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Finance

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Abbreviations

AF	Adaptation Fund
AfDB	African Development Bank
AFD	Agence Française de Développement
AGF	UN Secretary-General’s High-level Advisory Group on Climate Change Financing
BCCRF	Bangladesh Climate Change Resilience Trust Fund
CDM	Clean Development Mechanism
CDTF	Community Development Trust Fund
COP	Conference of the Parties
CSO	Civil Society Organization
EBRD	European Bank for Reconstruction and Development
ECBI	European Capacity Building Initiative
EIB	European Investment Bank
ESCO	Energy Service Company
GCF	Green Climate Fund
GEF	Global Environmental Facility
GEEREF	Global Energy Efficiency and Renewable Energy Fund
GHG	Greenhouse gases
GoK	Government of Kenya
IFC	International Finance Corporation
KCCAP	Kenya Climate Change Action Plan
KENSUF	Kenya Slum Upgrading Low Cost Housing and Infrastructure Fund
MRV	Monitoring, Reporting and Verification
NCF	National Climate Fund
NIE	National Implementing Entity
PCN	Project Concept Note
PoA	Programme of Activity
PPCR	Pilot Program on Climate Resilience

PPD	Project Proposal Document
RTAP	Regional Technical Assistance Programme
SCAF	Seed Capital Assistance Facility
SEFA	Sustainable Energy Fund for Africa
SME	Small and Medium-sized Enterprises
UECCC	Uganda Energy Credit Capitalisation Company Ltd.
UNDP	United Nations Development Programme
UNEP	United Nations Environmental Programme
UNFCCC	United Nations Framework Convention on Climate Change
VC	Venture capital
WSTF	Water Services Trust Fund
YEDF	Youth Enterprise Development Fund

1. Introduction

This section provides recommendations on the design of a Kenyan National Climate Fund (“the Fund”), which will represent a key element of the financing of the Kenyan Climate Change Action Plan. The Fund is intended to be the key mechanism by which international (and potentially domestic) public resources will be managed and channelled towards Kenya’s climate change response priorities.

The issue of the appropriate way to manage climate finance resources has gathered increasing salience given the commitment by developed countries ‘...in the context of meaningful mitigation actions and transparency on implementation, to a goal of mobilising jointly USD 100 billion per year by 2020 to address the needs of developing countries.’ If this goal is realised it will imply a significant increase in the scale of finance flowing from developed to developing countries to support low-carbon, climate resilient (and hence broader development) ambitions. Managing and disbursing these resources in an efficient and cost-effective manner will be crucial. In this regard, a number of other countries have already explored the possible role of so-called National Climate Funds (NCFs), including Brazil, Bangladesh and Indonesia. This paper explores this possibility, and sets out a design for such an NCF, in the Kenyan context.

This section forms one of a series that sets out the strategy for financing the Kenya’s Climate Change Action Plan (KCCAP). The focus on this section is on the management of international (and possibly national) public resources. A further part of the strategy (section C) provide recommendations on how the absorptive capacity of the Kenyan government may be increased to use more efficiently domestic and international resources. These recommendations will complement those surrounding fund design provided in this section and will also be relevant for any public climate finance resources that do not flow through the Fund. Section D provides recommendations for how Kenya may be able to continue to exploit carbon markets to engage the international private sector in mitigation activity; while Section E sets out a series of actions to improve the investment climate for climate investment so as to increase both domestic and international private sector resources devoted towards climate change activities. In this way, the sections collectively form a coherent set of recommendations that may scale-up all sources of climate finance so as to help realise the ambitions of the KCCAP.

The section is structured as follows: the next three chapters (3 to 5) describe barriers to low-carbon and climate-resilient investments in Kenya, set out the rationale for a National Climate Fund in Kenya, and outline our recommendations as regards the design of this Fund. The subsequent chapter consist of a draft “governing instrument” for the Kenya National Climate Fund. The recommended next steps conclude.

2. Kenya's mitigation and adaptation needs and barriers to their realisation

2.1 Kenya's priority mitigation and adaptation investment needs

The priority mitigation and adaptation needs for Kenya are being developed elsewhere in the Action Plan process (Subcomponents 1, 3 and Subcomponent 4).

The preliminary analysis from this work indicates that in terms of mitigation opportunities in the period to 2030 there is likely to be considerable emphasis on geothermal electricity generation in the power sector with a smaller role for landfill gas, solar PV and wind power while in the transport sector the fund may be called on to support the development of new public transport systems (light rail and/or bus rapid transit). Outside the infrastructure sector, the greatest mitigation potential lies in agricultural co-generation and improved charcoal manufacturing in the industrial sector (the latter also has very high development benefits), advanced cookstoves and efficient electrical appliances in the household energy demand sector (the former has very high development benefits).

In the agriculture sector, the greatest mitigation potential lies in agroforestry, followed by soil carbon sequestration and limiting use of fire in croplands and rangelands. All have high development benefits. In the forestry sector, options with high mitigation potential include regeneration of woody vegetation on degraded lands, afforestation of marginal agricultural lands, avoided deforestation and reforestation of degraded forest. All of the options, and especially the first two, involve trade-offs around land-use, for example, regeneration of woody vegetation on degraded lands means setting aside large areas of land currently used by pastoralists for grazing; afforestation of marginal agricultural lands could be difficult as farmers will be reluctant to reforest even non-productive land/marginal land. The latter two options have less negative impacts and greater positive impacts - enhanced biodiversity, reduction of soil erosion, maintenance of water towers - and may be more likely to be taken up.

In terms of adaptation actions, the immediate priorities (i.e. in the period to 2017) identified elsewhere in the Action Plan process include:

- integrating climate change risk assessments into investment appraisal and development plans;
- selected infrastructure investments e.g. design and implementation of a climate resilient Urban Electrification Programme, improving the Kenya Meteorological Department's observational network and digitising meteorological data and data rescue and ensuring rural and urban communities have access to safe water and adequate sanitation; and
- building adaptive capacity through, for example, implementing a research programme into climate resilient transport construction designs and materials and identifying climate resilient building construction designs and materials relevant to Kenya.

2.2 Main current barriers to mitigation and adaptation in Kenya

Kenya's Action Plan will set out an ambitious programme of activities and investments that, if delivered, can move Kenya on to a low-carbon, climate resilient trajectory. However, despite progress by Kenya in recent years, as reflected in the development of the National Climate Change Response Strategy, as well as Kenya's relative success in developing Clean Development Mechanism (CDM) projects¹, there remain a number of barriers which will need to be overcome if Kenya's ambitions are to be realised. Drawing on other aspects of the strategy for financing the KCCAP², some of these key barriers are listed below.

Regulation and policy

- Insufficient understanding and experience across government of the low-carbon investment arena, including mandatory and voluntary carbon markets, renewable energy and energy efficiency.
- Inadequate communication between government and private sector on regulatory and policy matters.
- Little engagement of the (international) private sector by the Government of Kenya (GoK) on its low-carbon development strategy, with the goal of attracting investment.
- Low levels of transparency in decision-making and the awarding of contracts by ministries, departments and agencies of the Government of Kenya.

Access to commercial finance

- Very high interest rates; real interest rates are about 6-7 per cent and nominal rates close to 20 per cent for tenors less than 5 years; no long term funds readily available.
- Lack of experience of banks and other financial institutions with the financing of low-carbon projects, that is, in renewable energy and energy efficiency sectors.
- Limited development and early stage capital for project developers, especially at the small and medium enterprise (SME) level. A lot of private equity investors currently seek projects in Kenya, but the terms are often prohibitive – exit within five years and 25-30 per cent return on equity for long term energy efficiency and renewable energy projects.
- Lack of experience in, and availability of, project finance.
- High collateral requirements on the part of banks which disproportionately affects projects in the new sustainable energy space.

