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## Policy pointers

**Developed countries** must commit to driving implementation of Article 2.1c, in relation to both domestic and international financial flows. They have a range of tools to progress this goal.

**Support for developing countries to implement Article 2.1c** should include assistance in evolving and updating nationally determined contributions and long-terms strategies; both should encompass ways to operationalise Article 2.1.c that are consistent with national development priorities and a framework for a just transition.

**While implementation of Article 2.1c** is important to all countries, it should not dilute developed countries' responsibility to provide climate finance to countries that have not historically contributed to climate change (in accordance with Article 9 of the Paris Agreement).

**To reach a shared understanding of Article 2.1c** that can support progress and the Global Stocktake, Parties to the UNFCCC could propose a dedicated work programme for deeper discussion and explore opportunities within the UNFCCC architecture to increase accountability for this goal.

# Urgent but overlooked: a spotlight on the long-term finance goal of the Paris Agreement

Article 2 of the Paris Agreement provides a reinforced framework for climate action by setting out three interlinked long-term goals: limiting temperature rise (2.1 a); increasing ability to adapt (2.1 b); and making financial flows consistent with a low-emission and climate-resilient development path (2.1 c). While the phrasing of the final goal seems relatively straightforward, its implications are far-reaching, with potential to be transformative. But to date, this third objective has received insufficient consideration. Uncertainties around how to interpret, implement and assess Article 2.1 c remain high, but attaining more clarity is crucial: the pending first Global Stocktake will assess progress on all three long-term goals. This briefing paper introduces Article 2.1 c, unpacks its meaning and relevance, and looks ahead to next steps in 2022's UNFCCC talks by providing key messages for national-level policymakers keen to better understand this long-term goal.

Article 2.1 of the Paris Agreement sets out three interconnected long-term goals, which aim to provide a reinforced framework to act on climate change:

- The first (2.1a), relates to efforts to limit temperature increase to well below 2°C above pre-industrial levels with pursuit of efforts to limit the increase to 1.5°C
- The second (2.1b) relates to increasing the ability to adapt to and foster resilience to the adverse impacts of climate change
- The third (2.1c) refers to “making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development”.

The third goal has far-reaching implications, recognising that we must not only increase climate finance to achieve the temperature and adaptation goals, but also redirect the public and private finance that is locking countries into high-emission, low-resilience futures.<sup>1</sup> But it has received the least consideration of all the goals: there is currently no official definition nor detailed description of its content. Article 2.1c refers neither to the traditional terms related to climate finance nor to its providers and recipients. Instead, it uses new terms such as finance ‘flows’, ‘consistent’ and ‘pathway’ that are not further defined.<sup>2</sup> Currently no dedicated space exists within the UNFCCC process to fully articulate a definition for this goal nor to develop requirements for Parties to report on the consistency of their

## *The need for definition and guidance on Article 2.1c is becoming increasingly evident*

climate flows. These knowledge gaps pose a challenge to operationalising Article 2.1c and assessing it over time.

The need for definition and guidance on Article 2.1c is becoming increasingly evident<sup>3</sup>: the first Global Stocktake (GST), due to be completed in 2023, will seek to assess collective progress toward all three long-term goals of the Paris Agreement. However, given the uncertainty around Article 2.1c, it is not clear how the GST will assess progress or

hold governments accountable for their supportive and non-supportive actions.

In anticipation of the GST and next steps in this year's UNFCCC talks, this briefing seeks to shed much-needed light on Article 2.1c by unpacking the key issues arising from it, highlighting challenges around definition and implementation, and providing key messages for those policymakers keen to ensure their national development pathways are climate resilient, emission light, and adequately funded.

### **Article 2.1c: unpacking the issues**

#### **A signal for systemic change**

Financing the global transformation of the energy sector alone will require US\$4.4 trillion annually from 2021–2025.<sup>4</sup> Clearly, to embark on a transition to a low-emission and climate-resilient development pathway, public finance flows alone will not suffice. Decarbonising the global economy to mitigate the effects of climate change can only be achieved if the entire financial system is aligned with the objectives of Article 2.1.

