

Climate Finance Advisory Service (CFAS) - Response to Query

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Query 8/2013:

"The Governing Instrument of the GCF states that "the Fund may employ results-based financing approaches, including, in particular for incentivizing mitigation actions, payment for verified results, where appropriate." In the discussions at the 4th GCF Board meeting, also the term "performance-based payment" has been used.

How are the terms "results-based" and "performance-based" defined in general, is there a difference? What types of categories of results-/performance-based financing are there, for mitigation and for adaptation? What are their opportunities, what are their limitations?"

Confidentiality: non-confidential

1. Terminologies

Results-based funding or results-based financing (RBF) can be regarded as "a form of Payment by Results and generally refers to the delivery of national or sub-national outcomes and outputs".¹

The objectives can include "to increase accountability and incentives for delivering and sustaining results, improve the effectiveness and efficiency of government-owned sector programs, promote institutional development, and enhance development effectiveness."²

Pearson argues that "Results based funding means different things to different people. There is no commonly agreed definition and different agencies use different terms (e.g. results based aid, payment by results, performance based aid, output based aid) to describe what are similar, and sometimes identical, concepts."³

We could not determine a clear difference between results-based funding and performance-based funding. However, a distinction might be made between *output*-based financing, which addresses payments after pre-agreed actions have been achieved and verified⁴, and *outcome*-based financing linking finance to verifiable results in the form of outcomes (e.g. at the national level).⁵ For instance, *output-based* financing could be related to the achievement of the installment of a renewable energy facility, while *outcome-based* financing would in this case be related to the avoided emissions with the renewable energy facility.

¹ https://energypedia.info/wiki/Results-Based_Financing

² <http://www.adb.org/sites/default/files/results-based-financing-r-paper.pdf>

³ <http://www.hlsp.org/LinkClick.aspx?fileticket=tdqKrWX321Q%3D&tabid=1570>

⁴ <http://de.slideshare.net/GPOBA/results-based-financing-mechanisms-experience-from-output-based-aid> [slides are also from this]

⁵ https://energypedia.info/wiki/Results-based_aid

Examples for *output-based indicators in the mitigation area* in a project which intends to build a renewable energy facility, could for instance be

- Number of awareness raising trainings carried out for surrounded local communities
- Number of stakeholder consultations undertaken
- Number of training for the locals to be able to maintain and operate the facility
- Installation of the facility finalised

Further examples for *indicators in the field of adaptation* for a project focusing on coastal protection program such as mangrove plantation could for instance be:

- Number of local people trained in awareness raising events on the impact of climate change, especially for coastal areas
- Number of stakeholders consultations undertaken on what kind of measures they are able to do and willing to do
- Results of trainings undertaken on how to use some relevant equipment, how to maintain it, and how to generate funds for maintenance of the equipment.

Key aspects for both, *output-based* funding and *outcome-based* funding, are:

- Disbursement of funds is linked to the delivery of pre-determined results (outcomes or closely related outputs). The achievement of these pre-determined results could for instance be measured by using pre-defined indicators.
- As far as possible, recipients have discretion over how results are achieved.
- (Ideally independent) verification acts as the trigger for disbursement.
- Different modalities may be applied regarding the flexibility of releasing funds in case the envisaged results are not fully met, which may be due to a variety of internal as well external reasons.

Result-based funding can include both grants and lending or other financial instruments, and the way these instruments are designed can reflect the results-based funding. For example, depending on the results the implementing organizations achieves, loan conditions could be varied, such as that overachievement of results leads to better loan conditions.

2. Approaches in the context of climate change

2.1 General approaches

In general, result based financing can be applied through different modalities. It could for instance include the release of the next funding tranche only against the progress report which assesses the project's progress against certain parameters, which can be on the output or outcome level. This is e.g. practice applied in the Adaptation Fund and the Global Fund to fight HIV/Aids, Tuberculosis and Malaria. This may also be connected to (independent) evaluations which can be regarded stronger with regard to validation or verification of the information provided.

