



Research letter

# The special climate change fund: origins and prioritisation assessment

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## Abstract

The Special Climate Change (SCC) fund was established by the Marrakesh Accords under the United Nations Framework Convention on Climate Change. This fund will finance climate change activities in the areas of: adaptation, technology transfer, certain specific sectors, and activities to assist oil-exporting countries diversify their economies. These activities are to be complementary to those funded by the Global Environment Facility and by bilateral and multilateral funding. This paper describes the origins of the SCC fund and proposes a framework for the prioritisation of its activities. The fund has a complicated history that is intrinsically linked to numerous Convention issues, which explains the range of activities included in it. The framework proposed is based on certain principles: sound scientific knowledge, the ultimate objective of the Convention, “common but differentiated responsibilities and respective capabilities” and the status of the climate negotiations. This appraisal suggests that the fund should prioritise adaptation, followed by mitigation and finally economic diversification.

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## 1. Introduction

The Marrakesh Accords<sup>1</sup> to the United Nations Framework Convention on Climate Change (FCCC) established three new funds at its Seventh Conference of the Parties (COP-7) in November 2001 (Barnett and Dessai, 2002; Dessai and Schipper, 2003; Huq, 2002). A Least Developed Country (LDC) fund

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<sup>1</sup> Contained in FCCC/CP/2001/13/Add.1–4.

and a special climate change (SCC) fund were established under the Convention<sup>2</sup> and an Adaptation fund under the Convention's Kyoto Protocol.<sup>3</sup> Due to a generalised perception of the urgency to tackle the vulnerability of LDCs to climate change,<sup>4</sup> negotiations on the operationalisation of this fund were promptly started at COP-7. A LDC Expert Group (LEG) was established “to serve in an advisory capacity to the LDCs, for the preparation and strategy for implementation of National Adaptation Plans of Action (NAPA)”.<sup>5</sup> COP-7 also provided initial guidance for the operation of the LDC fund by the financial mechanism of the Convention, the Global Environment Facility (GEF).<sup>6</sup> Between COP-7 and COP-8, the LEG met to improve the guidelines for the preparation of NAPA,<sup>7</sup> while the GEF Council approved the establishment of the new funds under its wings. At COP-8, in New Delhi in October/November 2002, additional guidance was provided to the GEF for the operation of the LDC fund.<sup>8</sup> According to the GEF report to COP-8, this fund should be operational by early 2003.<sup>9</sup> From the formulation of the LDC fund at COP-6 in November 2000, to its adoption at COP-7 and its likely implementation in 2003, the LDC fund is probably one of the instruments to become operative most rapidly in the short history of the FCCC.<sup>10</sup>

The SCC fund and the Adaptation fund did not follow the same track as the LDC fund. These funds lacked a sense of urgency and COP-7 did not produce initial guidelines for their operation. The Kyoto Protocol's Adaptation fund is likely to be dealt with once it enters into force and under the Meeting of the Parties to the COP. It was expected that guidance on the operation of the SCC fund would be devised at COP-8, but Decision 7/CP.8 lacks substance and simply defers work to COP-9. This article reviews the history of the SCC fund and proposes a framework for the prioritisation of its activities.

## 2. Origins of the special climate change fund

The origins of the Marrakesh funds date prior to The Hague Conference. Aware of the need to accommodate developing country concerns, Jan Pronk, chairman of COP-6, proposed the creation of two new funds. An early form of the SCC fund first appeared in the ‘Pronk paper’<sup>11</sup> as an ‘Adaptation fund’ and a ‘Convention fund’. This Adaptation fund would implement concrete adaptation projects in non-Annex I Parties, with financing from the share of proceeds of the Clean Development Mechanism (CDM), thus becoming intimately linked to the Kyoto Protocol. The Convention fund was in essence a mitigation fund, which included *inter alia* technology transfer, capacity building and assistance with

<sup>2</sup> Decision 7/CP.7 contained in FCCC/CP/2001/13/Add.1.

<sup>3</sup> Decision 10/CP.7 contained in FCCC/CP/2001/13/Add.1.

<sup>4</sup> The IPCC Third Assessment Report concluded, “those with the least resources have the least capacity to adapt and are the most vulnerable” (IPCC, 2001). The Marrakesh declaration expressed deep concern that “all countries, in particular developing countries, including least developed countries and small island states, face increased risk of negative impacts of climate change” (Decision 1/CP.7).

