



Climate Action Network

Financial instruments to address loss and damage associated with the adverse effects of climate change

*Best practices, challenges and lessons learned
from existing financial instruments*

Submission to the Executive Committee of the Warsaw International Mechanism on Loss
and Damage

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Climate Action Network International (CAN) is the world's largest network of civil society organizations working together to promote government action to address the climate crisis, with more than 950 members in over 110 countries. www.climatenetwork.org

Introduction

Loss and damage are the adverse effects of climate change that go beyond people's capacity to cope and adapt to climate change impacts (Warner, van der Geest and Kreft 2013; LDC 2012). Loss and damage impacts range from extreme events, for example, weather-related natural hazards, to slow-onset events, including sea-level rise; increasing temperatures; ocean acidification; glacial retreat and related impacts; salinization; land and forest degradation; loss of biodiversity; and desertification (UNFCCC 2012).

Communities are already experiencing significant loss and damage to quality of life, livelihoods, food, and livelihood security as well as secondary loss and damage in the form of stress on the social fabric essential for adaptive capacity and resilience (LDC 2012).

We welcome the agreement at Paris to aim to keep warming to 1.5°C. This would prevent some of the worst impacts of climate change, but will still poses serious challenges, especially for least-developed countries, small island developing states, African countries and a number of vulnerable Latin American countries including with drought, ocean acidification, and sea-level rise (Schaeffer et al. 2013, pp. 3–4). Hence, even with the best possible future mitigation efforts, vulnerable countries will still have to deal with loss and damage (LDC 2012; Verheyen and Roderick 2008, pp. 10–11). Even worse, current mitigation ambitions as expressed in the INDCs might still lead the world to a warming in the order of 3°C of average by the end of this century. This level of warming may be beyond the limits of adaptation for a large number of countries (Schaeffer et al. 2013, p. 4), in particular as it results in significantly higher increases in many regions.

Effective and timely adaptation approaches – such as integrating disaster risk- reduction; climate change adaptation and sustainable development; ecosystem-based approaches for building resilience; sector-specific measures and tools (UNFCCC 2012); and community-based adaptation – can be utilised to reduce loss and damage by increasing resilience to climate change impacts. The international community lags well behind what is necessary to provide support for adaptation, hence increasing the expected burden of loss and damage upon the most vulnerable.

At its heart, loss and damage concerns fairness and justice when dealing with climate impacts. As a result there are a number of principles which it is relevant to bear in mind when considering approaches in this area. These include the principles of equity and common but differentiated responsibilities enshrined within the UNFCCC and Paris agreement, but also the general obligation in international environmental law that states should ensure that activities within their jurisdiction and control respect the environment of other states and areas beyond their national jurisdiction.¹

In line with equity and human rights requirements, CAN is of the view that it is of particular importance to **address the needs and concerns of those segments of the population which are particularly vulnerable**, in line with the WIM work plan. For many financial instruments, this also requires an in-depth understanding of the livelihood situations of these population groups, people and communities, and therefore we encourage every institution involved in the setting up and delivery of finance to address loss and damage to pay special attention to this and work closely with the vulnerable.

Furthermore, given the principles set out above, the origin of climate change caused by anthropogenic greenhouse gas emissions and also to provide incentives for the reduction of emissions, **CAN also supports the introduction and use of instruments which apply the polluter pays principle**, generating resources from those countries, institutions, or individuals who produce (or have produced) significant emissions². The generation of additional resources is urgently required to (partially) cover costs occurring as a consequence of climate change and in many vulnerable developing countries undermining poverty reduction and sustainable development progress. Such resources can then also help scaling-up effective delivery mechanisms for channelling resources to the vulnerable and most affected for addressing the spectrum of loss and damage (incl. e.g. disaster relief, insurance, relocation efforts).

