UNPACKING FINANCE FOR LOSS AND DAMAGE

Lessons from COVID-19 for addressing loss and damage in vulnerable developing countries

What is loss and damage?

Loss and damage\(^1\) has been defined as the impacts of climate change which are not avoided by mitigation, adaptation and other measures such as disaster risk management (Verheyen, 2012; Roberts and Pelling, 2018). It has both economic and non-economic costs and results from both extreme weather events like hurricanes and floods and slow onset climatic processes such as sea level rise and salinisation. Loss and damage includes permanent and irreversible losses such as to lives, livelihoods, homes and territory, for which an economic value can be calculated and also to non-economic impacts, such as the loss of culture, identity and biodiversity, which cannot be quantified in monetary terms. Loss and Damage became officially recognised at COP 19 in 2013 after the catastrophic effects of Typhoon Haiyan (also known as Super Typhoon Yolanda) on the people of the Philippines made it apparent that vulnerable developing countries required significant levels of support in the face of such widespread devastation. In 2015, at COP 21, Loss and Damage was included as a distinct article in the Paris Agreement, separate from adaptation. This was an important milestone as developing countries have long stressed that loss and damage refers to climate change impacts that are “beyond adaptation”.

The COVID-19 crisis: resetting our level of ambition

The COVID-19 pandemic has had significant and potentially long-lasting impacts on economies and societies worldwide. Globally, COVID-19 has had the most profound impact on vulnerable developing countries, communities and people, impeding both sustainable development and efforts to build resilience to climate change. Worldwide, more than 100 million more people are expected to join those already living in extreme poverty and global poverty is expected to rise in 2020 after decades of successful alleviation efforts (IMF, 2020). The pandemic has stretched already overwhelmed budgets and diverted resources away from climate action to respond to an acute social, health and economic crisis. While COVID-19 is an acute, but hopefully short-lived crisis, the spectre of catastrophic climate change looms as a long-lasting challenge. In the midst of our response to and recovery from the pandemic, we must not sideline efforts to minimise the long-term impacts of climate change. Indeed, we must use the crisis as an opportunity to reset our level of ambition, ensuring that, aligned with the Paris Agreement, we both speed up and scale up the climate action so urgently needed.

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\(^{1}\) Loss and Damage (capitalised) has been used to refer to the spectrum of policies which can be implemented to address loss and damage while loss and damage refers to the manifestation of the impacts of climate change (IPCC, 2018).
Strengthening international solidarity to address global challenges

In most parts of the world, the most vulnerable people, communities and countries are already experiencing significant loss and damage from climate change impacts. As the pandemic has raged, the climate crisis has not abated even if the attention of the world’s media has been consumed with COVID-19. Severe impacts of climate change have continued resulting in billions of dollars in losses and damages. In early April 2020, Cyclone Harold hit Vanuatu causing widespread damage, leaving up to 90 percent of the population homeless. In late May, Cyclone Amphan crashed into India and Bangladesh, two countries that had been hit hard by the pandemic. In Bangladesh, the cyclone resulted in 13 billion USD in loss and damage to infrastructure alone. This came as the country was experiencing the economic toll of the global response to COVID-19 which has had significant repercussions for the garment industry – among other sectors. Meanwhile, in East Africa above average rainfall throughout 2020 has resulted in widespread flooding forcing more than 1.5 million people to leave their homes.

One of the greatest lessons of the response to COVID-19 is the importance of solidarity at all levels to support the most vulnerable cope with and recover from a crisis. Early in the pandemic, the UN Secretary General stressed the importance of global solidarity and international cooperation in the response to and recovery from COVID-19 (UNESC, 2020). In March of 2020 the UN Conference on Trade and Development (UNCTAD) estimated that 2.5 trillion USD would need to be mobilised to help developing countries respond (UNCTAD, 2020). In May of 2020 the UN launched the Financing for Development in the Era of COVID-19 initiative (UN, 2020). Under the leadership of Canada and Jamaica, six discussion groups were established on issues relevant to financing development during and after the pandemic. Each discussion group was led by at least two UN member states and engaged a range of relevant stakeholders (Ellmers, 2020). The process has seen unprecedented levels of engagement from heads of states and government as well as the heads of the International Monetary Fund (IMF), World Bank and the Organisation for Economic Cooperation and Development – who traditionally have not actively engaged in UN processes (Ibid).