Technical and financial capacity

- Low level of capacity amongst firms, especially SMEs, in developing a bankable business plan and/or feasibility study, encompassing low skill levels in finance, accounting, auditing, management, addressing regulation and negotiating with government, amongst others.
- Challenges relating to availability and access to information on low carbon investment by all stakeholders including banks.

Government and development partners

- The slow disbursement of public funds to most projects and programmes implemented by the private sector, including by bilateral and multilateral development agencies, ministries and trust funds.
- Multiple and poorly-aligned sources of development partner finance for low carbon investment activities and duplication of effort.
- Competing and complex development partner requirements for accessing funding.

It should be emphasised that the most important means of overcoming these barriers is through establishing a sound policy and regulatory framework. In the long term, getting the policies right is likely to be of crucial importance in delivering the investment flows, especially from the private sector, that Kenya requires to grow in a low-carbon, climate-resilient fashion. There is considerable literature examining both the overall properties that such policies need to have³, as well as studies on the relative effectiveness of different types of policies in different circumstances⁴. These have informed the recommendations made elsewhere in relation to the wider investment climate for climate investment.

At the same time, there are a variety of reasons why exclusive reliance on establishing a conducive business environment is unlikely to be sufficient to overcome all the barriers and drive the necessary investment for Kenya to implement its Action Plan. Other important issues include market failures in capital markets, the social/redistributive impacts of introducing incentive policies too quickly (that is, a large increase in renewable energy capacity caused by high feed-in tariffs could lead to steep electricity price rises) as well as the fact that the characteristics of an important component of climate change activities and programmes such as some adaptation activity and capacity building will always require concessional/grant finance. Consequently, there is a need to complement these policy initiatives with a focus on publicly resourced finance mechanisms and the appropriate institutional arrangements surrounding their delivery. The next chapter examines the advantages and disadvantages of a National Climate Fund versus other options as a means to deliver these resources.

3. Rationale for a National Climate Fund in Kenya

A National Climate Fund (NCF) can be defined as: “a mechanism that supports countries to direct finance toward climate change projects and programmes by facilitating the collection, blending, coordination of, and accounting for climate finance. NCFs provide a country-driven system that can support climate change goal setting and strategic programming, oversee climate change project approval and implementation, measure performance, offer policy assurance and financial control of climate change funds, and assist with partnership management”⁵.

The first question to address is whether there is a strong rationale for setting up a fund. This requires assessing the advantages and disadvantages of the fund with alternative approaches for managing and disbursing public sources of climate finance, especially from development partners. We identify two alternatives.

- Scaled-up use of the existing architecture where bilateral and multilateral agencies continue to provide finance for climate change programmes largely according to their own criteria. This can be considered as, broadly speaking, a continuation of the existing approach. Our review of these arrangements shows that there is a large number of such institutions – at least fifteen – currently supporting climate change mitigation and adaptation activities in Kenya through this architecture.
- Greater provision of financial resources for climate change activities to the Government of Kenya for it to disburse using its existing structures and mechanisms that is, budgetary support. Such a model could be considered consistent with the Paris Declaration and Accra Agenda for Action⁶ both of which stress the importance of development partners aligning with developing country strategies and using (existing) systems (the ‘systems alignment’ principle).

In choosing between the three alternatives (a fund, current approach or budgetary support), it should be stressed that they are generic models/paradigms to illustrate the key underlying differences between the different approaches. In reality all three are likely to co-exist within Kenya for the foreseeable future. Nonetheless, such an approach helps to define the key strengths and weaknesses of different approaches and where future effort might be concentrated, especially in the context of the expected scale-up of international climate finance resources towards the USD 100 billion target stated in the Cancun Agreements.

These alternative models can be assessed against a range of criteria. Ideally, the management and disbursement of climate finance within a country would allow for a wide range of **sources (1)** of climate finance to be tapped; and that efficient and transparent **processes (2)** would transfer these sources in an appropriate form to a range of **recipients (3)**, in a manner consistent with **national priorities (4)**. Each of these four key characteristics of a financing mechanism can be broken down further into a number of criteria.

Sources

- Will development partners be willing to provide resources to the financing mechanism?
- In addition to support from development partners (the primary form of support in all models), will the mechanism/approach to managing climate finance allow for complementary sources to be tapped, especially domestic finance?

- Does the funding approach insulate funding for climate change from national budget cycles so as to facilitate longer term planning?

Efficiency and transparency

- Are the transaction costs associated with managing and disbursing climate finance reasonable?
- Are decisions about climate finance flows and disbursements made in a timely fashion?
- Is there transparency about flows of finance and decision making?
- Is there sufficient capacity and expertise in managing and disbursing climate finance?

Recipients

- Can the mechanism engage with, and potentially resource, a wide range of beneficiaries, including, civil society organisations (CSOs) and the private sector, in addition to the public sector?
- Does the mechanism have the flexibility to provide a wide palette of different financial instruments?

National ownership and priorities

- Does the financial mechanism support and align with existing democratic processes within Kenya?
- Does the mechanism ensure that climate change funding decisions are aligned with national plans and the wider fiscal planning processes?

Table B1 below provides an indicative assessment of these three financing mechanisms against each of these criteria in Kenya. The scores are (necessarily) subjective but where possible draw on a range of evidence collected throughout the study.

They suggest that a National Climate Fund would have the following advantages.

- Relative to greater budgetary support, an NCF would have more clarity of purpose and allow the development of expertise and transparency. Creating a national climate fund creates a specially focused body with a clear mandate. This clear focus can ensure greater efficiency in decision making – currently for development partner disbursement through government systems a gap of between six and nine months is common between the preparation and submission of reports and funding requisitions and the actual receipts of the funds by implementing agents. It also allows for the development of a body with corporate expertise and detailed understanding of the specific challenges associated with that mandate. This expertise, in turn, can allow it to operate in ways that would be atypical for a line ministry, that is, providing a wide range of financing instruments and entering into contracts with a wider range of beneficiaries. In addition, by explicitly creating a separate body there is likely to be greater focus on the transparency of its decision making and associated financial flows, making it easier to demonstrate the additionality of climate finance, and insulating climate change funding decisions from short-term budgetary pressures.
- Relative to maintaining/augmenting the current approach, a National Climate Fund would offer greater opportunities for alignment with national priorities (the

‘ownership’ principle). This is in line with much of the existing literature on national funding entities (NFEs): the UN Development Programme (UNDP) notes, ‘national climate funds are consistent with several principles for the Paris Declaration on Aid Effectiveness and the Accra Agenda for Action’⁷ while Gomez-Echeverri⁸ states: *‘there is a gradual recognition that the current situation of financial support for climate change action in developing countries – characterised by a large number of international funds with complex administrative processes, minimal transparency or accountability, and conflicting mandates that do not always address or respond to developing country concerns or priorities – is untenable. Consequently, we see a gradual acceptance that more needs to be done in terms of shifting the responsibility for managing and disbursing the funds to developing countries...’* Further, by coordinating climate finance flows across a country, a national climate fund may also promote greater transparency and consistency in decision-making than is possible under the current approach.

- Finally NCFs may operate in a more streamlined cost-effective manner than existing bilateral and multilateral agencies. The underlying research undertaken for this study suggests that these arguments may be particularly salient in Kenya⁹. Although Kenya has been relatively successful at attracting international public support, this has come at the cost of fragmentation. There are at least fifteen different agencies supporting climate change activities and programmes in Kenya, each carrying their own administrative costs and with different rules and processes concerning both the extent, and means, of engagement with the Government of Kenya. There is little evidence of pooling of resources. Although the Joint Sector Working Group provides some harmonisation this is informal and not legally binding; it also focuses on a wide range of issues other than climate change.

