

ENSURING FINANCIAL INTEGRITY AND DUE DILIGENCE IN FUNDING FOR CLIMATE ACTION

Green Climate Fund Integrity Policies in Practice: Lessons from Direct Access Entities

Summary

- ▶ A strong financial framework is essential to ensure climate funding is used for intended purposes. This includes internal oversight mechanisms, publication of financial reporting and audit information, compliance reviews and proactive disclosures of spending. By keeping monetary flows fully transparent, entities working on climate issues can promote integrity in their financial systems, guarding against bribery, embezzlement, fraud and other prohibited practices.
- ▶ Thorough due diligence on all recipients of funding or payments is essential. Assessment and verification of financial systems of implementing agencies, suppliers, contractors and employees associated with a project give assurance that an entity's funds are well spent.
- ▶ The due diligence process must include scrutiny for “red flags” that raise concerns and warrant further investigation, including financial instability, inexperience or a history of project failures, conflicts of interest, legal violations, or poor transparency in financial reporting or decision-making.
- ▶ Entities are required to identify and verify the beneficial owners of any organisation they partner or disburse funding to. This may help indicate potentially unsound transactions. By knowing who ultimately owns or controls an entity, they can ensure the organisations they work with are not vehicles for exercising undue influence or operationalising corrupt deals.
- ▶ The [GCF Anti-Money Laundering and Countering the Financing of Terrorism Policy](#) outlines the high ethical standards and internal controls required to mitigate risks of financial and reputational loss through involvement with financial structures designed for money laundering or terrorism financing.
- ▶ Transparent financial systems and in-depth knowledge of partner entities support informed decisions on allocating climate finance for maximum positive impact.



AN ESSENTIAL COMPONENT OF ALL CLIMATE PROGRAMMES

A strong financial framework, backed by thorough due diligence on all recipients of funding or payments, is essential to ensure climate funding is used for intended purposes. Such a framework includes establishment of internal oversight mechanisms, publication of financial reporting and audit information, compliance reviews and proactive disclosures of spending, among other measures. Independent internal and external audits of an entity's accounts, processes and performance are also essential, giving a credible assessment of its competence and compliance with laws and regulations.

Assessment and verification of financial systems of implementing agencies, suppliers, contractors

and employees associated with a project also help ensure an entity's funds are well spent. By keeping monetary flows fully transparent at every level, climate entities can promote integrity and accountability in their financial systems, guarding against bribery, embezzlement, fraud and other prohibited practices.

Comprehensive financial safeguards provide valuable benefits to entities implementing climate programmes, promoting integrity in operations and safeguarding their projects, resources and reputation – ultimately helping protect the planet and people whose lives are directly impacted by climate change.



Image: Green Climate Fund / Angeli Mendoza

UNDERPINNING THE GCF'S ANTI-CORRUPTION APPROACH

The Green Climate Fund's fiduciary standards for administrative and financial capacities rest on three underlying principles:

- ▶ Financial inputs and outputs must be properly accounted for, reported and administered transparently, accountably and in full compliance with national legal frameworks.
- ▶ Reliable and complete information relating to the overall administration and management of an entity must be available.

- ▶ Entities must demonstrate a track record of effectiveness and efficiency.

These standards reflect the GCF's zero-tolerance approach to prohibited practices. The Fund views comprehensive financial integrity measures and due diligence procedures as critical to safeguard the resources entrusted to it, by helping prevent, detect and address wrongdoing effectively. The GCF's fiduciary standards and Anti-Money Laundering and Countering the Financing of Terrorism Policy provide clear avenues for assessing risk and establishing the safeguarding and oversight mechanisms needed for



effective financial management. This helps the Fund to maintain the highest integrity standards, and detect and mitigate financial and reputational risks as early as possible.

To further safeguard climate funding, the GCF also requires the Accredited Entities (AEs) whose climate programmes it finances to establish their own

measures for financial integrity and due diligence. AEs are encouraged to consult the GCF's Independent Integrity Unit (IIU) for advice and support on establishing their financial framework and best practice. The IIU will work closely with entities to prevent and deter prohibited practices, in support of meeting climate targets.

VALUABLE REAL-WORLD LESSONS ON ENSURING FINANCIAL INTEGRITY

This brief links good practices on implementing effective financial integrity measures and due

diligence procedures to GCF accreditation requirements. Drawing on the diverse real-world experience of AEs from the Peer-to-Peer Learning Alliance on Climate Finance Integrity, it shows how strong financial management and oversight mechanisms and thorough due diligence procedures can mitigate corruption risks effectively, and deter and identify integrity violations. Backed by insights from integrity experts at Transparency International and the IIU, the brief offers tools and tips to enable AEs, those seeking accreditation and their partners to safeguard climate programmes from corruption and strengthen integrity through effective financial management and protection measures.