<sup>5</sup> Decision 29/CP.7 contained in FCCC/CP/2001/13/Add.4.

<sup>6</sup> Decision 27/CP.7 contained in FCCC/CP/2001/13/Add.4.

<sup>7</sup> FCCC/SBI/2002/INF.14 and INF.16.

<sup>8</sup> Decision 7/CP.8. Contained in FCCC/CP/2002/7.

<sup>9</sup> Statement by GEF at COP-8.

<sup>10</sup> Probably only paralleled by Activities Implemented Jointly and Clean Development Mechanism projects.

<sup>11</sup> FCCC/CP/2000/CRP.14.

economic diversification. The Pronk paper was an attempt to reach a political deal at COP-6 in The Hague. Though similar ideas on funding had been floating since Rio,<sup>12</sup> it was President Pronk, who introduced the precursor of the SCC fund into the negotiations. Agreement over funding and a number of other issues, including sinks, mechanisms and compliance, could not be reached at The Hague so COP-6 was suspended and reconvened in the summer 2001 in Bonn (Dessai, 2001). Parties later submitted their views on the Pronk paper.<sup>13</sup> Developing countries (DCs) in particular were concerned that:

- Adaptation funding would only go ahead if the Kyoto Protocol entered into force, which became much harder with the rejection of the Protocol by the US.
- The CDM share of proceeds was expected to be low (Jotzo and Michaelowa, 2002).
- Few adaptation activities were eligible; only avoidance of deforestation, combating land degradation and desertification were included.
- DCs did not want the GEF to become the operating entity of the funds because of its perceived bureaucratic complexity, namely, long periods between project approval and the disbursement of funds by its implementing agencies,<sup>14</sup> competition between implementing agencies, the GEF policy of “incremental costs”,<sup>15</sup> the dominant role of the World Bank, etc. (Streck, 2001).<sup>16</sup>

Considering these submissions, earlier negotiating texts and wider consultations, President Pronk presented a revised negotiating text before Bonn.<sup>17</sup> In terms of the funds not much had changed except the substitution of the ‘Special climate change fund’ for the ‘Convention fund’. After protracted negotiations and intense horsetrading, a political deal was reached in Bonn.<sup>18</sup> The Bonn Agreement established three new funds: the Kyoto Protocol Adaptation fund as in the latest Pronk paper, the SCC fund as in the latest Pronk paper with the addition of funding in the area of adaptation<sup>19</sup> and a new LDC fund to support a work programme for the LDCs. However, in order to be adopted by the COP, the political agreement had to be translated into decision text. While finalisation of most other issues (sinks, mechanisms and compliance) took place at COP-7, developing country issues were agreed at the resumed session of COP-6 and were waiting adoption. At COP-7, the Marrakesh Accords were adopted, thus, fulfilling the Buenos Aires Plan of Action (BAPA; see below).

It is important to consider the context surrounding the creation of the SCC fund as well the other funds.<sup>20</sup> After the adoption of the Kyoto Protocol at COP-3, the BAPA was adopted at COP-4, which included an ambitious schedule of work on developing country issues, such as funding, technology transfer and capacity building, emanating from the Convention’s obligations. This process culminated in the adoption

<sup>12</sup> For example, during the negotiations of the FCCC, Germany proposed a protocol on the ‘adjustment to climate change and the prevention and containment of climate-related damage’ (Verheyen, 2002). Similarly, in the run-up to Kyoto, Brazil proposed the creation of a Clean Development Fund.

<sup>13</sup> FCCC/CP/2001/MISC.1.

<sup>14</sup> GEF’s three implementing agencies are: the UN Development Programme (UNDP), the UN Environment Programme (UNEP) and the World Bank.

<sup>15</sup> Incremental costs were defined as the extra costs incurred in the process of redesigning an activity vis-à-vis a baseline plane, which is focused on achieving national benefits, in order to address global environmental concerns (Streck, 2001).

<sup>16</sup> In their submission, Nigeria on behalf of the G77/China, renamed the Convention fund as ‘Special fund’.

<sup>17</sup> FCCC/CP/2001/2/Rev.1.

<sup>18</sup> Decision 5/CP.6 contained in FCCC/CP/2001/L.7.

<sup>19</sup> This addition was likely due to the concerns of DCs expressed in their submissions.