Overall examples for result based financing are included in Annex 1.

Yet there are also more specific aspects to take into account for the climate action areas of mitigation, REDDplus or adaptation.

For both outcome-based funding and output-based funding, indicators would need to be identified ex ante in order to be able to measure, report and where required verify the progress.

2.2 Specific approaches for mitigation

On mitigation, result-based funding could be applied as an incentive. This could give the freedom for countries to design their own mitigation action plan without any intervention from other countries, i.e. donor countries. What is needed is a monitoring, reporting and verification (MRV) system that could MRV for instance the amount of carbon reduced in one particular project. Results-based funding will be delivered after the project proofed to be able to achieve the intended output / outcome.

A combination between ex-ante grants/concessional loans and result-based payment (ex-post grant) would give developing countries both the capital for starting the project, as well as an incentive that they will receive further funding after they have implemented the project and achieved the desired result, which can be measured for instance through the greenhouse gases emission monitoring report. This can enable recipient countries to gradually move towards low carbon development.

However, there should be a concrete agreement on the terms of payment, the amount of payment, as well as the methodology to measure the achievement of the intended output/outcome. Based on the results achieved, the recipient organization would then receive the payment.

One example is the Clean Development Mechanism. The project developers would only get the revenue after they have completed a mitigation action, where its greenhouse gases emission reduction has been measured, and verified. After it is verified, and the Certified Emission Reduction (CER) is released, the project developer gets the revenue from the selling of the CER. However, results-based funding does in general not necessarily need any CER. As long as the indented output/outcome can be measured, reported, and verified, the project developer would get his/her payment.

2.3 Specific approaches for REDDplus

At COP19 in Warsaw, Parties agreed in regard to REDDplus on specific items related to results-based payment, which could also be of relevance for mitigation or adaptation activities. On the one hand, they agreed that all actions need to be MRVed in accordance with two specific decisions, namely FCCC/SBSTA/2013/L.33/Add.1 – which focusses on “Guidelines and procedures for the technical assessment of submissions from Parties on proposed forest reference emission levels and/or forest reference levels” – and FCCC/SBSTA/2013/L.33/Add.2, which focusses on “Modalities for monitoring, reporting and verifying”.⁶

Further, they agreed to establish “an information hub on the web platform on the UNFCCC website” where information on the funded activities “and corresponding results-based payments” shall be provided.⁷ Thus, this could potentially also generate valuable insights for mitigation or adaptation.

In addition, they requested the Standing Committee on Finance to consider “ways and means to transfer payments for results-based actions”.⁸

And finally, they requested the GCF to apply certain methodological guidance when it provides results-based finance.⁹ The methodological guidance shall be “consistent with decisions 4/CP.15, 1/CP.16, 2/CP.17, 12/CP.17” and the decisions focusing on “National forest monitoring systems”, “The timing and the frequency of presentations of the summary of information on how all the safeguards referred to in decision 1/CP.16, appendix I, are being addressed and respected”, “Addressing the drivers of deforestation and forest degradation”, “Guidelines and procedures for the technical assessment of submissions from Parties on proposed forest reference emission levels and/or forest reference levels”, “Modalities for monitoring, reporting and verifying” as well as the decision on the “Work programme on results-based finance to progress the full implementation of the activities referred to in decision 1/CP.16 paragraph 70”.¹⁰

2.4 Specific approaches for adaptation

In principle similar general aspects apply to result-based finance in adaptation as in the other areas. However, a specific challenge related to measuring outcomes is the lack of a “well-accepted, unitary, quantifiable measure of vulnerability to climate change that is applicable to all sectors”¹¹ which could therefore be used as a key, comparable metric to measure the results. A second challenge is that of baselines which are more difficult to determine, since the achievement of outcomes (and its verification) may for example depend on whether a weather disaster strikes the project region in the given project timeframe or not. Among activities within the same sectors or activity areas there may be greater opportunities for comparable metrics. Thus, there is a greater need to look at the specific aspects of an activity to be implemented and suitable indicators, as well as the potential reasons for non-compliance with the envisaged results.