This submission will focus on instruments which can generate new and additional resources, as one experience with current instruments is that their scale is insufficient to meet the growing loss and damage. Of course, their effective use on the ground depends on important factors and variables in the context of pro-poor sustainable development approaches, but also being concerned that this crucial dimension lacks political attention.

¹ See, for example, Art 4.2 UNFCCC Convention, Principle 21 of the Stockholm declaration, Principle 2 of the Rio declaration and the ICJ 1996 advisory opinion on nuclear tests.

² The International Law Association's draft principles on climate change also underline the need to "make good" or provide some form of compensation for the unequal use of the global atmosphere in the past by industrialized countries.

Scale of need for loss and damage finance

Estimates of the loss and damage associated with climate impacts indicating certain levels of financial needs are wide - but even low estimates show the need for loss and damage finance as substantial:³

- [Oxfam \(Climate Action Tracker 2015\)](#) 2050 economic damage for developing countries could be **\$1.85 trillion per year (about 1.45% of GDP)** for current iNDCs/current policy pathway leading to 3.6°C of warming.
- [AMCEN/UNEP Africa's Adaptation Gap 2 Report \(2014\)](#) with all cost effective adaptation **Africa loss and damage is estimated at ~\$100bn per year by 2050** for warming below 2°C, at least double that if warming goes above 4°C.
- [UNEP Adaptation Gap Report \(2014\)](#) the indicative cost of **adaptation and the residual damage (loss and damage) for the LDCs ~US\$50 billion/year by 2025/2030 and possibly double this value (US\$100 billion/year) by 2050** at 2°C.
- [Climate Vulnerability Monitor 2 \(2012\)](#), from DARA and the Climate Vulnerability Forum climate change caused net **global economic losses of \$609 billion in 2010, expected to increase to \$4.3 trillion by 2030. 80-90% of these costs are projected to fall on developing countries, with the LDCs suffering the worst.**
- **Dr Chris Hope (in Parry et al. 2009)** estimated that **by 2060 global loss and damage will be about US\$1.2 trillion per year**
- [Burke, Hsiang, and Miguel \(Nature 2015\)](#) said existing Integrated Assessment Models under-estimate future climate-change costs. Rather at **5°C GDP falls 25 - 75%.**

Three specific recent examples show how climate change can fuel natural hazards and increase the economic and non-economic damages for populations:

- Hurricane Tomas devastated Saint Lucia in 2010 and wiped out the equivalent of 43% of its GDP (World Bank 2013, p. 6).
- In the Horn of Africa, a prolonged drought that ended in 2011 and which, at its peak, left 13.3 million people with food shortages, caused total losses of \$12.1 billion in Kenya alone (Government of Kenya 2012 in World Bank 2013, p. 6).
- 2013 Typhoon Yolanda (Haiyan) displaced 4 million people, destroyed or damaged 1 million houses, killed at least 6,300 people, and caused approximately US\$2 billion in damage in the Philippines. In the preceding years the Philippines had six typhoons with combined damages of US\$2.8 billion (NDRRMC in Wikipedia).

New financial instruments that should be considered

The following section will elaborate on potential new financial instruments to raise resources for climate action, which should include loss and damage action, as experience from current financial instruments is that their scale lags far behind what is needed. In particular developed country governments have a responsibility to ensure that sufficient finance for loss and damage is provided and to make proven and new solutions of finance delivery work at the scale required. Both by providing financial support in the form of public funds via government treasuries, in addition to existing commitments to mitigation and adaptation finance, and in establishing new and innovative forms of finance. There is support for this approach in the ILC

³ The figures listed cannot be directly compared as they relate to different assessments. However, the main purpose here is to provide an illustration of the substantial financial implications of loss and damage.

principles on the allocation of loss in cases of transboundary harm⁴ which advocate for states to establish industry-wide funds for victims of harm at the national level (Principle 4(4)) and consult with states affected, or likely to be affected, to mitigate the impacts of the damage.