There are two main challenges associated with the use of a National Climate Fund.

- Compared to the current approach, funds may operate under different rules and procedures to those to which development partners are accustomed and/or may not have an established track record of efficient disbursement. This can make it difficult for development partners to move away from established approaches and commit resources to an NCF and may create challenges for an NCF that could be asked to provide different information to different development partners.
- Compared to budgetary support, creating a separate modality for financing climate change investments prevents the ‘mainstreaming’ of climate change within departments and line ministries. Climate change continues to be treated as an exceptional issue (with exceptional approaches to acquire funding, and so on).

These challenges are discussed in more detail in some of the underlying research annexed to this report.¹⁰ Although neither of these challenges is insurmountable, they do point to the importance of a strong design that seeks to minimise or overcome these potential disadvantages. This is discussed in the context of the draft Governing Instrument where we include a number of design aspects that seek to link the fund with existing government ministries, strategies, personnel and procedures and, for example, in terms of the approach taken to safeguards, and so on.

Table B1 A comparison of National Climate Funds with other modalities for disbursing climate finance

	Question/criterion	Existing approach	Budgetary support	National Climate Fund
Sources	Will development partners be willing to provide resources through this mechanism?	✓✓✓ - tried and tested. Kenya already receiving substantial climate change finance from development partners in the order of \$2-3 billion.	✓✓- some evidence of development partners providing general budget support to the government but also concerns over fiscal management and transparency e.g., Kenya is in bottom quintile in the World Bank's Governance indicator for control of corruption.	✓✓ - some evidence of development partners supporting similar funds in Kenya i.e. CDTF, but possible reticence over new (pooled) vehicle and corruption. However, new fund provides opportunity for best-practice processes.
	Can complementary sources be tapped (especially domestic sources)?	✓ - more reliant on existing development partner sources (cf. UNDP, 2011)	✓✓✓ - easy to collect and use domestic public resources; other sources may be more difficult	✓✓ - may be difficult to provide additional domestic budgetary support (especially if fund requires multi-year commitment)
	Is resourcing of climate change projects insulated from the budget cycle?	✓✓- main vulnerability is from budget cycle of development partners. Some programmes/funds demand multi-year commitments i.e. CIFs.	✓- no; considerable vulnerability	✓✓✓ - yes, conditional on receiving resources
Efficiency and transparency	Are the transactions costs associated with managing and disbursing climate finance low?	✓✓- no need to set up any new systems but processes can be complicated	✓✓✓ yes, can make use of existing disbursement mechanisms	✓✓- some costs associated with setting up the fund but thereafter processes can be designed to be streamlined and reasonably low cost
	Are decisions about climate finance flows made in a timely fashion?	✓ - development partner processes are typically lengthy	✓✓ - disbursement decisions and processes may take around 60 to 90 days	✓✓✓ - a potential strong advantage of a climate fund in Kenya. Disbursing resources through a strong, competent fund may be significantly quicker than through the standard budgetary routes.
	Is there transparency about flows of finance and decision making?	✓✓- lots of documentation but plethora of initiatives from different actors can make it difficult to monitor activity	✓- concerns over corruption (see above)	✓✓ depends on design and implementation but higher levels of visibility will attract attention
	Is the level of capacity and expertise in managing and disbursing climate finance sufficiently high?	✓✓ - individual initiatives likely to have capacity but plethora of initiatives can mean opportunities for learning are restricted	✓ - expertise will be focussed on broader government financing and disbursement activities; specialised focus on climate finance, and associated instruments, may be lacking	✓✓ team can be specifically selected for the objectives of the fund; some initial capacity building may be required
Recipients	Can the mechanism engage with a wide range of stakeholders?	✓✓ - yes, in principle; practice may vary	✓- focus is on providing resources to line ministries and parastatals. Institutions and frameworks to support CSOs and private sector less well established	✓✓ yes in principle; depends on implementation

	Does the mechanism have the flexibility to provide a wide range of financing instruments?	✓✓✓ - yes	✓ - no, existing focus and expertise is on providing grants/budgetary support to line ministries and parastatals	✓✓- yes in principle; some capacity-building may be required
Country ownership	Does the financial mechanism support and align with existing democratic processes within Kenya?	✓- in many cases, no; funding decisions taken outside of the government process	✓✓✓- yes, resources flow according to the priorities established by the government; resources for climate change treated identically to other funding priorities	✓✓ - funding decisions can be aligned with national priorities; if fund is at arms-length from government may be subject to less democratic accountability
		✓ - in many cases, no; funding decisions taken with only partial reference to GoK objectives or priorities	✓✓✓ - yes, resources flow according to the priorities established by the government; resources for climate change treated identically to other funding priorities	✓✓ -in part as decisions are made within the country but some challenges as separate funding mechanism to bulk of investments and programmes

Note: ✓ - scores poorly against question/criterion; ✓✓ - scores moderately well against question/criterion; ✓✓✓ - scores well against question/criterion

4. Summary of proposal

The proposed National Climate Fund of Kenya could have the following main features.

- The Fund's scope would include both mitigation (on account of the expected high growth of the Kenyan economy and the need to avoid locking in a carbon-intensive energy generation and other emissions intensive infrastructure) and adaptation (in light of Kenya's manifold potential vulnerabilities to adverse climate change).
- The Fund would aim to become the main (although not necessarily exclusive) recipient of external multilateral and bilateral climate finance mobilised by Kenya, and contribute to significantly scaling up these climate finance flows.
- The Fund would be structured as a separate legal entity for reasons of governance and effectiveness. The recommended form is that of a Trust Fund, that might be rapidly established by ministerial decision.
- The Fund would develop in a phased approach, providing relatively simple financial instruments, most obviously grants, in an initial phase, before evolving to provide a wider palette of financing instruments. The early phase of this evolution would be consistent with the practice among many existing national funding entities e.g. Bangladesh, Indonesia and would allow time for the institution to build capacity; the latter phase would recognise that the challenge and complexity of Kenya's required response to climate change will require a broader array of financial instruments. This latter phase could be associated with the Fund having the capacity to borrow. The government could ultimately decide, in view of its skills, performance and track record achieved over a wide cross-section of the Kenyan economy, to convert the Fund into a national development bank.
- Building on the experience of multilateral development banks, the Fund would aim to be a catalyst of private sector funding and to the extent possible to provide wholesale finance, that is, by using third parties, including commercial banks and existing funds within the country, for example the National Environment Trust Fund, to channel finance to projects more diligently and efficiently.
- The Fund's governance would allow broad (and equal) representation of the four main stakeholder constituencies (government including counties, civil society organisations, private sector, and development partners supporting the Fund).
- The Fund would initially have recourse to an external, competitively selected, Fund Administrator to run its day-to-day operations. But the objective is to quickly build domestic capacity to make possible a full transfer of Fund management services to the government, should it be desired.
- The Fund would follow best international practices and standards as appropriate in the Kenyan context and given the likely small size of many of its future projects.

5. Draft Governing Instrument of the Kenyan Climate Change Fund

This chapter sets out the main elements of the governing instrument of the proposed National Climate Fund, which may serve as the basis for its legal creation.

5.1 Purpose, Functions and Guiding principles of the Fund

5.1.1 Purpose

The Fund would financially support the implementation of climate mitigation and adaptation actions prioritised in the Kenya Climate Change Action Plan (KCCAP) (as regularly updated), which require public support to be viable, and which the Fund would be best positioned and equipped to support. The Fund would assist Kenya in furthering its ambition to become a leader in the fight against climate change on the continent.

