

Raising International Climate Finance

International Trade Union Confederation

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Executive summary & key messages

The gap between commitments made by the developed world for the fight against climate change and for poverty reduction and the effective level of financing (which we call “global public good resource gap”) ranges between USD300-320bn annually for the 2013-2020 period.

The same developed economies are under budget pressure arising from the global recession and the massive increase in public debt since 2008. Turning away from austerity is needed if growth is to be maintained, but also if indeed developed countries are to meet their global public good commitments..

Developed countries must demonstrate their commitment to meet the USD100bn target by 2020. If indeed the aim is to meet the needs of developing countries – including some USD70-100bn for adaptation only – we believe that grant-based official assistance should make up for the totality of the USD100bn commitment.

The pool of contributors could be expanded beyond crisis-hit OECD economies while respecting the principle of “common but differentiated responsibilities”. A critical part of making climate finance effective will also be based on the democratic and open design of the Green Climate Fund.

Given the sizeable need for grant-based financing, international funding of mitigation and adaptation policies must be broadened and supported by new sources of financing, both nationally and globally.

Carbon-related taxation in developed economies must be stepped up as part of broader industrial policies toward a low-carbon, low-emission economies.

The tax base for international climate finance can and should be broadened beyond carbon taxation in developed economies to include the financial sector. Various forms of financial taxation mechanisms could be introduced.

The creation of a global Financial Transactions Tax (FTT) would considerably enhance the tax base of governments to match the global mobility of capital worldwide.

Institutional investors can and should have a complementary role given the change in scale in climate finance that is needed. That role should indeed add on, and not substitute to public financing.

Pension funds in particular represent an important class of asset owners and one with which trade unions have a special relationship. Our calculations suggest that pension funds’ net contribution to financing of climate change projects could reach USD300bn in 2015 – if by that time portfolio exposure to climate change reaches 5%.

Beyond that there are important barriers that need to be overcome for the financial sector to effectively contribute to climate change financing. Transparency and accountability should prevail throughout the investment chain.

Any public support to private sector should be ruled by clear and fair risk-sharing arrangements that preserve public interest and public services in developing countries. “Leveraging” private finance must not transform into subsidising bankers and asset managers.

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The global public good resource gap

1. The current global policy agenda faces two major challenges. One is with the absence of a strong multilateral framework for effective action to tackle major global public good challenges, including climate change adaptation and mitigation, but also poverty reduction and access to social protection. This has several consequences, including the lack of a compliance mechanism for realising the financial commitments made by the developed world in a variety of fora. The other major challenge is the rise of budgetary constraints post-crisis in many developed countries which could weaken their capacity to fulfil old and new commitments.

The USD100bn target by 2020

2. Developed countries' commitments to climate finance are outlined in the United Nations Framework Convention on Climate Change (UNFCCC) and its Annex II list of countries and following the Conference of the Parties (COP) 15 and COP 16 decisions in Copenhagen and Cancun respectively. They committed to "mobilise" USD100bn "from a variety of sources" and "by 2020" to finance climate change adaptation and mitigation. They also committed to raise new and additional financial resources amounting to USD30bn annually for 2010-2012 as part of the "fast track finance" initiative. Progress has been very limited since then. The use of vague language on the precise of sources of financing in the COP decisions ("they could be public *or* private, grants *or* loans") as well as unclear guidance on the extent to which large emerging economies should contribute were unhelpful in this regard.

3. At the time of writing the starting point to this discussion is the report by the co-chairs of the UNFCCC work stream on long term finance, issued weeks prior to the COP18 held in Doha November-December 2012 (UNFCCC 2012). The key recommendations by the co-chairs included:

- The need for a *political process* to be triggered in order "to clarify how developed countries will (...) mobilize USD 100 billion per year by 2020" (#10);
- The need to "increase and improve information on climate-related financing needs in developing countries" (#11) and to ensure "*tracking of climate finance* – both public and private – (...) be strengthened" (#12);
- The need to "enhance *enabling environments* in many developing countries (...) in reducing investment barriers and using climate finance effectively" (#13).

4. In addition, the report includes specific proposals to help "scaling up" international climate finance, including:

- The necessity of a carbon price at USD20-25/ton CO₂, and the repeal of fossil fuel subsidies;
- The creation of a joint COP / ICAO (aviation) / IMO (maritime) working group on bunker fuels;
- Engaging the Board of the yet-to-be-capitalised Green Climate Fund into an active dialogue with private sector groups and representatives.