New and innovative forms of public finance offer significant potential to address the funding gap that exists in both adaptation and loss and damage. Some of these “new” sources of finance have been under discussion for a number of years, including by the High Level Advisory Group on Finance, the Leading Group on Innovative Finance and others. They include a Financial Transaction Tax (FTT), a fossil fuel levy (or Carbon Majors Levy), carbon pricing for international aviation and maritime, using a share of revenues from domestic or regional carbon pricing/carbon markets for international solidarity, and others.

It is important to clear up any confusion about what is meant by “innovative” sources of finance and how they can contribute to overall climate finance. Innovative sources of finance should continue to be defined as new ways and mechanisms -- such as those we lay out in this paper -- to generate additional and complementary public finance resources for international climate finance and sustainable development. In recent years, many donor countries and blocs have begun referring to ‘innovative finance’ as a means to leverage finance, mostly in the forms of investments, from the private sector which are then counted and labelled as climate finance. Innovative finance did not - and should not - exclusively set out to use existing and already scarce public resources to further leverage and incentivise private sector finance.

Innovative finance may play a role in both increasing finance to complement existing public flows and effectively internalise the social and environmental damage and costs incurred by state and non-state actors; for example, through the application of the FTT and the carbon majors levy. We also emphasise previous assertions made by both the Leading Group on Innovative Finance and the UNDP that innovative finance should add further predictability, quality and efficiency to flows of finance, particularly ODA.

During 2010 significant work was undertaken on innovative sources of finance, including from the Leading Group on innovative finance and High Level Advisory Group on Climate Finance (AGF). New ideas have been explored since then in a range of fora, including the recent Africa Adaptation Gap Report 2, the IMO and ICAO. 2016 is the year to begin unlocking these ideas as the scale and interconnectedness of the climate, sustainable development and poverty reduction, disaster risk challenges become clear, and the need to generate large sums of additional resources is clearer than ever.

The UNEP estimates that between USD 26 billion & USD 115 billion could be raised by 2020 from just 3 innovative sources: auctioning of emission allowances (ETS); revenues from international transportation (Carbon Pricing); and a Financial Transaction Tax (FTT). Other opportunities include a proposal for a Global Fossil Fuel Extraction Levy (to be paid into the Warsaw International Mechanism for Loss & Damage) as well as shifting finance from dormant mechanisms. A short background on each is explored below.

Once established, the resources that these instruments would generate could for good reasons be used for different purposes, incl. climate change adaptation, but also addressing loss and damage, e.g. oriented towards the main work areas of the Warsaw International Mechanisms which reflect support needs. They could be channelled through different existing or also new instruments in support of actions in developing countries, as appropriate.

Carbon pricing (taxes or markets)

⁴ <http://legal.un.org/avl/ha/palcthaoha/palcthaoha.html>

Mechanisms to price carbon at national levels help internalise the cost of pollution and are central to many governments' efforts to reduce emissions. As a result of carbon pricing, such mechanisms raise revenues, which could play a significant role in raising finance for climate action, domestically for all countries, and internationally for those countries with greater capacity and responsibility.

The adoption of such mechanisms should be accompanied by agreed standards and rules for the use of the revenues they generate. The EU's Emissions Trading Scheme is a particular case in point, as it urges EU Member States to allocate 50% of revenues from the auctioning of emissions allowances for climate action, though this is not an obligation. In 2013, EU Member States used 87% of auction revenues amounting to EUR 3 billion for climate action, though the large majority of this was used domestically and it is unclear how much of this simply displaced other domestic budgetary sources. From the finance generated, less than EUR 500 million, or just 13%, of these revenues went to international climate finance, from just five EU Member States. Firmer commitments need to be made to support efforts to raise international climate finance and provide an example to other countries setting up carbon pricing mechanisms (whether taxes or markets). However, it is worth noting that the unpredictability of carbon market auction revenues means that these should be conceived as part of a broader package of financing.