The ambition of the Paris Agreement goes beyond 'climate finance' as articulated in Article 9 (which obliges developed countries to provide climate finance to developing countries) and seeks to engage a broader range of actors. The term 'finance flows' used in Article 2.1c is simultaneously vague and all-encompassing,<sup>5</sup> referring to all finance flows, public and private, national and international, and including financial instruments such as bonds, insurances and equity.<sup>6</sup> This third long-term goal involves diverse financial actors with a role in managing and distributing financial resources, including financial institutions, corporations and governments.<sup>7</sup> For many, it is a vital piece of the Paris puzzle, sending a strong signal about the need to ensure that **all** finance flows actively support the transition to a low-greenhouse emissions, climate-resilient world.<sup>8</sup>

### **The need to define 'Paris alignment'**

In recent years, growing numbers of public and private institutions have publicly committed to 'align' their activities to the goals of the Paris Agreement. The Institute for Climate Economics notes, "while not used in the Paris Agreement itself, the term 'Paris Alignment' has rapidly become a catch-all phrase referring to the process needed to make an actor's activities 'consistent' with the goals of the Paris Agreement."<sup>9</sup> But without pre-defined criteria, the 'Paris alignment' of finance flows is open to interpretation.

National governments, the actors primarily responsible for delivering Article 2.1c, already have a range of levers to influence how finance is spent; for instance, by aligning their own public finance flows with the Paris Agreement by increasing the budget for climate action and decreasing public funding and investment in fossil fuels (see Box 1). Governments can also provide fiscal, policy and regulatory frameworks and incentives to shift private investments and consumer choices towards climate-friendly options. Specifically, governments can: (1) gradually eliminate financing, investment and subsidies for fossil fuels and other high-polluting industries; (2) introduce carbon pricing and taxes; and (3) harness public finance to 'de-risk' private sector investments and support low-carbon development projects.<sup>10</sup>

Private sector actors have also shown increasing interest in aligning finance flows with the Paris Agreement. Several voluntary initiatives and coalitions have emerged since the adoption of the Paris Agreement,<sup>11</sup> including the UN-convened Next Zero Asset Owner Alliance, which represents 74 pension funds, insurance companies and investors all committed to transitioning their portfolios to net zero greenhouse gas (GHG) emissions by 2025. But to see real progress on Article 2.1c, it is necessary for both the public and private sectors to better understand which activities could be relevant,<sup>12</sup> including by asking what exactly constitutes a 'green' or 'climate-aligned' investment? Does it mean climate proofing all financing-related activities? If so, how? Does consistency mean alignment with a 2°C target, or 1.5°C? Recent government efforts outside the UNFCCC system, such as the EU 'taxonomy' of sustainable economic activities,<sup>13</sup> can offer informative insight. However, minimum criteria and guidance must still be clarified by Parties to the Paris Agreement, especially as the term 'pathway' implies a variety of routes to assess the consistency of activities with the Agreement's goals, including national and sectorial pathways.<sup>14</sup>

## A developing country perspective

The long-term goal articulated in Article 2.1c is relevant to both developing and developed countries. However, it rests within Article 2 of the Paris Agreement, which aims to strengthen the global response to the threat of climate change in the context of sustainable development and efforts to eradicate poverty.

Options and progress for implementing Article 2.1c will look different for different countries. Decarbonisation and a climate-resilient transition will be challenging for developing countries with high proportions of fossil fuels in their energy mix, or those still economically dependent on fossil fuel product exports to support public spending. In addition, in many countries, a significant proportion of emissions come from deforestation due to expansion of the agricultural frontier and the transformation of forest into pastures for cattle ranching, which increases economic and social challenges.

As some countries have emphasised, it is unrealistic to expect that developing countries will follow similar timelines to developed countries to transition their economies and entirely shift away from fossil fuels.<sup>15</sup> Transition to an environmentally sustainable, climate-resilient, low-carbon economy and just society does not happen overnight. Developing countries will require significant financial support and investment to transform their economies and embark on a low-carbon pathway. This will involve diversifying national economies to create sustainable alternatives and jobs for those in sectors, cities and regions relying on carbon-intensive industries and production. Developing countries would indeed need a framework for a 'just transition' that aims to achieve economic transformation without jeopardising important development goals such as employment, food security and eradicating poverty.<sup>16</sup>

Alongside this, a critical distinction must be observed. While implementing Article 2.1c is important to all countries, efforts to do so must be understood as separate from the provision and mobilisation of climate finance mandated by Article 9 the Paris Agreement, which sets out developed countries' obligation to provide and mobilise climate finance for mitigation, adaptation and loss and damage to countries that have not historically contributed to climate change.<sup>1</sup> The commitment to provide US\$100 billion per year originates in this provision.