5.1.2 Functions

The Fund would have three main functions.

- i. The Fund would be responsible for the overall coordination of climate-related financing issues in Kenya, including, but not limited to the collection and publication, of relevant financial data in accordance with best practice¹¹. As regards the proposed new international Green Climate Fund (GCF), the Fund would become the “national designated authority” (referred to in point 46 of the GCF governing instrument approved by the Conference of the Parties (COP) 17 in Durban in December 2011), recommending funding proposals to the GCF Board and being consulted on all funding proposals originating from the country.
- ii. The Fund would be the vehicle (recipient) of choice for external multilateral and bilateral climate finance (including, possibly private finance). This is an objective consistent with the ‘country ownership’ principle of the Paris Declaration. However, development partners will not convert to this new approach immediately. Some development partner programmes are already being implemented; development partners may need some convincing to switch to a new approach which means less ‘development partner ownership’, the risk of losing influence and control, and potential concerns over the approaches to the allocation and spending of funds that may differ from their own. These will be addressed through features of the design of the Fund, particularly various ‘safeguards’ (see below.)

The two main exceptions to the Fund being the recipient of all external public climate finance flows would be: (i) development finance institution (DFI) project financing (for example, the direct financing of investment projects); and (ii) bilateral or multilateral development partner funding that is required to transit via accredited ‘implementing entities’ (were the Fund not willing or able to become one¹²): Three

prominent examples are the Adaptation Fund (AF) which accepts national ‘implementing entities’ (NIEs¹³); the Global Environment Facility (GEF) and the Pilot Program on Climate Resilience (PPCR) which to date do not use NIEs¹⁴. Greater discussion on such national implementing entities, and their similarities and differences, with national climate funds are covered in the underlying research accompanying this paper¹⁵.

The Fund would also aim to become a ‘funding entity’ of the GCF (as referred to in point 47 of the above GCF document), should this modality of access to the GCF emerge.

- iii. The Fund would have overall responsibility for capacity building in relation to mobilising and spending climate finance in Kenya.

As such, the Fund would map capacity building needs in-country in relation to finance, draw up an action plan or road plan, and finance actions.

5.1.3 Guiding principles¹⁶

The Fund’s operations would be guided by the following principles which would be set out in a Fund Charter and if the need arises clarified and elaborated upon in internal policy documents.

- **Coherence with the national policy framework and KCCAP:** the Fund would finance or support projects and programmes which are included or consistent with the KCCAP (as periodically updated) and otherwise comply with Kenya’s policies.
- **Additionality:** the Fund would not provide financing or financial support when the applicant is able to obtain sufficient financing or facilities elsewhere on terms and conditions that the Fund considers reasonable; the Fund would aim to be catalyst to other parties’ funding, in particular the private sector.
- **Equity:** the Fund would seek to ensure that the needs of those most vulnerable to climate change in Kenya, i.e women, children and the elderly, are addressed in the projects and programmes it supports.
- **Efficiency and effectiveness:** the Fund would seek to operate cost-effectively and support projects and programmes that are viable and professionally managed and whose results and performance can be monitored.
- **Risk management:** the Fund would carefully consider the risks of the projects and programmes it supports, and use diversification and other risk management instruments adequate to the type of exposure it takes.
- **Market distortions:** the Fund would seek to avoid distorting competition and/or trade in making its funding decisions.
- **Transparency and openness:** the Fund would publish its decisions, and report at least annually on its operations in its annual report. Key stakeholders would be involved in decision-making and supervision of the Fund’s management and operations via representation on its Governing Board, and governance arrangements would be free from political interference.

- Flexibility: the Fund would adapt its approach, instruments and internal organisation to changes in the global and national environment in which it operates (in terms of needs; regulatory framework; new carbon finance and climate finance mechanisms and rules, amongst others).

5.2 Resources and fund raising process

5.2.1 Potential sources of funds

The Fund would mobilise its resources from the following main sources

International

- public bilateral grants;
- public multilateral grants, such as (possibly) from the Green Climate Fund; and
- private grants (most notably from philanthropists as commercial sources are not considered to be a realistic potential resource for the Fund, as the Fund will likely accept returns and take risks that commercial capital providers will not).

The first two are expected to provide the bulk of the Fund's resources To date most other national climate funds have received the bulk of their international resources from public bilateral grants.

Domestic

- Budgetary resources, such as could originate from environmental fines and taxes, for example, a carbon tax and petrol tax (e.g. Thailand's Energy Conservation Promotion Fund).
- Private contributions (from individuals, charities, NGOs or corporations).

It is not envisaged at this stage that the Fund would borrow. The main reason is that the Fund will not at least initially give loans, and this is predicated on the assumption that the Kenyan banking system has liquidity and is broadly competitive and qualified enough to fulfil its role in implementing the KCCAP, with targeted support from the Fund. This is discussed in more detail in the accompanying paper on Kenya's investment climate for climate investment¹⁷. Another reason is that the Fund would not be able to borrow without a guarantee of the state and would borrow on no better terms than the state, which would not enable it to offer sufficiently concessional terms to target beneficiaries.

5.2.2 Fund mobilisation

In terms of process, the Fund should aim for the highest possible level of predictability of its resources, particularly for programmes that need to be implemented over the medium to long term, and to be regarded as a reliable partner by potential applicants.

The Fund should operate based on three-year cycles, allowing it to plan its operations and calibrate its financing, as well as human and other resources, accordingly.

This budgeting process (every three-year) could be institutionalised by holding a ‘fund-raising’ conference in Kenya prior to the beginning of each cycle. This would allow the Fund management to present its Action Plan (and initial list of priority spending items, both updated as the need may arise) and report on past activity of the Fund. This would contribute to greater visibility and transparency of the Fund operations.

5.2.3 Thematic windows

The Fund would create different financing ‘windows’ allowing development partners to earmark their funding, if they so wish (the Kenyan Water Sources Trust Fund offers a precedent).

5.3 The Fund’s approach to financing

5.3.1 Scope

The Fund would target both mitigation and adaptation. It would set rules to keep a balance between the two, for example: aggregate disbursements made under each window will not represent less than [40] per cent of the Fund’s total disbursements in any period of three years.

5.3.2 Beneficiaries and implementing entities:

The Fund would support projects or programme undertaken by the public sector (central and local government, and other public sector agencies), private sector, and civil society organisations (CSOs). The existing international experience of national climate funds tends to involve these bodies focussing on supporting public sector implementing entities and CSOs, e.g. the Indonesia Climate Change Trust Fund and the Bangladesh Climate Change Resilient Fund. However, other national climate funds have included support for the private sector, e.g. the Ecuador Yasuni Ishpingo-Tambococha-Tiputini Fund and Brazil National Fund on Climate Change, and others intend to do so in the future (e.g. the Indonesia Climate Change Trust Fund). In Kenya’s case, the broad range of implementing entities is justified by the wide range of activities that the Fund will support.

Detailed eligibility criteria would be laid out in the Fund’s Operations Manual, but would include, as a minimum, demonstrated need for Fund support, integrity and capacity to undertake the project or programme, amongst others.

5.3.3 Eligible expenditure

The Fund would support both specific projects and programmatic approaches. Detailed eligibility criteria would be laid out in the Fund's Operations Manual. The following types of expenditure would be eligible for Fund support:

- i. capital expenditure;
- ii. operating costs, where revenue streams are insufficient (for example, in the case of public good adaptation), including a possible reduction in interest payments charged on commercial loans;
- iii. preparatory activities (the likes of feasibility studies and energy audits); and
- iv. capacity building.