There are concrete re-enforcing ways to deliver additional international climate finance:

1. Member States should seek to establish an ETS International Climate Fund, which can be replenished by a percentage of total auctionable permits to be withheld at European level before permits are distributed to Member States. The Fund could channel revenues directly to the Green Climate Fund for mitigation and adaptation actions in developing countries, as well as to existing or new instruments which address loss and damage. Depending on the percentage of allowances dedicated in this way, and dependent on the carbon price, climate finance contributions generated by the EU carbon market could deliver between 1 to 3.4 bn a year.
2. Changing the current rules to stop giving emissions allowances for free to companies, hence generating billions in finance.

Fossil Fuel Levies (Carbon Levy)

A global fossil fuel extraction levy (a "Carbon Levy") would provide a new source of finance and ensure that the fossil fuel industry pays for the climate loss and damage that their products are causing.

A proposal on how a Carbon Levy could work was made in June 2014 and uses [The Carbon Majors Report](#) that attributes 63% of emissions in the atmosphere to 90 specific entities, known as the Carbon Majors - including investor owned entities such as Chevron, ExxonMobil, Saudi Aramco, BP, Gazprom, and Shell, and state owned entities and states. It is based on existing international law and precedents for such a scheme – including the oil spill regime (IOPC) where companies that ship oil pay a levy into an international mechanism that provides compensation in cases of oil spills.

The Carbon Levy proposal is for a global fossil fuel extraction levy, applied to each tonne of coal, barrel of oil and cubic litre of gas extracted. It could be paid directly into the financial mechanism or an international fund on loss and damage, e.g. set up as part of the Warsaw International Mechanism for Loss and Damage.

Equity, or differentiation, can be incorporated via a process allowing developing countries at a low level of development to “opt-out” by keeping the funds raised by the levy on fossil fuel extraction within their own budgets for climate change purposes.

The fossil fuel extraction levy is a new idea, and could provide a new source of finance for loss and damage, with the co-benefit of placing a price on carbon. At a low level of \$2 per tonne of CO₂e the levy would raise approximately \$50 billion per year. The levy would need to increase each year, as the costs of loss and damage increase and as fossil fuels are phased out and the volume of extraction decreases.

Financial Transactions Tax (FTT)

A financial transactions tax is the application of a modest levy on financial trades, such as on stocks, bonds and derivatives.

Ten European countries, including Germany, France, Italy and Spain, are in the process of establishing a regional FTT, with the goal of having it operational by 2017. French President Francois Hollande has pledged to seek agreement amongst the 10 countries to commit FTT revenues to the Green Climate Fund (GCF) and a mechanism to implement this. After Paris, the pressure to ensure public climate finance, specifically for adaptation, is delivered, will continue to increase. France and its European partners have to work to: 1) set a minimum amount of revenues to be mobilised by the FTT, for example, EUR 34 billion per annum the EU commission estimates will be generated; 2) commit to earmark a significant proportion of these revenues to international solidarity and the GCF, and; 3) ensure the FTT is implemented as early as possible in 2017.

Other developed countries, particularly those with large financial markets, should also establish a broad FTT covering all financial instruments and applying to all financial actors, dedicating a significant proportion of forthcoming revenues for international climate finance, a portion of which may be allocated to loss and damage.

Carbon Pricing for International Aviation and Maritime Transport

Carbon pricing for the sectors of international aviation and maritime transport have been identified as potential sources of revenue for, inter alia, the following reasons:

- Fuels used for international transport are currently exempt from taxation;
- Emissions from these international sectors are not included in national emissions targets, and are the fastest growing emissions of any sector globally;
- Carbon pricing – levies or carbon markets – applied in a fair and equitable way can be effective ways to achieve emissions reductions in these sectors, as well as raising revenue that can be used for climate change adaptation, mitigation, and addressing loss and damage;
- These sectors can raise substantial revenue for climate finance - the AGF estimated that a carbon price of \$25 per tonne on international transport emissions could generate around \$30 billion in total revenue annually, of which over \$10 billion could be used for climate finance as a contribution from developed countries.
- Specific proposals have been put forward by certain countries, such as the International Air Passenger Adaptation Levy, by the group of Least Developed Countries