International climate finance comes on top of past commitments

5. For unions however, the starting point is to be found in the context of past and current commitments to finance other global public goods. Regarding poverty reduction in particular, OECD countries have already committed, but so far have failed to raise Official Development Assistance (ODA) to 0.7% of their Gross National Income (GNI). Given the COP principle of "additionality", any international climate finance commitment would come on top, and not be lumped with previous ones, including the 0.7% GNI target for ODA. Climate change is an additional burden for poor countries, requiring additional resources.

6. ODA amounted to USD133.5bn in 2011, of which some USD21.7bn (16%) were specifically targeted at climate change (of which USD8.6bn in adaptation and USD13bn in mitigation). Our calculations would then suggest that some USD160-180bn would be missing annually for poverty-related ODA (excluding CC-related ODA) to meet the 0.7% GNI target in the years to come. Considering the current CC-related ODA flows (USD21.7bn) the funding gap to meet the USD100bn by 2020 would range in between... zero (if all additional

inflows come from purely private finance sources) and USD80bn (all additional inflows come from official assistance only).

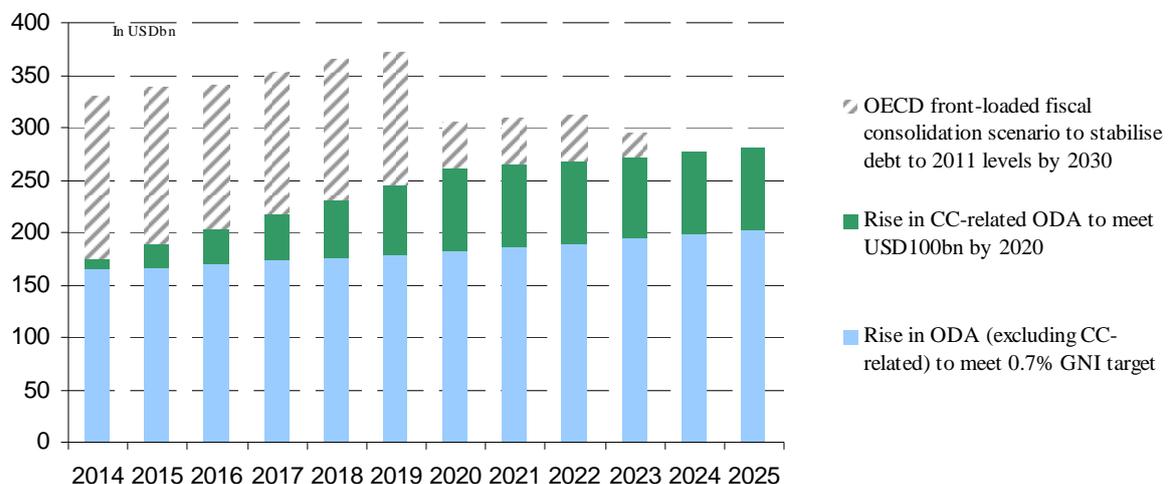
7. These calculations do not account for other current or future global financial commitments such as access to universal social protection floors and to health. They also reflect commitments, and not the real needs of the developing countries. There are various estimates and projections for the true cost of adaptation and mitigation measures that would be required, all of which far surpass the USD100bn figure. Some indicate that “at least USD150bn per year is needed in *public finance* alone from 2013, rising to at least \$200bn per year by 2020” (Oxfam 2012). The above co-chairs’ report refers to recent World Bank and UNEP estimates according to which developing countries financing needs for adaptation *alone* would reach no less than USD70-100bn annually. Other estimates suggest that the total needs (adaptation & mitigation) would at minimum reach USD156bn annually. Naturally the longer is the process for delivering past commitments the greater becomes the cost of adaptation and mitigation future needs.

Austerity would kill growth and global public good commitments

8. The trade union movement strongly believes that there is a way out of the current global economic crisis that does not put the burden on working families through “front-loaded” austerity measures and cuts in public services – as advocated by the European Commission, the OECD and the IFIs. Front-loaded fiscal consolidation consists in concentrating the bulk of the budget efforts – cuts in public expenditure and/or tax rises – in the first years of the programme. Austerity would kill growth, deepen the recession further while at the same time intensify financial market turmoil.

9. Should this type of austerity policy prevail, the state of OECD public finance would become very bleak. Based on OECD projections (OECD 2012), our calculations suggest that the financing needs for OECD economies to stabilise public debt at current levels by 2030 through front-loaded austerity measures would amount to some USD140bn / year during 2014-2018. When combined with the above global public good gap – ODA reaching 0.7% of GNI and gradual increase in CC-related grants to meet USD100bn target – the total financial requirements would amount to some USD350bn annually as shown in graph 1.