We propose that such a fund or facility must equally be set up to address loss and damage, targeted to those countries most impacted by climate change. This international solidarity facility on loss and damage would be made up of both public, private and innovative sources of finance and would represent substantial support to those most vulnerable and exposed to climate change impacts, yet least responsible for them, ensuring the human rights of affected populations are protected (see ActionAid, 2019).
Harnessing finance to fund an international solidarity facility on loss and damage

Another lesson from the COVID-19 crisis is that we can address huge global challenges. During the pandemic, resources have been created and mobilised when needed. In March of 2020 the UN Conference on Trade and Development (UNCTAD) called for 2.5 trillion USD to be mobilised to help developing countries respond to COVID-19 (UNCTAD, 2020). At the beginning of the global pandemic, in April 2020, the IMF announced that it had already secured 1 trillion USD in lending capacity to begin meeting the demands. By October of 2020, countries had taken fiscal action amounting to 12 trillion USD to respond to the pandemic – which amounts to nearly 12 percent of global GDP (IMF, 2020). A similar effort could also be taken to mobilise funding to address loss and damage, targeted to support the most vulnerable developing countries. The recovery from COVID-19 must also build the resilience of vulnerable developing countries and better enable them to address loss and damage in the long-term.

Scaling up support to developing countries to finance their efforts to address loss and damage is pragmatic and will help create a safer, more resilient world. Implementing measures to ensure that vulnerable people, communities and countries are equipped to prepare for and address loss and damage is inextricably linked. Given that loss and damage also impedes both development and efforts to build resilience, it is illogical not to invest in addressing loss and damage. In addition, if developing countries are forced to devote their own resources to addressing impacts of loss and damage, their efforts in respect of mitigation and adaptation are put in jeopardy and will almost certainly be delayed.

How much funding is needed to address loss and damage?

The projected economic cost of loss and damage by 2030 has been estimated to be 400 billion USD a year by one study (Baarsch et al., 2015) and between 290 and 580 billion USD in another (Markandya and González-Eguino, 2018) in developing countries alone. By 2050 the economic cost of loss and damage in developing countries is estimated to be between 1,132 and 1,741 billion USD (Markandya and González-Eguino, 2018) and between 1 to 1.8 trillion USD (Baarsch et al., 2015). This does not include the cost of non-economic loss and damage such as the loss of culture, biodiversity and ecosystem services – as well as the untold psychological and mental costs that climate change impacts bring – for which very little funding is available (Schäfer and KüNZel, 2019). The economic costs of addressing loss and damage will likely be even greater given the impacts of COVID-19 on economies and societies and the resulting set-back to sustainable development efforts in vulnerable developing countries.

Where should support for vulnerable developing countries to address loss and damage come from?

If between 290 and 580 billion USD is needed annually by 2030 to address loss and damage in developing countries alone, we must start scaling up finance for Loss and Damage today. We suggest a commitment from developed countries to begin immediately with the provision of “fast start” loss and damage finance of USD 75 billion between 2020 and 2023 with the goal to scale up financing in order to provide at least 150 billion USD a year by 2030 for vulnerable developing countries to address loss and damage – from public sources. This is ambitious, certainly, given historical levels of climate finance provision. However, the response to COVID-19 has demonstrated that it is entirely possible to mobilise substantial sums quickly. Moreover, previous efforts to catalyse global solidarity have set a precedent for how additional funding can be channeled to those who need it most to meet urgent global challenges.