Market-based Measures (MBMs) – Carbon Pricing – have been under consideration in the International Maritime Organization (IMO) and International Civil Aviation Organization (ICAO) for well over a decade. While very little progress was made in the early years, ICAO now has a deadline of agreeing a cap on emissions growth after 2020, through a market-based offsetting measure to be agreed at its triennial assembly in September/October 2016. The Paris Agreement’s strong provisions against double-claiming offer the possibility that the environmental integrity of this measure could be strengthened significantly. In March 2016, US President Obama and Canadian Prime Minister Trudeau announced their joint commitment to get the measure done this year. The shipping sector, having wavered on the issue, has recently begun considering supporting global MBMs as an alternative to a patchwork of regional measures.

Efforts to use the aviation MBM as a means of raising revenue are being resisted. Other types of MBMs including those that could generate revenue to be used for climate finance are still officially on the table, though receiving little attention.

Neither IMO nor ICAO has yet agreed to an emissions reduction target. Both sectors have argued that a tax will have little utility in controlling emissions, given the historically high fuel prices in recent years. The recent drop in fuel prices has led to changing practices such as speeding up ships that result in lower efficiency and higher emissions, and airline operators preferring to lease older less fuel efficient aircraft over purchasing newer more fuel efficient ones. While a tax could generate significant revenue, whether the environmental effect of any tax would be swamped by these fuel price swings remains to be seen.

The recent proposal from the Marshall Islands for the IMO to set a sector-wide international shipping emissions reductions target is welcome - and IMO member states should move to adopt and implement this quickly. If ICAO does agree to an MBM later in 2016, it must be environmentally robust. CAN is also calling for ICAO and the IMO to work on a levy scheme to provide financing for adaptation in developing countries (CAN Annual Policy Document 2015).

Appropriate mechanisms that can be the basis for differentiating between countries based on their level of development, capacities and responsibilities, while respecting the approaches and customary practices of these bodies have been proposed, and should be implemented.

Financial instruments from other fields

International Oil Pollution Compensation Fund (IOPC)

The oil spill liability schemes provide the most practical example of an active international liability scheme that compensates victims of environmental damage (Daniel n.d., pp. 225, 227).

Oil spill pollution became a serious concern to the international community during the 1950s, when there was a major expansion in movement of oil by sea, and in the following decades a major increase in oil spills. The international community adopted a number of treaties establishing duties to prevent pollution, and eventually a liability scheme. The initial regime,

with instruments from 1967, 1969, 1971, and 1977, was amended in 1992 by two protocols, which broadened the scope of the original treaties and increased compensation limits (1992 Civil Liability Convention (CLC 92) and the 1992 Fund Convention).

The IOPC funds are financed by levies on entities that receive more than 150,000 tonnes of oil per year. Governments are obliged to monitor and submit this information annually to the IOPC Secretariat (Verheyen and Roderick 2008, p.25).

The international scheme that governs liability for oil spill pollution has been one of the most widely accepted international liability schemes (Xue 2003, p.60). Corporate entities have contributed at a rate of 99.8% (Jacobsson 2007, p.7).

Damage must result from oil pollution and have caused a quantifiable economic loss including: property damage; costs of clean-up operations; economic losses by fisher people or those engaged in mariculture; economic losses in the tourism sector; and costs for reinstatement of the environment.

Anyone may bring a claim for compensation within the courts of a Contracting State or States, which provides a useful precedent for allowing communities to directly access the International Mechanism for loss and damage.

The IOPC Fund is not a perfect model - it does not provide compensation at a high enough level, and communities have had difficulties to access it - but it does provide an existing example of a polluter pays approach to dealing with loss and damage that has wide acceptance across governments and industry.