose additional conditionalities on the recipients.

There is also a danger that the climate investment funds will create onerous obligations on developing countries to comply with emissions targets and other rules under the international climate change regime for which they have been exempt on grounds of their differing responsibilities and capacities. As discussed above, access to financing under the CIFs will be contingent upon countries' demonstrated readiness to transit to a low-carbon economy and there appears to be no provision for assessing what impact such a transition will have on a country's overall development and efforts for poverty reduction in the context of other extenuating economic factors.

This enforcement through the back door through financing conditions once again goes against the principles underpinning the UNFCCC and the Kyoto Protocol which are based on developing countries' having obligations that are non-binding in recognition not only of their lower financing and technological capabilities, but also of their negligible historical role in the build up of greenhouse gases and their continued need for social and economic development.

6. Parallel Structures

The World Bank's climate investment funds will create parallel structures for financing climate change adaptation and mitigation outside the ongoing multilateral framework for climate change negotiations and within a process dominated by G8 countries. Developing countries have long argued for greater commitments and increases in financial resources under the UNFCCC to enable them to fulfil their obligations under the Convention but have maintained that such resources should be placed under the guidance of the state parties to the Convention to ensure consistency with internationally agreed priorities and principles.

The World Bank maintains that the UNFCCC stipulates that the obligations of developed countries under the UNFCCC to provide financial resources to developing countries to enable them to fulfil their obligations under the Convention may be satisfied through the provision of funds via 'bilateral, regional and other multilateral channels' (under Article 11(5) of the UNFCCC).

However, under the current UNFCCC negotiations on long-term cooperative action, only financial resources that are taken up within the auspices of the Convention with the coherent guidance of *all* the signatory parties to the Convention and consistent with the objectives of the Convention are acknowledged as meeting the financial resources and technology transfer commitments under the regime. Donor governments channelling their resources through mechanisms established outside the Convention therefore run the risk of not have their contributions recognised under the Convention.

In addition to parallel financing structures, there are also concerns that these structures will create parallel climate change governance policies outside the multilateral process. In particular, there are concerns that the inclusion of the US-driven Clean Technology Fund within the portfolio of funds could imply support for the US Major Emitters Meeting process which lies outside the UN track of negotiations on a post-2012 framework. In this manner, the Bank will be creeping into uncharted waters of climate change regulation through its financing policies and conditionalities and playing a role in international environmental governance which it has neither the constitutional mandate nor technical competence to perform.

7. Poor Track Record

Given the Bank's poor track record in managing the social and environmental impacts of its operations, not to mention its existing carbon-intensive financing portfolio, the institution is hardly a credible body to be managing, let alone designing the use of, significant financial resources aimed at helping developing countries develop climate-resilient development strategies and transit towards low-carbon economies. The Bank neither has the constitutional mandate nor the technical expertise to be engaging in the delivery of such fundamental global public goods as climate change mitigation and adaptation.

There are significant inconsistencies between the Bank's rhetoric on climate change and its operational policies and practice. In particular, the Bank's core energy portfolio continues to be focused on supporting conventional fossil fuel production over renewable energy.

The Extractive Industries Review (EIR), which is a Bank-commissioned independent evaluation of the Bank's activities in extractive industries, recommended that the Bank end immediately support for coal projects and phase-out support for oil by 2008. But despite this, the World Bank's support for fossil fuel projects grew by 93 percent from US\$450 million to US\$869 million from financial years 2005 to 2006.

The negative impacts of the Bank's infrastructure investments have been significantly documented over the years. Aside from social and environmental dislocations caused by large projects for energy extraction and production, such as oil pipelines and hydropower dams, the Bank's support for privatisation and deregulation of energy sectors in developing countries have also resulted in energy insecurity, especially for the poor.

In 2006, the World Bank increased its energy sector commitments from US\$2.8 billion to US\$4.4 billion with oil, gas and power commitments accounting for 77 percent of the bank's total energy programme, while 'new renewables' accounted for only five percent. Meanwhile, 40 percent of what the Bank calls 'low-carbon lending' in financial year 2007 consists of large hydropower projects with questionable environmental impacts, with support for hydropower the highest since 1996. The other 40 percent of its 'low-carbon' portfolio focuses on carbon finance.

Studies have shown that the primary beneficiaries of these investments have been large transnational energy companies and not developing countries with projects designed for export rather than the alleviation of energy poverty. A 2004 joint study by the Institute of Policy Studies and the Sustainable Energy and Economy Network found that in most cases, the principal beneficiaries of Bank financing to oil, coal and gas projects in developing countries were developed countries' consumers and corporations, facilitating a massive transfer of developing countries' oil and gas resources to feed the north's energy demands rather than supplying energy to the poor in developing countries.

Moreover, the CIFs' proposals for private sector involvement in the climate change agenda, particularly the use of official development financing to leverage private investment, highlights the World Bank's schizophrenic approach to public subsidies. The institution claims that public sector financing can assist in creating enabling environments for private sector development and securing private financing flows in the area of climate change.