The 150 billion USD a year by 2030 from public sources for addressing loss and damage is above and beyond finance provided for adaptation. This would
be integrated into the new finance goal under the UNFCCC, to come into effect from 2025. This level of support is commensurate with developed countries obligations as part of a global commitment to keep global average warming to below 2°C and ideally, 1.5°C. With higher emission trajectories, the costs of addressing loss and damage in vulnerable developing countries will be much greater. The majority, if not all, of this finance must be provided in the form of grants, particularly for countries that have been deemed highly vulnerable such as the least developed countries (LDCs) and the small island developing states (SIDS).

We would propose that, additionally, at least 150 billion USD a year would be mobilised, from alternative and innovative sources, the most promising of which are described below. The funding raised by these and other innovative sources of finance could be channeled to vulnerable developing countries through an international solidarity facility on Loss and Damage. Vulnerable developing countries have already articulated the types of actions for addressing loss and damage that they require finance for.

Special Drawing Rights

Special Drawing Rights (SDRs) are foreign exchange reserve assets, units of account rather than a currency, which are maintained by the IMF. SDRs are the potential to claim on the currency of IMF members and can be exchanged for these currencies to create liquidity. At the beginning of the pandemic UNCTAD proposed that 1 trillion USD could be mobilised through SDRs (UNCTAD, 2020) though others have proposed that 2 trillion USD could be raised through this modality (Ghosh, 2020). Most IMF member states support an issuance of 1 trillion USD in SDRs and with support of the new US administration, the proposal could be adopted (Elli, 2020). A report by the Global Policy Forum and partners outlines a roadmap for how SDRs could benefit vulnerable developing countries, which includes developed countries allocating their SDRs to developing countries (see: Elli, 2020). A recent report on the resilience and just recovery from COVID-19 proposes that along with a new and sizeable allocation of SDRs developed countries could also reallocate their unused SDRs to developing countries (Voltz et al., 2020). When combined with debt relief (see below) and the mobilisation of new capital, SDRs would free up fiscal space to respond to and recover from COVID-19 in the short-term and build resilience to climate change in the longer-term (Ibid).

The role of SDRs in scaling up the level of finance available for climate action was raised in 2010 in a report by ActionAid (see: ActionAid, 2010). There is a precedent for the use of SDRs in times of crisis. Most recently they played a role in responding to the global financial crisis in 2009 when 250 billion USD in SDRs were issued in a special allocation (Elli, 2020). Climate change has already been conceptualised as a global challenge. Financial tools like SDRs could therefore be extended towards efforts to address loss and damage. This would require unprecedented levels of global solidarity on climate change, but the pandemic has demonstrated that this is possible. Lessons from the Financing for Development in the Era of COVID-19 and Beyond initiative could be drawn upon to strengthen the global effort to address loss and damage in vulnerable developing countries and SDRs could be issued and allocated to support this effort.

Subsidies

In 2015, the world spent US$ 4.7 trillion on fossil fuel subsidies, growing to US$ 5.2 trillion in 2017 or 6.5% of GDP. According to Dr Edward Cameron, by redirecting “fossil fuel subsidies as part of [post-Covid] stimulus, we could cut global carbon emissions by 28% and increase government revenue by 3.8 % of GDP.” Currently, developed countries continue to pay significant subsidies to fossil fuel producers despite commitments to reduce them. There are five types of fossil fuel subsidies which are indicated below with the average sums that G-20 countries spend as well as the share of total support for 2017-19 (Geddes et al., 2020).

- **Direct budget transfers**, consisting of payments made directly to consumers or producers of fossil fuels: 25 billion USD (4 percent);
- **Tax expenditure**: tax breaks and reliefs offered to those consuming or producing fossil fuel (for example, additional tax relief on investments): 79 billion USD (29 percent);
- **Price support**: below-market prices regulated on behalf of consumers: 172 billion USD (29 percent);
- **Public finance**: loans and guarantees at market and below-market price: 51 billion USD (9 percent);
- **State-owned enterprise (SOE) investment**: support for SOEs in fossil fuel production: 257 billion USD (44 percent).