<sup>20</sup> See Verheyen (2002) for a primer on adaptation and funding under the climate regime.

of the Marrakesh Accords. For DCs, the creation of three new funds and the promise of certain Annex I Parties to contribute money to these funds,<sup>21</sup> was in essence a *quid pro quo* for their acceptance of a watered down Kyoto Protocol. While DCs wanted binding contributions to be made to these funds, it was only possible to agree that “predictable and adequate levels of funding shall be made available to Parties not included in Annex I”.<sup>22</sup>

The SCC fund is intimately linked with a number of Convention issues, which further explains its convoluted design. One such issue is technology transfer, a much-discussed matter since the Convention was signed in Rio. The Convention required that developed countries “promote, facilitate and finance the transfer of, or the access to, environmentally sound technologies” to DCs, but did not elaborate how this was to be done.<sup>23</sup> It was only at COP-7, in response to the BAPA, that a framework to enhance the implementation of technology transfer was adopted, including the establishment of an expert group on technology transfer.<sup>24</sup> The implementation of this framework will be financed by the GEF’s climate change focal area as well as the SCC fund.

The SCC fund is also closely associated with the issue of adverse effects and the impacts of response measures, commonly known as Article 4.8 and 4.9 of the Convention (Barnett and Dessai, 2002). In essence, adverse effects<sup>25</sup> refer to adaptation to climate change, which is one of the areas addressed by the SCC fund. The following activities will be supported by the SCC fund and/or the Kyoto Protocol’s Adaptation fund:

- (a) Starting to implement adaptation activities promptly where sufficient information is available to warrant such activities, inter alia, in the areas of water resources management, land management, agriculture, health, infrastructure development, fragile ecosystems, including mountainous ecosystems, and integrated coastal zone management.
- (b) Improving the monitoring of diseases and vectors affected by climate change, and related forecasting and early-warning systems, and in this context improving disease control and prevention.
- (c) Supporting capacity building, including institutional capacity, for preventive measures, planning, preparedness and management of disasters relating to climate change, including contingency planning, in particular for droughts and floods in areas prone to extreme weather events.
- (d) Strengthening existing and, where needed, establishing national and regional centres and information networks for rapid response to extreme weather events, utilizing information technology as much as possible.<sup>26</sup>

The issue of impact of response measures is ‘in theory’ clearly distinct from the adverse effects of climate change, but ‘legally’ the fact that they are mentioned together in Article 4.8 of the FCCC conflates and complicates the issue. The Marrakesh Accords include a single decision on these two issues, though the

<sup>21</sup> The EU, Canada, Iceland, New Zealand, Norway and Switzerland pledged to contribute 450 million annually by 2005 (with this level to be reviewed in 2008) for the three funds, GEF climate change activities, bilateral and multilateral funding and the CDM. Canada further pledged to contribute C\$ 10 million to enable the prompt start of the LDC fund.

<sup>22</sup> As Verheyen (2002) notes, there is currently no mechanism in place for this requirement to be met.

<sup>23</sup> Article 4.5 of the FCCC.

<sup>24</sup> Decision 4/CP.7 contained in FCCC/CP/2001/13/Add.1.

<sup>25</sup> According to the Convention, adverse effects of climate change “means changes in the physical environment or biota resulting from climate change which have significant deleterious effects on the composition, resilience or productivity of natural and managed ecosystems or on the operation of socio-economic systems or on human health and welfare” (Article 1.1 of the FCCC).

<sup>26</sup> Decision 5/CP.7 contained in FCCC/CP/2001/13/Add.1.

decision is separated into different sections.<sup>27</sup> In the language of the Kyoto Protocol,<sup>28</sup> the impact of response measures requires Annex I Parties to minimise the adverse social, environmental and economic impacts on developing countries when they implement their commitments. In this area, the SCC fund will finance activities to assist developing country Parties referred to under Article 4.8(h) for the Convention,<sup>29</sup> in essence oil-producing countries, to diversify their economies.

In summary, the SCC fund will finance climate change activities, programs and measures, that are complementary to other GEF efforts, in the areas of

- (a) adaptation;
- (b) transfer of technologies;
- (c) energy, transport, industry, agriculture, forestry and waste management;
- (d) activities to assist oil-producing countries in diversifying their economies.