## Next steps within the UNFCCC?

2022 offers several opportunities for the UNFCCC to support progress on Article 2.1c:

### Box 1. Challenge and opportunity of bridging the 'alignment gap'

The latest Intergovernmental Panel on Climate Change (IPCC) report<sup>19</sup> showed how far investment and financial flows are from reaching the levels needed to deliver on the Paris Agreement. The considerable gaps in mitigation investments indicate these must grow across all regions and sectors. One analysis of the report estimates that investments in electricity need to grow by 2–5 times, in energy efficiency by 2–10 times, in transport by 7–8 times and in agriculture, forestry and other land use by 10–29 times.<sup>20</sup>

To compound this, the IPCC also found that the increasing finance flows for climate action remain insufficient in comparison to fossil fuel investment and subsidies. Latest figures from the UNFCCC's Standing Committee on Finance (SCF) showed climate finance flows for 2017–2018 reached as much as US\$775 billion on average per year;<sup>21</sup> but investment in fossil fuels amounted to US\$977 billion in the same period. Fossil fuel subsidies amounted to US\$472 billion in 2018 alone.<sup>22</sup> These numbers indicate the scale of the challenge, but also the scale of the opportunity that would arise if all financial flows were consistent with climate objectives in the near future.<sup>23</sup>

## Increase information to inform action

At COP26, the SCF (the central body within the UNFCCC providing input on Article 2.1c) was given two mandates related to advancing work on this long-term goal. Both are expected to be delivered in time to inform discussions at COP27:

### 1. Further map the available information

**relevant to Article 2.1c.** This builds on the first mapping exercise, conducted as part of the fourth biennial assessment in 2020 (an overview of climate finance flows given in Chapter 4 of the related technical report<sup>11</sup> offers a valuable starting point for understanding Article 2.1c).

### 2. Synthesise views on ways to achieve Article 2.1c, including options for approaches and guidelines for implementation.

Considering the existing knowledge gaps, it is important that the synthesis report:

- (i) Discusses activities that might be relevant to implementation (this involves defining 'consistency' and 'alignment')
- (ii) Suggests criteria and methodologies for tracking progress
- (iii) Explores solutions, methods and tools for accelerating action.

## Enable deeper, broader engagement

Next year, the first Global Stocktake (GST) will consider how far implementation of the Paris Agreement's three long-term goals has progressed, including Article 2.1c. We know the GST process will certainly rely on reports by the SCF and IPCC, but it is unclear whether additional data or information sources will be collected and considered. While limited sources

are a concern, the GST has already shown interest in better understanding Article 2.1c.

In June 2022, the GST's first technical dialogue<sup>17</sup> (held during the 56th meeting of the Subsidiary Bodies) included a roundtable meeting that discussed progress on climate finance and on Article 2.1c more specifically; presentations by experts from the SCF and IPCC were followed by interventions from Parties addressing a set of reflection questions. This meeting demonstrated that there are still diverging views on Article 2.1c, including uncertainties around interpretation and implementation.

It is yet to be seen whether Parties will engage more deeply with these questions at the third and fourth technical dialogues, later in 2022 and in June 2023 respectively. To assist the GST, Parties could propose the creation of a dedicated work programme under the UNFCCC to discuss matters related to Article 2.1c in more depth, including engaging non-Party stakeholders such as private sector actors. A dedicated space could help to crystallise relevant methodologies, standards to track progress, and guidance to the international community on implementation of Article 2.1c.

## Consider leveraging transparency reporting

Ultimately, transparency is what will build trust and confidence for effective implementation of the Paris Agreement. The challenge of Article 2.1c is that individual country reporting is not yet defined. But the Enhanced Transparency Framework (ETF), though not equipped to require specific information on progress towards Article 2.1c, could generate valuable information. For instance, in 2024, developed countries' first

biennial transparency reports are expected to describe how support provided and mobilised has assisted the long-term goals, including Article 2.1c. While this reporting requirement — set out in paragraph 121.q of the modalities, procedures and guidelines (MPGs) of the ETF — does not request specific information, future versions of the MPGs could do so. This might, for example, be done via an additional column in developed countries' CTFs (the 'common tabular formats' used for electronic reporting). More specific information on Article 2.1c could in turn increase the substance of inputs to the GST.