Graph 1: Teal and committed ODA and climate change financing in context of front-loaded austerity measures (2014-2025)



10. Budget cuts and fiscal consolidation initiatives must not be used as an excuse to avoid climate finance or any other international commitment. Economic growth is needed to facilitate fulfilling past commitments. Turning away from austerity is needed if growth is to be maintained, but also if indeed developed countries are to meet their global public good commitments. In addition to shifting from austerity to stimulus, innovative solutions must be found, including the reform of domestic and international taxation policy.

The need for a political process

11. Should developed countries adopt a very flexible and pro-business understanding of what “mobilising” climate finance would consist in, then the task of meeting the USD100bn in fact is relatively straightforward, if not trivial. USD100bn may be a lot of money from a real economy perspective – foreign direct investment flows to the developing world China excluded were USD560bn in 2011¹. But it compares little when set against the massive wealth accumulated by large corporations and the financial sector wealth post-crisis. For example in 2011 the combined profits of the Fortune 500 companies was USD824bn² and the top ten hedge fund managers earned a combined net income of USD9.75bn³. Meanwhile the environmental damage created by the blow-out of British Petroleum’s Deepwater Horizon oil rig on 20th April 2010 was evaluated at USD40bn alone.

12. If the USD100bn is to be met by private sector finance alone – something that the labour movement strongly object – governments would simply need to turn the GCF into a “mega” climate investment fund, ensure that asset managers and bankers have direct and unrestricted access to the fund behind closed doors, adopt very loose criteria for determining what project and asset would to qualify for adaptation and for mitigation and finally not least push developing countries further toward eliminating any form of barrier to foreign investments. “Mission accomplished”, so to speak.

13. But that is not how the UNFCCC decisions were framed. These were based on the needs of the developing world, not on private finance terms, and they were based on a “balanced” distribution between adaptation and mitigation. That is why a political process on the sources of revenues is needed and as recommended by the co-chairs’ report. For trade unions, official assistance in the forms of grants should make up for the totality of the USD100bn target if, indeed, commitments are to meet the needs of the developing world.

Adaptation needs adequate grant-based funding

14. UNFCCC decisions endorsed a “balanced” distribution of financial flows between mitigation (emission reductions) on the one hand and for adaptation (actions to increase resilience to climate change) on the other. In reality a majority of flows has been directed to mitigation measures. The cause for this unbalance might be found in the fact that profits and returns on investments are more likely to be found in emission reduction investments than in adaptation measures –crucial for sustaining the development of the poorest countries. Rather than a vague principle of balance, there should be a mandatory requirement for half of

¹ <http://unctadstat.unctad.org/TableViewer/tableView.aspx?ReportId=88>

² http://www.huffingtonpost.com/2012/05/07/fortune-500-company-earnings_n_1497593.html

³ http://www.forbes.com/lists/2012/hedge-fund-managers-12_land.html#fulllist

climate-related official assistance to be directed to adaptation. Grants (tax-financed), not loans (market-financed) are needed for adaptation.

15. The lack of financing for adaptation is particularly worrying because it is the poorest and the most vulnerable populations who then pay the price for the financing gap. It further goes against the UNFCCC principle of “common but differentiated responsibilities and respective capabilities” for which climate finance should be distributed by accounting for its incidence on each developing country, and by giving priority to the most vulnerable groups.

Expanding the list of contributors

16. Developed countries have committed to international climate finance. The rationale for this list is clear: these are the countries that have been identified as major contributors to the current concentration of GHG in the atmosphere and considered as those having the greater capacity to help the developing world cope with the consequences of GHG concentrations.

17. A significant number of developed countries however are under heavy budget pressure. This situation requires that developed countries that are not or are less under fiscal pressure than others raise the ambition of their respective financing commitments. Beyond this group, some of the largest emerging economies have already indicated their willingness to contribute to climate finance. This is of major importance because it would surely help climate finance go beyond the levels foreseen by COP agreements.

Governing the resources

18. A critical part of making climate finance effective will also be based on the democratic and open design of the Green Climate Fund. While this paper does not deal with the GCF specifically, it is important that the Fund be governed by a transparent and democratic framework including a voice for civil society organisations. The Fund’s investment policy should include social safeguards – including the compliance with ILO Core Labour Standards – and have strict rules for risk sharing arrangement with private sector operators through the Private Sector Facility. It should be guided by two principles: adequacy of financing in volume and predictability and fair distribution of funding raised bases on those who pollute the most and who have a higher capacity to pay.