No specific guidance exists by the UNFCCC on using adaptation indicators to measure results and release funds against their achievements. However, certain multilateral adaptation funds have developed various approaches related to these matters. The Adaptation Fund (AF) applies a form of result-based payment by releasing the next tranche of funding against the submission of usually annual project performance reports, in which project implementers also have to describe progress towards the envisaged targets for outputs and outcomes. These are reviewed by the Secretariat of the AF and accepted by the Board of the AF on a non-objection basis.¹² The LDCF/SCCF also monitors progress towards the envisaged results as part of its result-based management framework, but no information could be identified that this is directly linked to the release of funds and therefore does not fall under the category of result-based funding.

⁶ http://unfccc.int/files/meetings/warsaw_nov_2013/decisions/application/pdf/cop19_redd_finance.pdf, para 3; The two decisions can be found at: <http://unfccc.int/2860.php>

⁷ http://unfccc.int/files/meetings/warsaw_nov_2013/decisions/application/pdf/cop19_redd_finance.pdf, para 9

⁸ http://unfccc.int/files/meetings/warsaw_nov_2013/decisions/application/pdf/cop19_redd_finance.pdf, para 20 a

⁹ http://unfccc.int/files/meetings/warsaw_nov_2013/decisions/application/pdf/cop19_redd_finance.pdf, para 7

¹⁰ http://unfccc.int/files/meetings/warsaw_nov_2013/decisions/application/pdf/cop19_redd_finance.pdf, para 7. The decisions referred to can be found here: <http://unfccc.int/2860.php>.

¹¹ http://gcfund.net/fileadmin/00_customer/documents/pdf/GCF_B05_03_BMF_RMF_fin_20130919.pdf

¹² <https://www.adaptation-fund.org/page/project-performance-and-reporting>

3 Opportunities and limitations to results-based funding

Depending on their specific design, result-based funding approaches carry certain opportunities, but also risks.

Potential benefits of result-based financing (both output and outcome) may include:

- Existence of targeted outputs/outcomes, since the eligibility for the scheme is ex ante determined¹³;
- Strong focus on achieving results: there are incentives for all stakeholders to deliver the agreed activity /output/ outcome¹⁴;
- There is room for innovation and efficiency, since the actual outputs/outcomes of the activity are more important than the inputs¹⁵;
- Strengthening of institutional capacity: Result-based funding can "seek to strengthen key program systems, including monitoring and evaluation, fiduciary (financial management, procurement, and anticorruption measures), and safeguards. Institutional development will also include organizational and behavioral changes that strengthen accountability and incentives for results."¹⁶
- Opening up of partnerships: when the funding focus is not on a single activity, but on broader programme outcomes, different funders can contribute which allows for fostering broader partnerships

With regard to risks one could argue that the donor bears less risk than in the case of conventional financing approaches, whereas greater risk is placed on the recipient of climate finance. The advantage is that the recipient will face a stronger incentive to provide the results agreed upon between recipient and donor beforehand. If the recipient is able to respond to that incentive, and manages the risks that might otherwise threaten the delivery of the project, then this will increase the probability of delivery of the desired results. Hence, the donor benefits from the fact that (s)he can achieve a higher chance of result delivery with a given amount of resources.

The disadvantage is that additional risk is being placed on the recipient, which might mean that the recipient will ask for a higher reward as a sort of "compensation" for taking up this additional risk. Further there might be external risks which are outside the influence of the recipient, hence the occurrence of such risk – and what this means for the payment in case such external risk occurs – needs to be discussed beforehand between donor and recipient. It might be for instance that the less recipients are able to control the risks that threaten project success, the greater the "compensation" could be which they might require. Then the donor would need to balance the possibility that results-based financing approaches increase the probability of achieving a set of results against the likelihood that results-based financing approaches make delivery of these results more expensive.¹⁷

One major limitation to a results-based financing approach is that some project executing agencies do not have the financial or technical capacities they would need in order to provide the costs upfront.¹⁸ In order to overcome this, the above mentioned combination between ex-ante and ex-post financing might be needed.