Governments should phase out and redirect fossil fuel subsidies. If redirected, a 4 percent decrease annually in fossil fuel subsidies by G-20 countries could raise space to respond to and recover from COVID-19 in the short-term and build resilience to climate change in the longer-term (Ibid).
245 billion USD to support efforts to address loss and damage between now and 2030.

In 2016 G-7 countries committed to ending fossil fuel subsidies by 2025. An analysis by Action Aid and the Robin Hood Tax Campaign found that if G-7 countries ended fossil fuel subsidies this would free up 101 billion USD by 2026 (Action Aid, 2020).

**Financial Transactions Tax**

Finance for addressing loss and damage could be raised through a financial transactions tax (FTT) on financial trades including stocks, bonds and derivatives (Climate Action Network, 2018). The FTT has pedigree and provenance appearing in Keynes’s *General Theory* and developed (particularly in respect of the taxation of currency trades) by Nobel prize-winning economist, James Tobin. First emerging in the 17th century, the stamp duty – a fee for receiving a stamped document officially granting legal title or ownership rights over a purchase – predates income tax.

Over the last ten years, the FTT has been introduced in a number of states, including France, Italy, Spain, Tanzania and Kenya. The nature of these FTTs, whilst robust in respect of tax capture, has been unambitious in terms of scope, limited for the most part to transactions in the shares of large companies. A regional European FTT is currently under negotiation along the same lines, which would add Germany, Austria and Portugal to the family of FTT countries, which already include the UK, India and South Africa.

A more comprehensive taxation of financial trades offers the prospect of a sizable new income stream which could be used to address loss and damage. Due to the enormous sums traded in financial markets, levying a modest charge on transactions of not only equities but also bonds and derivatives has the potential to raise tens of billions a year in additional revenue. With the addition of foreign exchange – the largest market in the world currently standing at a staggering 6.6 trillion USD a day (BIS, 2019) – income could be as high as 297 billion USD a year (Spratt and Ashford, 2011). FTTs are progressive in nature with economic incidence falling on financial firms undertaking large quantities of transactions on a daily basis and on high net worth individuals.

**Climate Damages Tax**

The Climate Damages Tax (CDT), also known as the Robin Hood tax on polluters, is a proposal for a charge for each tonne of coal, barrel of oil or cubic litre of gas extracted based on how much CO2 is embedded in each fossil fuel (Richards et al., 2018). The CDT could be introduced in 2022, beginning at 5 USD per tonne of CO2e and would increase by 5 USD per year until 2030 when it would be raised to 50 USD per tonne of CO2e, increasing by 10 USD each year. The revenue from the CDT would raise an estimated 210 billion USD in the first year, increasing thereafter and would also incentivise the eventual phasing out of fossil fuels (Richards et al., 2018). The CDT would work with existing systems of payment where fossil fuel companies already pay royalties (or similar) to the states in which they operate. It would tax those benefiting from the extraction of fossil fuels, the main contributor of human induced climate change, and would benefit those countries who are most greatly affected by the impacts of climate change. ActionAid has identified the CDT as the financing mechanism for loss and damage best compliant with human rights (ActionAid, 2019).

**Air Passenger Levy**

In 2008, the Group of LDCs in the UNFCCC negotiations proposed an International Air Passenger Adaptation Levy (IAPAL) as a tax on international airfares of up to 6 USD for economy class and up to 62 USD for business or first class (Chambwera et al., 2011). It was estimated that this could raise between 8 billion and 10 billion USD annually which would be allocated to support adaptation in LDCs and other developing countries (Legal Response Initiative, 2013). This proposal was ultimately not taken forward at the time it was initially proposed but has recently been revived. In a recent report to the UN General Assembly, the UN Special Rapporteur on Human Rights and the Environment proposed that the IAPAL could be used to finance Loss and Damage in vulnerable developing countries (UN General Assembly, 2019).