How to deliver long term finance

19. On the short term, developed countries need to shift away from austerity policies. To fulfil medium term commitments developed economies need to grow. Austerity kills growth in the developed countries, and international climate finance abroad. The COP should also engage a political process to clarify the sources of revenues that should finance the USD100bn target in 2020. If indeed the aim is to meet the needs of developing countries – including some USD70-100bn for adaptation only – we believe that grant-based official assistance should make up for the totality of the USD100bn commitment. This process should also investigate the extent to which the pool of contributors could be expanded beyond crisis-hit OECD economies while respecting the principle of “common but differentiated responsibilities”.

20. This political process should go hand in hand with effective budget transparency and reporting – to ensure principle of additionality is fully respected (notably vis-à-vis the commitment for ODA to meet 0.7% of GNI) – and with the setting of clear metrics for assessing progress and ensuring funding effectively qualify for mitigation and adaptation in the developing world. Finally the governance and design of the Green Climate Fund would need to meet minimum adequacy of financing and fair distribution objectives and ensure civil society representation.

21. On the medium term however, and given the sizeable need for grant-based financing, international funding of mitigation and adaptation policies must be broadened and supported by new sources of financing, both nationally and globally. Carbon-related taxation in developed economies must be stepped up as part of broader industrial policies toward a low-carbon, low-emission economies. But beyond carbon taxation, the international community should agree on new innovative financing mechanisms that are not linked to carbon-behaviour, including substantially increasing financial sector taxation. In our view however the creation of new innovative finance mechanism is not an “option” anymore considering the state of public finance across OECD economies. It has in fact become a pre-requisite if indeed long term commitments are to be respected and if private finance (resources that the developing world would somehow need to repay) is not to substitute to public finance and to grants.

Carbon taxation

22. Research suggests that between USD44bn and USD89bn could be collected annually via: (i) the repeal of existing subsidies that benefit the fossil fuel sector, (ii) general carbon taxation in developed economies, and (iii) international carbon taxation for the maritime and airline industry.

Table: IFI & OECD estimates of new sources of international climate finance

	Revenue base (USDbn)	Share of climate finance allocations (%)	Share of international climate finance flows (USDbn)
Carbon Pricing (\$25 per ton CO ₂) in Annex II countries	250	10-20	25-50
MBIs for int'l aviation/maritime fuels (\$25 per ton CO ₂)	22	33-50	7-11
Fossil Fuel Subsidy Reform	40-60	10-20	4-12
EU ETS auction revenues & CDMs			8-16
Total			44-89

Source: AGF 2010, G20 2011 & OXFAM 2012

23. Domestically, carbon pricing in developed economies is a powerful mechanism for changing industry and market behaviour by putting a charge on externalities created by GHG emissions. It would also help send the right ‘price signal’ to investors because it would indirectly lift the profitability of clean energy projects. The development of domestic carbon taxation (at \$25 per ton of CO₂) across OECD economies could unleash some USD25-50bn in climate finance revenues according to the co-chair’s report sources. In the same vein, the repeal of fossil fuels subsidies could generate some USD4-12bn.

24. International aviation and shipping taxation would also make sense given the global dimension of these sectors and their role in generating carbon emissions. Some USD7-11bn could be collected for international climate finance. But it needs to be universal in scope if it were to be efficient and would require appropriate compensation mechanisms to address equity concerns in developing countries.

25. To the above one should add the auction revenues generated by current carbon offset mechanisms, such as the EU emissions trading schemes. According to Oxfam, the EU ETS auction revenues could reach some USD25bn per year (with an emission reduction target of -20%) and USD34bn (-30% target). This in turn would free up some USD7-9bn per year for international climate finance. In the same way the increase in the “share of proceeds” beyond 2% of the revenues drawn the sale of certified emission reductions through the Clean Development Mechanism could raise some additional USD1-5bn.

What Just Transition would mean for carbon taxation

26. The political feasibility of developing a global coherent framework for carbon taxation is a challenging one. The situation that prevails today is one of fragmented carbon regimes, and increasing disputes on trade grounds. Importantly carbon taxation is a tax on the real economy and as such must be accompanied by measures that ensure its fairness within society. Carbon taxation should help reduce, not increase income inequalities. Many consumption-related fossil fuels subsidies for example have a legitimate social purpose. Putting an end to these subsidies would require introducing financial compensation schemes for that protect low- and middle-income households. Similar approach should prevail for job-creating small businesses.

27. More broadly carbon taxation in developed economies should be accompanied by ‘Just Transition’ policies toward greening industries, the need for active labour market policies – including re-skilling of the labour force – and social protection measures to help workers integrating new companies, the design of social dialogue mechanisms, local diversification policies, etc.