¹³ <http://www.climateinvestmentfunds.org/cif/sites/climateinvestmentfunds.org/files/Results%20Based%20Financing%20Mechanisms.pdf>

¹⁴ <http://www.climateinvestmentfunds.org/cif/sites/climateinvestmentfunds.org/files/Results%20Based%20Financing%20Mechanisms.pdf>

¹⁵ <http://www.climateinvestmentfunds.org/cif/sites/climateinvestmentfunds.org/files/Results%20Based%20Financing%20Mechanisms.pdf>

¹⁶ <http://www.adb.org/sites/default/files/results-based-financing-r-paper.pdf>

¹⁷ „Results-based Financing in the Energy Sector – An Analytical Guide“, Energy Sector Management Assistance Program (ESMA), Technical Report, 004/13

¹⁸ „Results-based approaches in German Financial Cooperation“, Jonas Blume, Policy Division Governance, KfW, February 2012

3. Annex I: Examples of result-based funding

Scheme	Category	Short description
Global Fund (GFATM)	RBA/RBF hybrid	Funding for years 3 to 5 dependent on overall performance achieved during first two years of grant implementation.
GAVI Alliance – Immunisation Services Support (GAVI ISS¹)	RBA	Initial investment based on (self reported) number of children expected to be vaccinated in year 1. Subsequent reward payments of \$20 per child vaccinated above this baseline.
UK Quality and Outcomes Framework (QOF)	RBF	Payment made against performance by general practitioners in the UK against over a hundred quality based indicators.
UK Payment by Results (PbR)	RBF	Fixed payment (based on national average unit costs) paid to hospitals in the UK for delivering a specific health output (e.g. hernia operation).
US P4P (Pay for Performance)	RBF	Payment made to providers with level based on performance against a range of quality based output indicators.
Vouchers	RBF	Reimbursement made to accredited providers on the basis of services delivered to voucher recipients.
Conditional Cash Transfers	RBF	Payment made to targeted beneficiary in return for using specified services. Heavily focused in middle income countries using domestic funds.
Health Results Innovation Trust Fund (HRITF) *	RBA/RBF hybrid	Vehicle for supporting results based financing approaches. HRITF also focuses on raising resources and knowledge generation.
Global Programme for Output Based Aid (GPOBA) *	RBA/RBF hybrid	Multi-donor partnership and trust fund established to: i) fund and facilitate the preparation of OBA projects in which payment is made to an implementing agent (usually private sector but potentially NGOs, and usually in the utilities sector) for each unit of output supplied; and ii) document and disseminate lessons learned.
Poverty Reduction Budget Support (PRBS)	RBA	Payment made to government in return for commitment to good governance and satisfactory progress in poverty reduction. Variable or performance related tranche payments are a form of results based aid.
European Commission MDG Contracts	RBA	Payment made to government in return for commitment to good governance and satisfactory progress in poverty reduction. Variable tranche is a form of RBA. Schemes have been established but are new.
Cash On Delivery Aid (CODA)	RBA	A concept for making payments to government in return for achievement of specific results (e.g. increase in primary school enrolment). Yet to be established.
Millennium Challenge Account (MCA)	RBA	Payment made to government in return for demonstrable commitment to democracy, good governance, 'economic freedom' and pro-poor public services.

Source: Pearson, Mark, 2011: Results based aid and results based financing: What are they? Have they delivered results? HLSP Institute, to be found on: <http://www.hlsp.org/LinkClick.aspx?fileticket=tdqKrWX321Q%3D&tabid=1570>, retrieved on: 05.12.2013