The Fund may wish to create a list of ineligible expenditures as part of its Operations Manual, as exists for example for the Pilot Program for Climate Resilience (PPCR), one of the suite of the World Bank-managed Climate Investment Funds¹⁸.

5.3.4 Financing modalities

Mitigation window: the Fund would not normally fund the entire project or activity cost (except for capacity building), but would co-finance projects roughly in proportion to the additional costs and risks associated with mitigation projects (that is, incremental costs; shortfall to normal returns¹⁹).

- *Example 1:* Geothermal project. The high capital costs and first-of-its-kind character of the project in a Kenya context may justify a capital investment grant to enhance project returns and bring them in line with investors' expectations. Additionally, banks may require a partial loan guarantee given the risks of the project.
- *Example 2:* Energy efficiency-retrofit project in industry. Fund support may be required to buy down the costs of the initial energy audit, a modest expenditure but one that sponsors may not be willing to consider given the barriers to information and lack of experience with similar projects in Kenya.
- *Example 3:* Off-grid solar PV systems, enhanced cook-stoves or bio-digesters. In non-electrified, primarily rural areas a range of proven technical solutions can simultaneously solve the issue of access to energy and reduce greenhouse gas emissions. However, because they are diffuse in nature they are difficult to finance with conventional carbon finance. Programmes of Activities (PoAs) under the Clean Development Mechanism were meant to remedy this problem, but new PoAs will be increasingly difficult to establish in Kenya given that credits from projects and PoAs registered after 2012 will not be eligible in the EU Emission Trading Scheme. The Fund could support these programmes at least pending the emergence of a successor to PoAs.

Adaptation window: The Fund would co-finance projects that reduce vulnerability to both current and future climate events (win-win adaptation) and the additional costs of integrating climate risk and resilience in long-term development activities, for example as they adversely affect the viability of investments²⁰.

- *Example 1:* In Tanzania, the Adaptation Fund (AF)²¹ is financing an integrated blend of ‘hard’ and ‘soft’ coastal protection measures in the Ilala and Temeke Districts (Dar Es Salaam region) with a \$5-million grant. The project approach is built on the idea that a sea wall alone is less effective than a sea wall supported by a restored shoreline (directly behind it), and a rehabilitated coral reef barrier (in front of it). Rehabilitated mangroves will provide a direct protective service to part of the city of Dar es Salaam, which is currently not adequately protected, and relieve some of the pressure from downward currents on the sea wall portion. Both types of interventions —hard and soft – will be further supported by a set of policy and learning process that will create the enabling environment for policy changes and the ground for project sustainability and coordination with on-going initiatives in the country²².
- *Example 2:* In Uruguay, the AF is financing with a \$10-million grant a project aimed at reducing vulnerability and building resilience to climate change and variability in small farms engaged in livestock production located in some extremely drought-sensitive regions of the country. This will involve investments in water supply, best practices for native grasslands management, shadow trees and animal management improvements and agro-forestry, as well as capacity building and other ‘soft’ measures²³.

Several types of financing instruments, on their own or in combination, can achieve these outcomes; they are described below.

5.3.5 Direct and indirect financing

The Fund would provide direct funding for larger projects and programmes, for example, a wind farm, or a large industrial energy efficiency retrofit, and other similar activities.

The Fund may also provide funding indirectly, via intermediaries, if this enables it to better reach out to projects and beneficiaries and enhance its impact. For example, the Fund could extend ‘wholesale’ funding to three types of intermediaries, and for the following purposes:

- Commercial banks:* to extend dedicated low-carbon loans²⁴, with a grant element as necessary, for example, through interest rate reductions (as exist in Lebanon), or investment grants paid on project completion, as are provided in several central and eastern European countries in parallel with European Bank for Reconstruction and Development (EBRD) or European Investment Bank (EIB) dedicated low-carbon credit lines.
- Venture capital (VC) funds* to support Kenyan developers of low-carbon or clean technology projects, including energy service companies (ESCOs) and renewable energy developers, with seed, and other forms of early stage capital and expansion capital if warranted²⁵.
- Other public sector funds and entities, or NGOs*, particularly to reach out to smaller projects, including at community and/or county level. The Community Development Trust Fund (CDTF), Water Services Trust Fund (WSTF) and the National Drought Contingency Fund (NDCF), for example, could request support from the Fund to finance specific adaptation costs in their respective fields of activity.

5.3.6 Financing instruments

Although initially focused on grants, the Fund may over time deploy a wider palette of financing instruments in order to address the various barriers to low-carbon investments prevailing in Kenya- see Table B2 and B3 below.

Table B2 Fund’s potential palette of financing instruments

Types of financing instruments	Definition	Application
<i>Short-term</i>		
Investment grants	Non-reimbursable grant for capital expenditure projects	Mitigation / adaptation
Operating grants	Recurring grant for non-investment spending	Adaptation mostly Preparatory activities Capacity building
<i>Longer-term</i>		
Partial credit guarantees	Guarantee that the loan principal and interest will be (re)paid	Mitigation / adaptation
‘Patient capital’	Equity with lower return expectations, longer exit, and junior to commercial investors’ equity	Mitigation mostly
‘Mezzanine’ debt	Type of debt that is subordinated to senior debt, and may have features of equity, e.g. convertible debt	Mitigation mostly
Contingent grants	Reimbursable grant, but reimbursement can be foregone if project fails	Mitigation / adaptation
Concessional loans	Loans on terms & conditions more favourable than those offered in the market	Mitigation / adaptation

Table B3 below provides an overview of how various barriers can be addressed by these mechanisms as well as examples of schemes or institutions that have implemented them.

Table B3 How selected financing mechanism address barriers to low-carbon investments

Issue	Fund instruments	Examples / precedents
Lack of development/early stage capital	Equity, contingent grants via grants to dedicated funds	UNEP/GEF Seed Capital Assistance Facility (SCAF) AfDB's Sustainable Energy Fund for Africa (SEFA)
Lack of equity for project developers	Mezzanine or equity via 'patient capital' investments in dedicated funds	Global Energy Efficiency and Renewable Energy Fund (GEEREF), Investment Fund for Environment and Renewable Energy (FIDEME)
Capacity building for banks and projects proponents	Technical assistance grant Project preparation Facility	Agence Française de Développement (e.g. RTAP programme in Kenya), EBRD, EIB, amongst others.
High risk perception by banks	Loan guarantees	International Finance Corporation, World Bank
Short loan tenors	Refinancing guarantee	Uganda Energy Credit Capitalisation Company (UECCC)
High interest rates	Interest rate subsidies	UK Carbon Trust
Low returns/long paybacks	Investment grants Concessional loans	EBRD in Eastern Europe, Tunisia, etc. AFD in Kenya, Uganda, Tanzania
High transaction costs of small transactions	Project preparation Facility Grants for energy audits/feasibility study Performance fees to banks	AFD Kenya (RTAP) EBRD in Eastern Europe
Lack of awareness	Campaigns, subsidised energy audits	Canada, New Zealand, Tunisia

Straight investment and/or operating grants would be the predominant instrument in the initial phase of the Fund's operations as grants are the most suitable instrument for early-stage adaptation (which, as discussed in the introductory section, section A, is currently relatively neglected by the international climate finance architecture), support for preparatory activities and capacity building. It would also allow the Fund to focus on the provision of a simple and well-understood instrument while building up capacity and expertise in terms of personnel, procedures, and so on.