28. If the potential for raising international climate finance through carbon taxation is real and should be acted upon, the net revenues generated might be lower than expected considering the need for compensation mechanisms both to stimulate clean investments and to mitigate the social impact. And that need might not decrease in the future considering that current social protection and safety nets are already under pressure as a result of the global recession. Increasing the sources for international climate finance should not come at a cost of growing inequalities.

Changing scale on financial sector taxation

29. The tax base for international climate finance can and should be broadened beyond that of climate-related measures to include the financial sector. Changing the scale of financial sector taxation would be needed for regulatory purposes – curbing financial speculation, ensuring the financial system is serving, not dominating the real economy. It is also needed because it would help make the financial system pay its share of the financing burden of public services and public goods. Today’s reality is somewhat different: the case for the current “under-taxation” of the financial system is in fact one that is difficult to

oppose. Financial services are most often exempted from Value Added Taxation (VAT) which represents by far the largest source of government revenues in developed economies. The financial system is also a major source of tax evasion. Tax havens are first and foremost offshore financial centres. The uncontrolled growth of the shadowing system in the past decade and the wave of “financial innovation” – including the ‘subprime’ structured credit products that triggered the current crisis in 2008 – were fuelled by ‘tax arbitrage’ and ‘tax optimisation’ objectives.

30. There are various forms financial taxation mechanisms that could be introduced or enhanced further: the Financial Transaction Tax (FTT) to curb speculative trading behaviour, the Financial Activity Tax (FAT) to redress the VAT-exemptions that benefit financial services, and/or the Financial Stability Contribution (FSC, or ‘bank levy’) to limit excessive leverage of the balance sheet of “too-big-to-fail” financial conglomerates. These different financial tax mechanisms complement each other.

Taxing financial transactions

31. The creation of a global FTT, or the coordinated implementation of several regional and national FTTs, would considerably enhance the tax base of governments and ensure that it matches the global mobility of capital. A global FTT could generate some USD400-500bn annually. The European Commission proposal for a “coordinated FTT” could raise some USD47bn annually among those EU countries that have recently agreed to its implementation. Considering that a quarter of the FTT revenues would go to climate change, this FTT would free up some USD12bn annually to finance the commitments made by the EU countries that participate in the FTT scheme. Part of that funding could be directed toward collaterals to finance government guarantees on the issuance of ‘green bonds’ and on clean energy infrastructure funds which would be badly needed as discussed below.

32. Likewise carbon taxation however, there should be a global harmonised framework for financial sector taxation. Many Annex II countries and the largest emerging economies are opposed to the EU-style FTT – including the US, Japan, Canada, Australia, the UK and all the BRICS: Brazil, Russia, India, China and South Africa. Yet the same governments that oppose the FTT are not offering alternative plans for increasing financial sector taxation.

Mobilising responsible long term asset owners

33. The IFIs and the G20 Finance ministers see a lot of potential in the rise of private climate finance. Climate Investment Funds could attract some USD30-40bn annually – we are told – while “other private flows” could generate another USD100-200bn annually (AGF 2010 & G20 2011). Excessive attention given by some governments to the involvement of the private sector raises concern however, as these could be seen as an attempt to delegate public responsibilities and commitments to the private sector. Governments and publicly accountable financial institutions have the prime responsibility to ensure proper financing of mitigation and adaptation policies. By opposition private investors and corporations will only invest in projects for a profit. There is little profit to be made by helping poor people adapt to climate change. Some specific adaptation projects can indeed fit a private sector approach – such as micro-credit and community-based insurance systems – but the vast majority of adaptation measures will simply not.

34. Trade unions agree that institutional investors can and should have a complementary role given the change in scale in climate finance that is needed. But that role should add on, and not substitute to public financing. Importantly any UNFCCC discussion on the role of “private sector finance” should at its core clearly distinguish between asset owners – including pension funds, insurance companies, sovereign wealth funds – and asset managers – including bank asset management branches – and give pre-eminence to the former over the latter as a matter of accountability and prevention of conflicts of interest.