### 3. Prioritisation of special climate change fund activities

It is clear that the design of the SCC fund was shaped by the historical developments within the Convention. The result is a fund that allows the financing of a myriad of climate change activities ranging from adaptation (to climate change) to disaster management as well as technology transfer and mitigation in a number of areas including sequestration. COP-8 initiated a process to define the prioritised activities, programmes and measures to be funded out of the SCC fund.<sup>30</sup> It is expected that the process will be completed at COP-9, where further guidance will be provided to the GEF. This section presents some ideas on how the numerous areas of the SCC fund could be prioritised in order to allow its prompt operationalisation.

In a submission regarding their views of the Pronk paper, Colombia suggested that the Convention fund (precursor to the SCC fund) resources should be distributed 60% on adaptation projects and 40% on capacity building and technology transfer projects. The grounds for these specific percentages are not discussed, but they are considered to be open to negotiations by Parties. It is this sort of prioritisation that will need to be performed for the SCC fund, but based on certain criteria which this paper now considers.

Sound scientific knowledge should be at the core of the distribution of resources among the different areas of the SCC fund. If we consider Article 4.8 and 4.9, we can easily find estimates of adverse effects and estimates of the impacts of response measures in the literature. It is known that current models are not able to model either adequately.<sup>31</sup> Modelling both areas is highly uncertain, however, there is a voluminous non-modelling literature that substantiates that there will be adverse effects on DCs because they are already occurring under present climate variability (IPCC, 2001). While the exact spatial, temporal and magnitude of adverse effects may be uncertain, what is far less uncertain is that there will be adverse

<sup>27</sup> (1) Adverse effects of climate change; (2) implementation of Article 4.9 of the Convention (relates to LCDs); (3) impact of the implementation of response measures; and (4) further multilateral work (relates to workshops).

<sup>28</sup> Articles 2.3 and 3.14 of the Kyoto Protocol.

<sup>29</sup> Countries whose economies are highly dependent on income generated from the production, processing and export, and/or consumption of fossil fuels and associated energy-intensive products.

<sup>30</sup> Decision 7/CP.8 contained in FCCC/CP/2002/7/Add.1.

<sup>31</sup> See, for example, the report of the workshop on “the status of modelling activities to assess the adverse effects of climate change and the impact of implemented response measures” convened under the FCCC (FCCC/SBI/2002/9). It provides an overview of the state-of-the-art on this matter.

effects (Barnett, 2001). There is no supplementary non-model based evidence for impacts of response measures, meaning that the uncertainty in these models has no reliable counterpart information to qualify it. However, it is essential to acknowledge that oil is an important commodity in the world economy and thus any changes in demand or supply could have far-reaching effects of a global nature, in particular to the Organisation of Petroleum Exporting Countries (OPEC). There are, nonetheless, a range of policy measures available to lessen whatever impact, if any, climate mitigation policies may have on OPEC (Barnett et al., 2003). To sum up, while both issues are uncertain, the impacts of response measures are less methodologically appropriate and do not have the corroborating evidence that models estimating adverse effects do. Therefore, prioritising measures to reduce adverse effects (adaptation) would be better since the possibility for regret is less.

While the case of adverse effects versus impacts of response measures (bullets a and d) has been presented, the SCC fund also includes other areas related to mitigation (bullets b and c). The case for adaptation versus mitigation within the SCC fund could also be debated. A useful principle for this approach is to consider the ultimate objective of the Convention: “stabilisation of greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system”.<sup>32</sup> This implies that both mitigation (by stabilising concentrations) and adaptation (by avoiding dangerous climate impacts) need to be considered with equal standing. Some economic analysis suggest that it will be much more costly to mitigate rather than pay the costs of adaptation to climate change (Lomborg, 2001). Using an integrated assessment model, Tol (2002) shows exactly the opposite: that development aid (adaptation) is less effective in reducing vulnerability than emission abatement (mitigation).<sup>33</sup> This clearly shows that there is a wide range of views in the literature. The trade-offs between mitigation and adaptation need to be further researched, but we also know that adaptation and mitigation are not mutually exclusive. Therefore, projects that simultaneously tackle adaptation and mitigation need further investigation.<sup>34</sup>

Another useful principle enshrined in the Convention is that of “common but differentiated responsibilities and respective capabilities”.<sup>35</sup> While this principle has been extensively used in order to have developed countries take a lead in combating climate change, it can also be applied to this prioritisation problem. Some developing countries are much more capable of coping with climate change than others. Furthermore, Parties that are particularly vulnerable to the adverse effects of climate change and that would bear a disproportionate or abnormal burden under the Convention, should be given full consideration.<sup>36</sup> While the poorest DCs have little financial and technological capacity to cope with the impacts of climate change, OPEC countries can cope with the impacts of response measures by acting as a cartel and by self-supporting economic diversification (Barnett and Dessai, 2002). The principle of more capable states would give the highest priority to adaptation and the least to economic diversification of OPEC countries.