However, in reality the Bank does not necessarily apply these principles in other aspects of its operations, notably through conditionalities in its policy-based lending which require the removal of state-backed subsidies to domestic economic sectors and local firms. Therefore, while championing subsidies in one arena, the Bank, through its other financing operations, continues to remove the policy space required by the public sector in developing countries to support its domestic private sector.

8. Credibility Issues and Conflict of Interest

Aside from its poor environmental track record, as a potential beneficiary of the CIFs, the Bank's appointment as trustee, secretariat and overall coordinator for the funds represent a clear conflict of interest, particularly when its performance in the delivery of global public goods and technical assistance and development policy advice remains questionable at best.

The Bank's performance in managing trust funds for the delivery of financing for global public goods has been criticised by its own evaluation unit, particularly in respect to the quality of technical assistance delivered to client states where these form a core part of the programme. In 2004, the Bank's Independent Evaluation Group (IEG)'s evaluation on the organisation's global partnerships programme found that evidence on the value-added of these programmes in terms of development outcomes varies, with many programmes lacking 'clearly defined objectives' in programme design and implementation.

The evaluation unit found that it is unclear whether the knowledge disseminated under these programmes were 'sufficiently evidence-based, quality-tested, and contextual to add value to what the Bank's client countries themselves do, need, or want or what the Bank can achieve working through country-level partnerships'. This is compounded by the fact that the voices of developing countries in these programmes are 'inadequately represented' and that such programmes, including the trust funds, have contributed little towards the overall increase in ODA.

9. Place Climate Financing Under the UN

The climate investment funds will form a major pillar in the Bank's new ambitious climate strategy, outlined in its Strategic Framework on Climate Change which will be presented to the Bank's Executive Board for approval in September 2008 and for discussion at the institution's Annual Meeting. This mission creep must be placed within the context of its declining relevance as a development bank and dwindling revenue streams, especially from its middle-income member countries.

The CIFs, as part of the Bank's overarching strategy to weigh in on the climate change debate, enable the Bank to capture a significant portion of financial resources set aside by developed countries' for climate-related activities, partly in fulfilment of their commitments under international climate change regimes. Through the administration of these climate investment funds and leveraging other aspects of its operations for climate-related financing; technical assistance work and efforts to play a leading a role in the development of carbon markets, the World Bank is setting itself up to be a key, if not *the* key, player in the governance of climate change.

The danger of such an aggressive move on the part of the Bank is evident. Not only does the institution have a poor track record in environmental matters, its technical 'expertise' on a variety of

issues – from structural economic reforms to health and social policy to public administration and governance – have been shown to be lacking if not damaging to its developing country borrowers.

The Bank has neither the constitutional mandate nor the technical competence embark on the delivery of such an important global public good. Moreover, the Bank's asymmetrical governance structure will further marginalise developing countries from having a stake in the fight against climate change and is at risk of creating 'solutions' for countries which may undermine rather than support their efforts to mitigate and adapt to the effects of climate change.

Creating parallel structures for climate change regulation would also enable developed countries to migrate away from existing multilateral channels for implementing their international climate change commitments and may add to the undermining of existing multilateral negotiations. Developing countries, especially those facing the most immediate and severe threat from the effect of climatic changes and with the least resources to deal with these impacts, will be substantially short-changed in this process.

Providing the bulk of climate change resources through a non-UNFCCC and developed country-driven entity such as the World Bank-led CIF mechanism will not only be counter-productive to the aims of achieving global GHG emission reductions (which are key to combating climate change) but also be contrary to the provisions of the UNFCCC to which most of the CIF contributors are signatories. Moreover, as the Bank itself is a potential beneficiary of financing from the CIFs, there is a significant conflict of interest between its roles as trustee and secretariat of the funds and its role as an implementing entity.

Any legitimate effort to increase the amount of resources for climate change adaptation and mitigation must therefore be placed within a genuine multilateral framework which provides for adequate representation for both developed and developing countries, especially as financial resources remain the main impediment to developing countries meeting climate change challenges.

Given that the UNFCCC remains the only truly international framework which is not just scientifically-based but also guided by multilaterally negotiated principles and has almost universal membership, effective and sustainable financing for meeting climate change commitments of both developed and developing countries must be located within this framework.

Efforts must therefore be focused on developing a genuinely multilateral fund for climate change financing under the auspices of the UNFCCC which is governed by the UNFCCC membership on the basis of regional representation. This would give developing countries due representation and voice within the governance structure and ensure that the resources set aside for climate change are used in accordance with internationally agreed principles and meet the objectives of the multilateral climate change regime.

NOTE: For further details, please see the TWN Briefing Paper No 5: 'No Additionality, New Conditionality: A Critique of the World Bank's Proposed Climate Investment Funds' available at the link below but please note that this paper was based on earlier drafts of the Bank proposals: <http://www.twinside.org.sg/bangkok.briefings.htm>

For details of the proposed funds, see: <http://go.worldbank.org/58OVAGT860>