5% of pension funds’ portfolio allocated to climate change finance

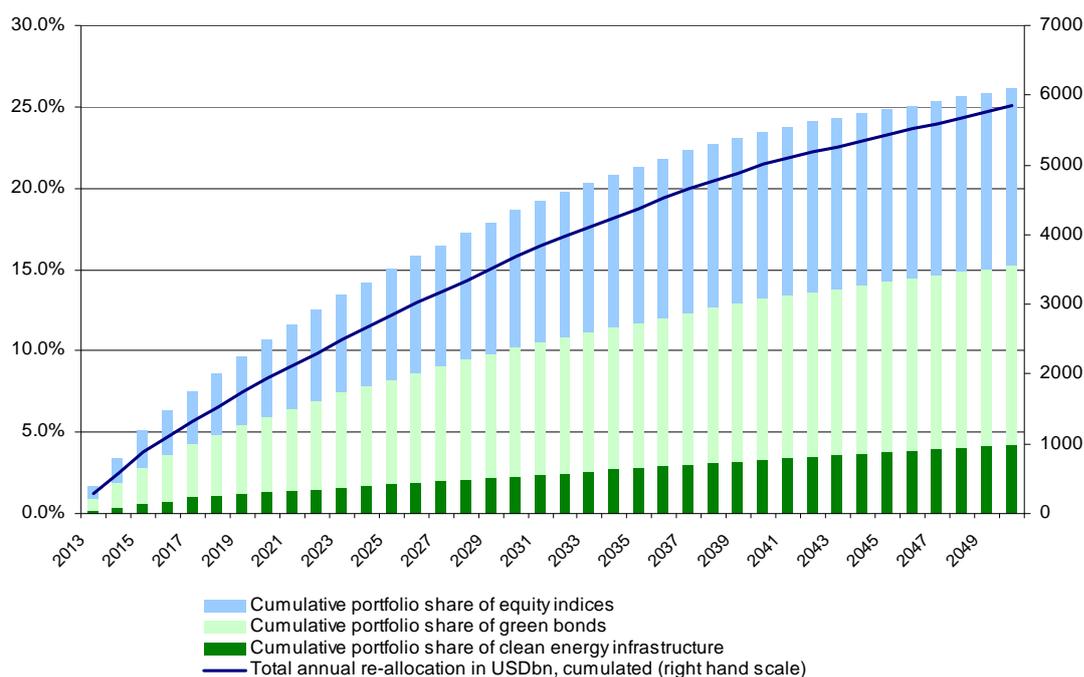
35. With over USD30tr assets under management pension funds represent an important class of asset owners and one with which trade unions have a special relationship. They have a social purpose, that of financing workers’ right to retirement and most often they are established as part of a collective bargaining agreement and include union representatives on their board of directors (the “pension trustees”). There is wide consensus on the need for workers’ pension money – of which 90% are managed in developed economies – to shift away from short term to long term investments and to help promote responsible investment practices – integration of environmental, social and governance criteria in the design of the investment policy, greater exposure infrastructure and job creation projects, etc. Climate change-related assets fit very well on all these aspects. Not only that the long term horizon of climate change finance also happens to match the liability profile of pension funds, which extends beyond 20-30 years (ie. the time needed to accumulate capital to finance workers’ right to retirement).

36. Current pension leaders in green investments are in fact trade union-friendly in so far as they are based on collective agreements and have trade union pension trustees on their boards: Danish ATP, US CalPERS & CalSTRS, Dutch ABP and PGGM, Swedish APs and several industry funds in Australia to mention a few. The recent decision by the South African Government Employees Pension Fund – another pension fund with strong union-representation on its board – to invest R1bn in green bonds is another example hereof.

37. In order to deepen this movement, ITUC and the TUAC have undertaken calculations to identify the potential for pension funds’ contribution to climate finance, in particular to clean energy and clean infrastructure investments⁴. Our calculations suggest that pension funds’ net contribution to financing of climate change projects could potentially reach USD301bn in 2015 if by that time portfolio exposure to climate change reaches 5% of which 0.6% would be invested in private infrastructure funds, 2.3% in green bonds and 2.3% in environmental focussed equity indices. Cumulated flows would then reach some USD2tr around 2020 and USD3.7tr by 2030.

⁴ For further information, see ITUC/TUAC background paper: “What role for pension funds in financing climate change policies?” May 2012 <http://www.ituc-csi.org/what-role-for-pension-funds-in,12358.html>

Graph 2: Pension funds’ potential for financing climate change-related assets in share of portfolio and in cumulated net annual flows 2013 - 2050



Source: ITUC & TUAC 2012

38. These projections are based on conservative assumptions: (i) only the larger public and private pension schemes – accounting for approximately half of worldwide pension assets – would have the flexibility and capacity to re-allocate and (ii) portfolio exposure per asset class remains within prudential norms throughout the period. Reaching 5% exposure is a realistic objective in the next three years. There are however several challenges and barriers that would need to be addressed and overcome to sustain this financial contribution beyond three years. These barriers are not on the demand side, they are on the supply side.