There is already a precedent for generating income from this type of taxation following the French-led Air Passenger Levy Initiative. Revenue raised through this aviation tax is channeled directly to UNITAID, hosted at the World Health Organization, which supports efforts to prevent, diagnose and treat HIV/AIDS, tuberculosis and malaria. Since it was established in 2006, UNITAID has raised over 3 billion USD. In 2018/2019 UNITAID invested 1.3 billion USD in global health initiatives. UNITAID provides an example of
national collection of tax revenue which contributes to an international solidarity fund.

In respect of rationale, taxing an activity that contributes greatly to global emissions and using the funds to support efforts to address loss and damage draws a direct line from cause (air travel which increases global emissions) to effect (loss and damage from the impacts of climate change). In terms of the potential for political will to implement an aviation levy when air travel has been so severely impacted by the COVID-19 pandemic, the prospects of decision makers increasing taxation on this industry at this time are challenging. Escalating charges on most frequent flyers would appear to be the most politically appealing of aviation levies in the near future.

**Debt relief**

Loans can help countries in times of crisis to address liquidity shortfalls quickly. However, loans can also be unjust and unsustainable and can ultimately keep developing countries in a cycle of poverty, impeding both sustainable development and climate action. Each year 300 billion USD is spent in debt repayments by developing countries (Eurodad, 2020) and even before the COVID-19 pandemic 31 countries were in debt crisis (Jubilee Debt Crisis, 2020). The pandemic is forcing vulnerable developing countries to take out additional loans to meet the basic needs of their populations. This has increased debt loads in many countries and will have lasting impacts on economies and societies. By the end of 2020 the level of global public debt is expected to approach 100 percent of global GDP (IMF, 2020).

Early in the pandemic UNCTAD recommended that 1 trillion USD could be freed up to respond to the crisis in developing countries through debt relief (UNCTAD, 2020). In April of 2020 the G20 offered a moratorium on debt re-payments called the Debt Service Suspension Initiative, offered to low income countries. However, the moratorium covers only bilateral loans, which comprise a limited and decreasing share of overall debt (Ellmers, 2020). No support was offered to middle income countries. The report by the Global Policy Forum and partners proposes that debt cancellation could be extended to other types of loans including multilateral debt and debt owed to private creditors (see: Ellmers, 2020).

If a severe weather event strikes a small island state, for instance, that is already in debt distress (of which there are many currently in the world) the collapse in its GDP from catastrophic damage to its economy will lead to debt default, making an extremely difficult position, even worse. Provision for an immediate debt moratorium needs to be put in place with rapid negotiations to reschedule payments or preferably remove the debt burden.

There are two kinds of debt relief that could be used to address loss and damage: debt cancellation or debt swaps (Ellmers, 2020). Debt relief does not mobilise additional resources but frees up fiscal space (assuming countries had the resources to service debt in the first place) to allow countries to dedicate more domestic resources to adapting and building resilience to climate change and addressing loss and damage when climate change impacts cannot be avoided. During the pandemic, several proposals have been developed for how debt relief could and should play a role in the resilient recovery from COVID-19 (see: Voltz et al., 2020). One of these is the Debt Relief for Green and Inclusive Recovery Initiative which would support a sustainable recovery while building resilience through debt cancellation and debt swaps for sustainable development. This initiative should also include and support efforts to address loss and damage in the long-term.

**Summary: lessons from COVID-19 to finance efforts to address loss and damage**

The worldwide response and recovery from COVID-19 provides lessons for global efforts to address loss and damage. Resources have been mobilised at great speed and at substantial scale in response to the pandemic. We now have an opportunity to apply these lessons through an international effort to support vulnerable developing countries in their efforts to address loss and damage, including to:

- Ensure that the recovery from COVID-19 in vulnerable developing countries builds resilience to the impacts of climate change and increases their capacity to address loss and damage.

- Take lessons from the global response to COVID-19 including from the Financing for Development in the Era of COVID-19 initiative which has had strong engagement from heads of state and government and high level stakeholders, to focus on catalysing an international effort to address loss and damage in vulnerable developing countries.

- Establish an international solidarity facility to channel this funding to vulnerable developing countries for addressing loss and damage.


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