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<sup>32</sup> Article 2 of the FCCC. It further adds that such a level should be achieved within a time-frame sufficient to allow ecosystems to adapt naturally to climate change, to ensure that food production is not threatened and to enable economic development to proceed in a sustainable manner.

<sup>33</sup> Except for vector-borne infectious diseases (malaria) and for regions where such diseases dominate total climate change impacts (Africa).

<sup>34</sup> For example, some forestry projects could simultaneously enhance community resilience and sequester carbon from the atmosphere. However, only a few sectors might be able to benefit from this, for example, forestry and waste management. Furthermore, such projects might not maximise the efficiency of either adaptation or mitigation.

<sup>35</sup> Article 3.1 of the FCCC.

<sup>36</sup> Article 3.2 of the FCCC.

The history of the SCC fund has been reviewed in section two and is the basis for some of the principles proposed, but it is important to take stock of the climate regime as a whole (Dessai, 2001). With the completion of the BAPA at Marrakesh and the expected entry into force of the Kyoto Protocol, a number of issues are relevant to the fund. Most important is the fact that the Marrakesh Accords have commodified the atmospheric commons (Glover, 1999). The operationalisation of the CDM is particularly relevant for this fund because it deals with mitigation and technology transfer to DCs. Both public and private investments from developed countries are ongoing in DCs under the umbrella of CDM projects. Developed countries that have invested in such projects from 2000 onwards and that abide by the CDM rules agreed at Marrakesh<sup>37</sup> will gain credit<sup>38</sup> that can be offset against respective Kyoto targets. Even though the price of carbon is expected to be low in the absence of the US (Jotzo and Michaelowa, 2002), a carbon market has been created and various CDM projects are underway and many more are in the pipeline. There does not appear to be an incentive for donor countries to contribute money to a SCC fund, which would then finance mitigation projects (under b–d) for which they could not get credit. Thus, it seems clear that adaptation should be prioritised over mitigation because a market mechanism already exists for the latter. A further complication for adaptation is the duplication of activities being financed by the Kyoto Protocol's Adaptation fund and the SCC fund adaptation activities. The sole difference between the funds is that the former will also finance 'concrete adaptation projects'.

#### 4. Conclusions

Ultimately, the prioritisation of activities under the SCC fund will be based on politics because of the nature of the Convention process. OPEC will push for economic diversification and stall other matters under negotiation if progress on 'all issues' is not achieved. The Alliance of Small Island States and the LDCs will use their moral high ground position and bloc-voting to push for adaptation. Middle ground DCs are likely to prefer technology transfer and mitigation. The compromise deal will likely be somewhere in-between. However, there a number of other issues that will complicate the prioritisation process further, including: the amount and distribution of funding for the three funds; complementarity of funding and activities between funds (especially the Adaptation fund) and within the SCC fund; and whether funding will be used as a political conditionality for some DCs to take on commitments of some sort during the second commitment period of the Kyoto Protocol.

Some of the principles suggested in this paper, all based on the Convention, could help Parties reach an agreement on this difficult issue. If we follow the principles proposed, it seems clear that adaptation (to the adverse impacts of climate change) should be prioritised, followed by mitigation (technology transfer and the other sectors) and lastly economic diversification. The prioritisation of SCC fund activities will be a big test for the cohesiveness of the Group of 77 and China in particular.<sup>39</sup> The application of these principles could facilitate the negotiation of the process within the Group and with other Parties in order to reach a successful and equitable outcome by COP-9.

<sup>37</sup> Decision 17/CP.7 contained in FCCC/CP/2001/13/Add.2.

<sup>38</sup> Certified Emission Reduction units.

<sup>39</sup> See Williams (1997) on the Group of 77 and global environmental politics.

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