Conversely, under the ETF, developing countries can report on financial, technology transfer and capacity-building support needed and received for climate action. Within this, they could identify specific policy and capacity-building support needed to operationalise Article 2.1c in line with their nationally determined contributions and long-term strategies.<sup>18</sup>

## Time to act on the long-term finance goal

Article 2.1c is fundamental to the Paris Agreement: it is not just one of three goals, it is a **means** to meet the other two. To free the transformative potential of Article 2.1c, a unified understanding of 'Paris-aligned finance flows' and how to measure progress are both critical, especially as the GST looms closer.

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## Knowledge Products

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## Notes

<sup>1</sup> Lopez Carbajal, A, Rojas Squella, X and Watson, C (2021) Consistency case study: actions supporting Article 2.1c of the Paris Agreement in Colombia. Climate Works Foundation and ODI. / <sup>2</sup> Zamarioli, LH, Pauw, P, König, M and Chenet, H (2021) The climate consistency goal and the transformation of global finance. *Nature Climate Change* 11, 578–583. / <sup>3</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning Article 2.1c. Page 7. Climate Finance Advisory Service (CFAS). / <sup>4</sup> IRENA (2021) World Energy Transitions Outlook: 1.5°C Pathway. International Renewable Energy Agency, Abu Dhabi. / <sup>5</sup> Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) GmbH (2022) Submission to the UNFCCC. Matters relating to the SCF — ways to achieve Article 2.1c. / <sup>6</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning Article 2.1c. Page 4. CFAS. / <sup>7</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning Article 2.1c. Page 8. CFAS. / <sup>8</sup> Whitley, S, Thwaites, J, Wright, H and Ott, C (2018) Making finance consistent with climate goals. Insights for operationalising Article 2.1c of the UNFCCC Paris Agreement. Page 6. ODI, London. / <sup>9</sup> Cochran, I and Pauthier, A (2019) A Framework for Alignment with the Paris Agreement: Why, What and How for Financial Institutions? Page 9. Institute for Climate Economics. / <sup>10</sup> For more on tools to drive action see: note 8. / <sup>11</sup> See: UNFCCC (2021) UNFCCC Standing Committee on Finance. Fourth (2020) Biennial Assessment and Overview of Climate Finance Flows. <https://bit.ly/3OCHFVY> / <sup>12</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning article 2.1.c. Page 9. CFAS. / <sup>13</sup> This taxonomy establishes criteria for determining whether an economic activity qualifies as environmentally sustainable. / <sup>14</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning article 2.1.c. Page 12. CFAS. / <sup>15</sup> Republic of Zambia on behalf of the African Group of Negotiators (AGN) (2022) Views on ways to achieve Article 2, paragraph 1(c) of the Paris Agreement. <https://bit.ly/3PWLG6G> / <sup>16</sup> Republic of Kenya (2022) Views on ways to achieve Article 2, paragraph 1(c) of the Paris Agreement. <https://bit.ly/3clZYeM> / <sup>17</sup> The GST consists of three components: (1) information, collection and preparation; (2) technical assessment; and (3) consideration of outputs. The Technical Dialogues forms part of the second component. / <sup>18</sup> Whitley, S, Thwaites, J, Wright, H and Ott, C (2018) Making finance consistent with climate goals. Insights for operationalising Article 2.1c of the UNFCCC Paris Agreement. Page 26. ODI, London. / <sup>19</sup> IPCC (2022) Sixth Assessment Report. Climate Change 2022: Mitigation of Climate Change, the Working Group III contribution. / <sup>20</sup> See: Maitais, A (2022) Investment and finance gaps. In: *Eight takeaways from the IPCC report on climate mitigation*. Stockholm Environment Institute. [www.sei.org/perspectives/takeaways-ippc-report-climate-mitigation](http://www.sei.org/perspectives/takeaways-ippc-report-climate-mitigation) / <sup>21</sup> See: note 11, page 7. / <sup>22</sup> See: note 11, page 12. / <sup>23</sup> Goritz, A, Nettersheim, C and Ryfish, D (2021) Making finance flows consistent with the Paris Agreement: Opportunities and challenges concerning article 2.1.c. Page 5. CFAS.