Over time, as Fund capacity develops, investment barriers and the Fund's additionality can be better gauged, a track record is established, and financial resources have become more substantial, the Fund may decide to utilise more sophisticated instruments, such as equity, mezzanine debt, and guarantees. 'Patient capital' could be useful to leverage private investors in clean energy private equity funds. Loan guarantees could be instrumental in allaying the risk averseness of commercial banks to low-carbon investments. Interest rate subsidies and refinancing guarantees would reduce loan interest rates and extend bank loan tenors respectively, remedying two key barriers in the Kenyan context. For the latter instruments, careful monitoring will be required in order to ensure that it is the ultimate project developers who benefit from the concessional terms provided.

For reasons already mentioned, the Fund would, at least initially, not extend loans. The Kenyan banking sector is relatively liquid and competitive. The Fund's distinct role is to unlock and catalyse private capital addressing barriers with adequate instruments. Only if the Kenyan banking sector failed to play its role and respond to public incentives and support as provided by the Fund should the Fund consider directly providing loans. Another pre-requisite would be that the Fund's resources are sufficiently large and/or it has the ability to borrow on the desired scale and terms.

As in other climate-related funds, the Fund would justify that its support is indeed necessary, and (in a later stage when its offering of financing instruments has expanded) the level of concessionality²⁶ attached to it²⁷.

5.3.7 Project cycle

An indicative project cycle may consist of the following steps, inspired from the process used in multilateral development banks (simplified²⁸).

1. *Submission of a project concept note (PCN) by the project or programme proponent under the relevant window*

The Fund would develop a template for this PCN as well as a web-based interface, although paper-based applications will also be eligible.

2. *Screening by the Fund against eligibility criteria*
3. *Preparation and submission of project proposal document (PPD)*

Successful, applicants would prepare project proposals, possibly with support from the Fund to elaborate or improve the proposal as needed. The Fund would develop a template for this PPD.

For project and programmes of a certain size and/or complexity, a feasibility study would be required.

4. Project appraisal

The Fund would conduct a full appraisal of the project or programme in accordance with the following main criteria (to be fully elaborated in the Operations Manual):

- integrity of project or programme proponent;
- capacity of the project or programme proponent to implement the project or programme (as regards the likes of finance and human resources for example);
- financing plan;
- economic benefits;
- financial viability;
- climate-related impacts (that is, contribution to objectives of the KCCAP), and
- need for Fund support (that is, additionality of the Fund relative to other available sources of finance in the country).

5. Project approval

Following appraisal the Fund (and specifically the Operations Committee – see chapter 6 below) would decide whether to provide financial support to the project or programme, in which form (instrument), for what amount and on what terms (which may be indicative so as to allow some room for negotiation).

6. Signing of a financing agreement and implementation

Following project approval, the Fund will enter into negotiation with the project or programme to agree on the final terms of the financing. This process will culminate in the signing of a financing agreement, of which the Fund will develop templates (one for each key financing instrument as appropriate).

5.4 Governance

The three main bodies administering the Fund would be the Governing Board and under its authority the Operations Committee, and the Fund Administrator.

The rationale for this tripartite structure in ad hoc single-mandate institutions is as follows: the Governing Board where key stakeholders are represented is the body that provides overall guidance and has broad oversight over the Fund's operations; the Operations Committee makes funding and operational decisions; and the Fund Administrator provides the expertise and personnel necessary to run the Fund on a day-to-day basis.

A similar, three-tier, structure can be found, with nuances, in most existing national climate funds (e.g. Bangladesh and Indonesia), while multilateral climate funds (e.g. the AF and GCF) tend to use of two-tier structure (Board and Secretariat). The addition of an Operations Committee, to a large extent a sub-committee of the Board, is inspired from Multilateral Development Banks (although MDBs' board members normally do not sit in the Credit or Operations Committee) and aims to streamline and expedite the decision-making process, having in mind in the Kenyan context the likely high number of small projects. Numbers of members for each body are indicative.

5.4.1 The Governing Board

Composition

The Governing Board (the Board) would have [16] members (each with an alternate member) composed of an equal number of members from four constituencies: Government (central and counties); development partners; private sector; CSOs.

Selection of Board members

The [four] members (and alternate members) representing the Government would be appointed by the Ministers of Environment and Mineral Resources (MEMR) and of Finance²⁹, and by the counties³⁰, for the latter through a formal vote on the basis of a procedure agreed upon by at least a majority of the counties³¹.

The [four] members (and alternate members) representing the development partners would be appointed by development partners by the members of the development partner Climate Change Coordination Group through a formal vote.

The [four] members (and alternate members) representing the private sector would be appointed within the Kenya Private Sector Alliance ([two] members), the Kenyan Association of Manufacturers ([one] member) and the Kenya Banks Association ([one] member) through a formal vote, on the basis of a procedure agreed upon by these organisations.

The [four] members (and alternate members) representing the CSOs would be appointed jointly through a formal vote, on the basis of a procedure agreed upon among themselves by sector-relevant CSOs.

The Board would meet at least once every quarter, or at the request of at least half of its members.

Term of membership

Members and alternate members will serve for a term of [three] years, which can be renewed in accordance with the procedures adopted by their constituency.

Chairmanship

The Chair of the Board will be elected by the Board among its members representing the Ministry of Finance³². This is in line with other national climate funds, where senior government officials play a key role in the fund governance process. He/she will serve for a period of one year, which can be renewed.

Decision-making

Decisions will be normally made by consensus, save in circumstances set out in the Rules of procedure, which the Board may decide to adopt after its installation.

Role and functions

The Board would have overall responsibility for policy formulation and the good operation of the Fund in accordance with its constituting documents (for example, the Charter). In particular, the Board would:

- i. approve a mid-term (three-year) funding and expenditure strategy, in line with KCCAP (as periodically updated);
- ii. approve an annual budget and work programme;
- iii. approve operational modalities, including eligibility criteria for access to Fund support;
- iv. approve specific operational policies and guidelines;
- v. select, appoint and enter into legal arrangements with the Fund Administrator (see below);
- vi. confirm the appointment of the Executive Director of the Fund Administrator;
- vii. oversee the operation of the Fund;
- viii. commission independent evaluations of the Fund's operations; and
- ix. exercise such other functions as may be appropriate to fulfil the purpose of the Fund.

5.4.2 The Operations Committee

Composition

The Operations Committee (the Committee) will have [seven] members, [four] of whom will be elected by the Board among its members for a [two] year term, and the other [three] will be senior officers of the Fund Administrator (see below), including one of the latter's senior mitigation or adaptation experts as the case may be, depending on the window under which funding will be approved.

The Committee will be chaired by a member of the Board, elected by the Board for that purpose on the basis of his/her credentials.

The Committee will meet at least once a month depending on the agenda prepared by the Fund Administrator. Decisions will normally be taken unanimously by its members, and the quorum will be deemed constituted if at least [five] members are present.

Role and functions

The primary role of the Committee will be to take funding decisions (for example, on project approval), and prepare the annual budget of the Fund. The Committee will also run the selection process for the engagement of, and negotiate with, a firm or consortium of funds, which will provide Fund Administration services (see below.)

5.4.3 The Fund Administrator

In its initial configuration, the Fund would be staffed by an external Fund Administrator, brought from outside the Kenyan government, as a single coherent team possessing all the requisite skills to run an operation as proposed, including playing the role of secretariat and trustee to the Fund. In the future, as the Fund grows and becomes more institutionalised, it may hire its own staff. This arrangement is the most frequent one for existing NCFs. For example, in Bangladesh (in the Bangladesh Climate Change Resilience Fund) and Indonesia (in the Indonesia Climate Change Trust Fund), the World Bank and UNDP provide secretariat and trustee services on an interim basis. However, as explained below, in contrast to these arrangements, we propose that the Fund Administrator would be determined through an open competitive process, fully open to Kenyan citizens.