Distinguishing between productive and speculative risks

39. The most challenging obstacle is related to the limited access to climate change investment products. The current green bond market value (i.e. the stock) is estimated at USD16bn, “a drop in the ocean” of the +USD95tr world bond markets, while annual green bond issuances (i.e. the net inflows) are in the range of USD1-2bn (compared with some USD6tr worth issuances of ‘normal’ bonds). The Green Climate Fund could play a key role in promoting green bond issuances. Insurance-type derivatives could also help managing and mitigating risks that are specific to climate resilient low carbon projects, if – and that is a big if – they are properly regulated and supervised by authorities.

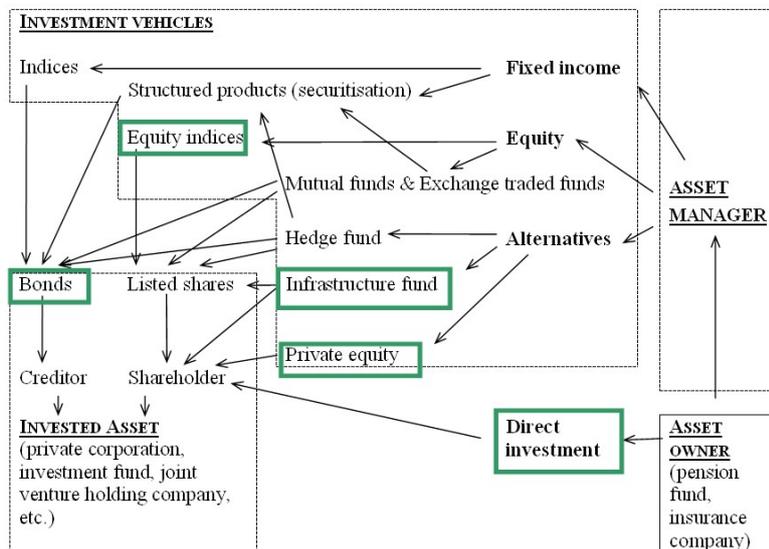
40. Pension funds are tightly regulated financial institutions when it comes to the risk management of their portfolio. Because they aim at financing a social purpose – workers’ right to retirement – they cannot take excessive risks in the choice and design of their investment policy. Climate assets however may entail a higher degree of investment risk than comparable ‘brown’ investments (due to the use of recent or unproven technologies, uncertainty and inconsistency of regulations and policies, cross-border investment risks). Government and lawmakers should ensure that pension fund regulation, but also insurance regulation are adapted to facilitate investment in clean energy and other CC-related assets.

41. A central question to raise in this context is whether the post-crisis wave of financial reforms – as legitimate as they may be from a financial integrity and stability perspective – may have had some unintended consequences for private financing of clean energy and mitigation projects. In particular the need to limit both risk taking behaviours and leverage levels in the financial sector – as aimed for, and for a cause, by several financial reforms – could hamper the capacity of institutional investors to re-allocated money to the green economy. In order to avoid any conflicts between financial stability and climate change objectives it would then be most appropriate for policymakers and regulators to distinguish between ‘productive risk’ (or ‘good risk’) and ‘unproductive’ or speculative risk, when setting or reviewing prudential norms for banks and insurance and funding rules for pension funds. Such distinction⁵ would help create the right incentives for investors to allocate to long term investments including clean energy and mitigation projects.

Ensuring accountability throughout the investment chain

42. The lengthening of the “investment chain” between asset owners – including workers’ pension funds – and invested assets constitutes another form of barrier to private climate finance. The multiplication of intermediaries (asset managers and the many consultancies that swirl around) and the growing “fragmentation” of markets (trading increasingly taking place outside regulated and supervised exchanges) are creating major complications for investors who wish to ensure proper accountability of how their moneys are being invested. Beyond the short term target of a 5% exposure of pension funds to CC-related assets, regulators would need to increase transparency and reporting requirements all along the investment chain so as to ensure that funding for climate change are effectively channeled to that end.

Graph 3: the lengthening of the investment chain



Source: ITUC & TUAC 2012

Leveraging private sector or... subsidising it?