Role and functions

The Fund Administrator would:

- i. verify that eligibility criteria are being complied with;
- ii. independently assess the technical, economic, financial, institutional, environmental and social viability of each investment or programme application, and submit appraisal reports to the Committee for approval;
- iii. monitor operations and risks;
- iv. report on the Fund's activities and performance;
- v. organize and execute all administrative duties;
- vi. support the Board in arranging the Fund replenishment process;
- vii. manage the Fund's liquid assets;
- viii. prepare the Fund annual accounts; and
- ix. perform any other functions assigned to it by the Board.

The Fund Administrator would not be involved in taking funding decisions: that would remain the responsibility of the Operations Committee, acting under the guidance of the Governing Board, as established above.

Staffing

In an initial phase of two to three years, the Fund may engage, through an international competitive process, a core team of professionals (the Fund Administrator), which would be supplemented by staff seconded by the Government of Kenya in order to build domestic capacity and skills. Terms of Reference for the Fund Administrator will be prepared by the Committee and approved by the Board. It should be a requirement in the tender that the winning bidder include in its offer a significant proportion of Kenyan nationals of high calibre, and that, furthermore, it undertakes to train staff for, and beyond, the Fund Administrator's own needs. In addition, bids exclusively from Kenyan organisations are, of course, not excluded.

The Fund Administrator team will include experienced experts possessing the following skills:

- project management;
- mitigation project expertise (for example, in renewable energy, energy efficiency and land use and forestry);
- adaptation expertise;
- financial and risk analysis;
- finance and accounting; and
- training, knowledge management and capacity building.

The Fund Administrator would be headed by an Executive Director, whose appointment would be confirmed by the Board. The Fund Administrator would be resident in Kenya.

5.5 Legal status and location

5.5.1 Legal status

The Fund would possess juridical personality. It would be established by ministerial decision as a Trust Fund. Precedents include the Youth Enterprise Development Fund (YEDF), the Kenya Slum Upgrading Low Cost Housing and Infrastructure Fund (KENSUF), and the Community Development Trust Fund (CDTF), which is also a multi-donor fund.

This legal form presents a number of advantages:

- it can be set up quickly, through ministerial decision;
- it is very flexible in terms of rules of governance, procedures, and such like;
- it remains within the public sector;
- it could extend loans should it decide to do so in the future.

As a legal entity in its own right, the Kenyan NCF would have its own budget and accounts, and the legal capacity to enter into contracts, lend and invest funds.

5.5.2 Location and representation in the counties

The Fund will have its headquarters in Nairobi. It is recommended that it create initially up to three offices in the counties, in [to be determined]. Funding decisions will not be taken in these cities but staff of the Fund Administrator in these offices will (i) contribute to creating awareness about the Fund and the type of projects the Fund can support, (ii) assist smaller project proponents in preparing projects and filling in funding applications, and (iii) assist with conducting 'due diligence' on projects and programmes, for which a funding application has been submitted.

5.5.3 Future development of the NCF

At a later stage, when the Fund has built a strong portfolio, developed skills in several areas, established a track record of efficiency, effectiveness, and overall credibility, and if the need has arisen that the Fund add loans to its financing armoury, the government might consider transforming the Fund into a national development bank as exist in many countries. This would be a financing institution supporting Kenya's green growth and broader development objectives across a range of sectors of the economy with a palette of approaches and instruments that are not available from the market at the country's particular stage of development.

5.6 Safeguards

The Fund would follow best international practices and standards in all areas relevant to its mandate, having also consideration for cost-efficiency, and the relatively small size (relative to what multilateral development banks or a global climate fund will typically finance) of many projects. In developing these policies and guidelines, the Fund will also take account of the existing Government of Kenya practices and procedures.

One of the first tasks of the Board would be to develop and adopt policies and guidelines, covering the following issues:

- integrity (that is, corruption and money-laundering, among others)³³ ;
- environmental and social standards, including but not limited to gender equality;
- financial management, auditing and financial controls;
- procurement;
- risk management policy (including exposure limits);
- information disclosure policy;
- complaints and redress mechanism; and
- whistle-blowing mechanisms.

5.7 Monitoring, reporting and verification

Monitoring, Reporting and Verification (MRV) is essential to the effective tracking of progress in meeting national commitments and achieving the overall goals of the UN Framework Convention on Climate Change.

Most applications of MRV first outline the various potential elements and requirements of an 'ideal' MRV process then use this as a basis for examining the approaches that can be taken given available resources and constraints.

What needs to be measured, reported and verified depends to a large degree on the precise nature and objectives of the Fund's activities as well as the intended uses for the information. Much of it comes down to monitoring, metering, sampling, data management, benchmarking between sites, sectors, companies or projects to identify indicators and outliers, quality assurance systems and quality checks. It has applications for eligibility criteria and assessments, compliance, allocation methodologies and is implemented through standards and provision of guidance.

Two examples of the Fund MRV activities are provided thereafter.

1. The Fund would collect data and regularly report, in its annual report and on its website, to stakeholders on its *operations and financial position*, including but not limited to the following:
 - the projects and programmes supported, including their names, names of beneficiaries, sector to which they belong, location, and expected project or programme impact;
 - all (non-commercially sensitive) information that informed its project appraisal process so that it can show how the funded project met the objectives of the Fund. Funding decisions by the Operations Committee will be published; this will contribute to strengthening the independence of the Fund's decision-making.
 - the amount of funding mobilised by the Fund by contributor, window, and such like.
 - the amounts of financing committed and disbursed by the Fund in total (that is, the whole portfolio), and from each period.
 - performance indicators (for example, primary energy saved; renewable energy capacity added; greenhouse gas emissions saved).
 - financial status.
2. The Fund would also contribute, in relation to projects and programmes that it finances and in conjunction with the Fund's beneficiaries, to fulfilling *Kenya's reporting obligations to the United Nations Framework Convention on Climate Change (UNFCCC)*, in particular those arising from the COP 17 in Durban in late 2011.

In its decision N°2, COP 17 decided that "non-Annex I Parties shall submit a biennial update report every two years, either as a summary of parts of their national communication in the year in which a national communication is submitted or as a stand-alone update report". It also adopted Guidelines for these reports according to which, non-Annex I Parties such as Kenya shall in particular provide:

- information, in a tabular format, on actions to mitigate climate change, including for each mitigation action or groups of mitigation actions:

(a) name and description of the mitigation action, including information on the nature of the action, coverage (that is, sectors and gases), quantitative goals and progress indicators;

(b) information on methodologies and assumptions;

(c) objectives of the action and steps taken or envisaged to achieve that action;

(d) information on the progress of implementation of the mitigation actions and the underlying steps taken or envisaged, and the results achieved, such as estimated outcomes (metrics depending on type of action) and estimated emissions reductions, to the extent possible; and

(e) information on international market mechanisms;

- information on the description of domestic measurement, reporting and verification arrangement;
- information on constraints and gaps, and related financial, technical and capacity-building needs; and
- information on financial resources, technology transfer, capacity-building and technical support received from the GEF, Annex II Parties and other developed country Parties, the Green Climate Fund and multilateral institutions for activities relating to climate change, including for the preparation of the current biennial update report.

As to Fund beneficiaries, they will be held to reporting obligations to the Fund (on such aspects as the execution of the project and climate-related impacts, among others). The Fund will develop reporting templates adapted as appropriate to each type of project and/or category of beneficiaries.

6. Next steps

To launch the Fund without delay the following steps, some of which may run in parallel, are recommended (with implementing agents in brackets).

- agree on the design of the Fund based on the detailed analysis accompanying this Action Plan document (GoK and stakeholders);
- appoint a multi-departmental Task Force within GoK to steer the process of establishing the National Climate Fund of Kenya (GoK);
- convene a climate finance pledging conference (Task Force);³⁴
- create a Trust Fund via legal decree (GoK);
- communicate and consult nation-wide about the Fund, its mandate, and target date for operational start (Task Force);
- appoint the Governing Board (Task Force and stakeholders);
- draft terms of reference for the Fund Administrator (Governing Board with temporary assistance from Task Force);
- establish a joint financing agreement with development partners (Task Force and Governing Board);
- recruit the Fund Administrator (Governing Board with temporary assistance from the Task Force);
- prepare the initial budget (Fund Administrator);
- develop and approve key policies, guidelines, procedures and templates (Board with assistance from Fund Administrator);
- appoint the Operations Committee (Board, Fund Administrator); and
- approve the initial budget (Board, Operations Committee).

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- Commercial Bank of Africa
- Danida
- DI Frontier Market Energy and Carbon Fund
- European Investment Bank
- Global Canopy Programme
- Inter-American Development Bank
- Japan International Cooperation Agency
- Kenya Association of Manufacturers
- Kenya Bankers Association
- Kenya Private Sector Alliance
- KfW
- Globe
- Grantham Research Institute on Climate Change and the Environment, London School of Economics
- Ministry of Environment and Mineral Resources
- Ministry of Finance
- Ministry of Planning
- National Environment Management Authority
- National Environment Trust Fund
- Oxford Climate Policy
- Standard Bank
- Swedish International Development Cooperation Agency
- Swiss Agency for Development and Cooperation
- Transparency International
- UK Department for International Development
- United Nations Development Programme
- United States Agency for International Development
- World Bank
- World Economic Forum

In addition, the expertise and insights provided by the Finance Team's Thematic Working Group has been invaluable in guiding the research and recommendations.

¹ See the work also developed by the finance subcomponent on the appropriate carbon trading platform options for Kenya (section D of this report).

² See work also developed by the finance subcomponent on improving Kenya's low-carbon investment climate (section E of this report).

³ See, for instance, Hamilton (2009) Unlocking finance for clean energy: the need for 'investment grade' policy or CMCI (2012) Principles for investment grade policy.

⁴ See, for instance, IEA (2008) Deploying renewables- principles for effective policies.

⁵ UNDP (2011) Blending Climate Finance through National Climate Funds, http://www.undp.org/content/dam/undp/library/Environment%20and%20Energy/Climate%20Change/Capacity%20Development/Blending_Climate_Finance_Through_National_Climate_Funds.pdf

⁶ http://www.oecd.org/document/18/0,3746,en_2649_3236398_35401554_1_1_1_1,00.html#Documents

⁷ UNDP (2011) Blending Climate Finance through National Climate Funds, , http://www.undp.org/content/dam/undp/library/Environment%20and%20Energy/Climate%20Change/Capacity%20Development/Blending_Climate_Finance_Through_National_Climate_Funds.pdf

⁸ Gomez-Echeverri, L. (2010) National Funding Entities: Their role in the transition to a new paradigm of global cooperation on climate change, ecbi policy report.

⁹ See work also developed by the finance subcomponent on development partner activities in the climate change space in Kenya annexed to this report (Annex

¹⁰ Vivid Economics (2011) National funding entities: existing practices and lessons for Kenya

¹¹ This will mean that the Fund will have an important role in collecting the financial data required to comply with the biennial update reports to the COP that will be required of Kenya

¹² Benin's Fonds National de l'Environnement (FNE) is a funding entity which is also an Implementing Entity.

¹³ The National Environment Management Authority (NEMA) is the Kenyan institution accredited as National Implementing Entity (NIE) by the Adaptation Fund.

¹⁴ The GEF is currently developing proposals to allow 'direct access' to its funds through such national implementing entities.

¹⁵ Vivid Economics (2011) Current and future international climate finance architecture: implications for Kenya's financing mechanism, Annex A to this report

¹⁶ To be set out in a Fund charter.

¹⁷ See work also developed by the finance subcomponent on improving Kenya's low-carbon investment climate (Section E).

¹⁸ The PPCR, approved in November 2008, aims to pilot and demonstrate ways in which climate risk and resilience may be integrated into core development planning and implementation. In this way, the PPCR provides incentives for scaled-up action and initiates transformational change.

¹⁹ These are the concepts underlying the approach of the GEF and the Clean Technology Fund administered by the World Bank.

²⁰ Climate Investment Funds (2010) Pilot Program on Climate Resilience: Financing Modalities, May

²¹ The Adaptation Fund was established to finance concrete adaptation projects and programmes in developing countries that are parties to the Kyoto Protocol and are particularly vulnerable to the adverse effects of climate change. Over the past two years, the fund has dedicated more than \$165 million to increase climate resilience in 25 countries around the world. The Global Environment Facility (GEF) provides secretariat services to the AF Board and the World Bank serves as trustee of the Adaptation Fund, both on an interim basis.

²² Adaptation Fund (2012) Implementation of concrete adaptation measures to reduce vulnerability of livelihood and economy of coastal communities in Tanzania. Available from <http://adaptation-fund.org/project/implementation-concrete-adaptation-measures-reduce-vulnerability-livelihood-and-economy-coas>

²³ Adaptation Fund (2012) Uruguay: Helping small farmers adapt to climate change. Available from <http://adaptation-fund.org/project/uruguay-helping-small-farmers-adapt-climate-change#attachments>

²⁴ The largely subsidised ongoing Agence Française de Développement (AFD) €30-million credit line to Co-operative and CFC Stanbic banks is a precedent.

²⁵ It is recommended that the Fund work with the UNEP-sponsored Seed Capital Assistance Facility (SCAF) (which precisely seeks to encourage private equity funds in the clean energy space to scale up early stage/development funding as part of their operations) to explore areas of cooperation. See <http://scaf-energy.org/index.html>

²⁶ Broadly defined, concessionality refers to various ways to provide financing on terms that are ‘softer’ than those available from commercial sources of capital (debt or equity). The concessionality can affect the rate, tenor, and so on. The most concessional form of financing is a straight, non-reimbursable grant.

²⁷ For example, the PPCR requires beneficiary multilateral development banks to “always seek the minimum concessionality necessary to enable projects to happen and [to] justify the amount of concessionality requested in each PPCR proposal”. Climate Investment Funds (2010) Pilot Program on Climate Resilience: Financing Modalities, para 44 .

²⁸ For example, at the World Bank, the documents prepared at steps 1 and 3 are called Project Concept Documents and Project Appraisal Documents respectively.

²⁹ The role of relevant ministers and ministries will be updated pending any changes in government organization under the new constitution.

³⁰ Exact number and allocation to be agreed between Central Government and counties.

³¹ In addition, in the event that a Climate Change Authority is established, this would also be entitled to appoint an individual to the Board.

³² At a later date, in the event of the establishment of a Climate Change Authority, the Chair could be appointed among the members representing this body.

³³ As an example regarding integrity, according to the CDTF website (<http://www.cdtkenya.org/>) applicants to the CDTF must declare that the applying group ‘is not bankrupt or being wound up or are having their affairs administered by the courts; has not been convicted of an offence concerning their professional conduct; has not been guilty of grave professional misconduct; has fulfilled its obligations on payment of social security contributions or taxes; has not been the subject of a judgment for fraud, corruption, involvement in a criminal organisation or any other illegal activity’.

³⁴ It is also recommended that a target (in terms of aggregate financing pledges) be set for first closing, failing which the launch (and expenses on establishment) of the Fund would be postponed.