43. On the short term, considering the regulatory challenges ahead the best way to ensure green finance becomes or remains attractive for pension funds is to enhance government guarantees on financial assets such as green bonds and on clean energy investment funds. The most common form of government guarantee is the public guarantee on the credit default risk

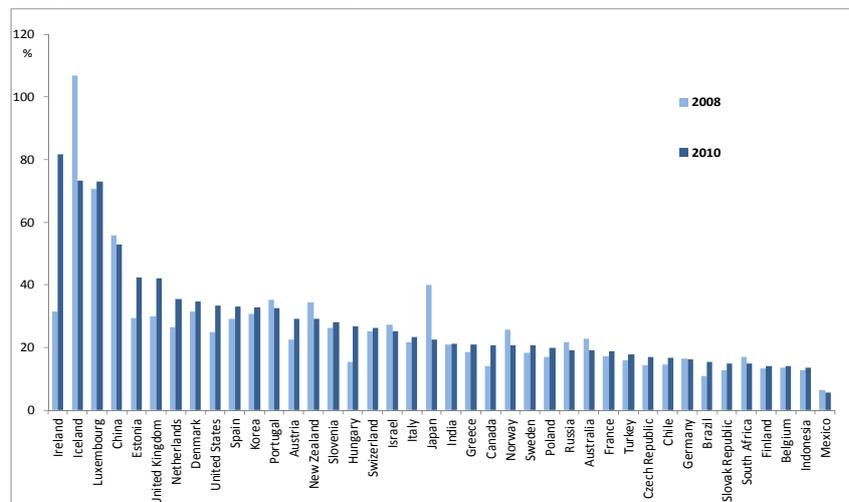
⁵ See for example LAZONICK & MAZZUCATO 2012

of a green bond. Such guarantee allows a green bond to be rated ‘AAA’ (and hence be illegible for investment by pension funds and other institutional investors) whereas its ‘stand alone’ rating would be closer to a BBB rating. With a few notable exceptions all green bond issuances to date have been accompanied by explicit guarantees by governments, by regional development banks or by the World Bank.

44. Government support to green financing can take other forms: subsidised low-interest direct loans, export credit insurance and facilities, foreign exchange risk insurance and subsidised support services to investment deals. Government-funded/run venture capital fund can also take “first equity loss” positions in green private investment deals. All these forms of public support to private deals already exist and are quite common under Public-Private Partnerships (PPP). However trade union experience with PPPs suggests that public support for private financing does not come free for governments and their citizens⁶. From a trade union point of view it is also clear that private infrastructure financing – however ‘green’ it is or becomes – would still be of concern if it directly or indirectly leads to privatisation or weakening of public services. Best practice for testing the extent to which risk-sharing arrangements under a PPP project are in line public interest consists in always applying a “public sector comparator” that is: comparing the costs and benefits of a given PPP project with the alternative solution of public sector procurement.

45. The use of government guarantees benefiting the financial sector should also be contemplated in light of the massive post-crisis government backed rescue package that have benefited the banking sector. As evidenced by OECD experts and shown in the graph below, government guarantees and other forms of contingent liabilities are equivalent to 20-30% GDP for most OECD economies and have grown substantial between 2008 and 2010. The underlying issue is whether these massive public guarantees benefiting bankers have not in effect transformed the entire industry into a publicly subsidized business. Andrew Haldane (2010) of the Bank England estimates that the explicit and “implicit” public guarantees represented a net saving of some USD160bn in 2009 for 13 banks in the UK alone. The Swedish central bank (2011) estimates that the average yearly reduction in funding costs for the four largest Swedish banks amounts to some USD4.5bn.

Graph 4: the rise of contingent liabilities in GDP % across G20 economies between 2008 & 2010



Source: SCHICH & KIM 2011

⁶ See TUAC 2010

46. There are good reasons to support and indeed expand government guarantees to help increase private financial flows, including pension funds' portfolio money, to climate change investments. However past experience with PPPs and more recently the post-2008 bailing out bankers show that government guarantees is a delicate policy issue. Importantly the need for "leveraging" private finance should not be mixed with, or transformed into some unconditional subsidisation of bankers and of asset managers, and/or situations in which profits and gains are privatised, while deficits and losses are socialised.

Conclusion

47. If the international community is to be serious about filling the current gap in climate finance while meeting the needs of the developing world, then there is no real alternative to ensuring that the US\$100bn target by 2020 is reached through official public assistance, not by loans. For that to happen the tax base of climate finance needs to be considerably broadened. This paper explores two avenues: (i) the development of a coherent framework for carbon taxation and (ii) the need to change scale regarding financial sector taxation. It will not be possible to rise to the challenge of international climate finance, if little or insufficient progress is achieved on either fronts.

48. This paper also shows that private finance can complement but not substitute to current climate commitments. In fact reaching 5% portfolio exposure to climate change-related assets by large pension funds in the coming three years is, we believe, a realistic objective. But beyond that, more work by policymakers and regulators need to be done to ensure global finance meets minimum transparency and accountability standards, "leveraging private finance" does not transform into subsidising bankers and asset managers, and public support to private finance does not weaken in any way the development of public services in developing countries.

Source

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