Sharing rich integrity experience: the Peer-to-Peer Learning Alliance

Established in 2017, the Peer-to-Peer Learning Alliance on Climate Finance Integrity brings together knowledgeable representatives of seven GCF Direct Access Entities from six countries, allowing members to openly share experience, competencies and practices, and to support each other in problem solving and strengthening their institutions' integrity frameworks.

The alliance covers diverse institutions such as development banks, government bodies and quasi-state organisations, spanning sectors including agriculture, conservation, renewable energy and water, under the overarching theme of climate change mitigation and adaptation. Members' programmes vary widely in terms of scale, fiduciary standards and project stage – from recent accreditation to advanced project implementation. This diversity makes the peers' combined experience widely applicable to many other national or regional entities, offering rich learning to those seeking GCF accreditation or wanting to apply best practice around issues of integrity.

“ To ensure financial integrity and that the recipients of funds disbursed by the Vietnam Development Bank meet GCF requirements, we evaluate and assess each borrower and their collateral, including their beneficial owners. Only when we are satisfied do we sign a credit agreement. These agreements contain special clauses covering GCF integrity requirements, which recipients must fulfil before we will release any funds. We then monitor our borrowers' spending closely and provide a letter of no objection for every step of their procurement processes, if required and applicable. We also assess implementation throughout the project lifecycle, looking out for red flags such as slow progress, poor reporting systems and weak communication.”

Nguyen Hoang Trung

Director, Foreign Loan Department,
Vietnam Development Bank



FRAMEWORKS FOR ACHIEVING FINANCIAL INTEGRITY

The GCF requires AEs to have in place a documented control framework that defines a culture of integrity at all levels, set by senior management (the “tone at the top”). It must include risk assessment, internal control and audit activities, monitoring, and procedures for information sharing. AEs need institutional risk-assessment processes to provide a basis for proactive risk responses in financial management. The control framework guides the financial management framework, which defines and assesses internal controls annually in core financial management areas, including budgeting, accounting, flow of funds, financial reporting and auditing. It is recommended that duties are segregated between settlement processing, procurement processing, risk management and accounting.

AEs are encouraged to have resources, systems and procedures in place to ensure regular, transparent reporting on the use of finance received from the Fund, reflecting internationally recognised accounting standards. Entities must use business plans, financial projections and budgets transparently, and continuously monitor performance and expenditure against these plans.

Key principles underpinning an effective financial management framework:



Integrated transparency and accountability

Entities’ general management policies, procedures and systems must promote an organisational culture conducive to fairness, accountability and full transparency across all activities and operations, and must demonstrate transparency and accountability to prevent mismanagement and fraudulent, corrupt or wasteful practices. These may be integrated into an entity’s conflict of interest policy and code of ethics, reflecting a culture of zero tolerance for fraud, financial mismanagement and other forms of wrongdoing. AEs should have the necessary capacity to prevent or address financial mismanagement and malpractice, including reporting channels, whistleblower protection mechanisms and an independent, objective investigation function.



Enhanced Due Diligence procedures

Safeguarding climate finance requires comprehensive due diligence measures to assess and evaluate the extent of associated financial and integrity risk – including risk of money laundering and terrorism financing. This involves ascertaining and verifying the true identity of another person, organisation or entity, so that you really understand who the entities receiving your money are, or who you’re partnering with – including their beneficial owners (see box on page 6).

Comprehensive due diligence procedures help you detect risk of conflict of interest, embezzlement, fraud and other prohibited practices, ensuring entities you work with uphold the GCF’s high integrity standards. These procedures entail examining another organisation’s financial records and management systems, ownership structure, decision-making processes, oversight mechanisms and integrity framework. These checks must be carried out before entering into a proposed agreement or transaction with any organisation. The GCF requires due diligence to be based on risk assessment and to be thoroughly documented to help protect the Fund’s financing and ensure it meets agreed climate targets.



Image: Radoslaw Baill/Unsplash



Knowing our partners' track record

To mitigate potential risks and ensure successful project execution, it's essential to conduct thorough due diligence and address any red flags, says Dr. Manish Raj Pandey, Head of the Department of Climate Change and Knowledge Management at Nepal's National Trust for Nature Conservation (NTNC).

"To ensure financial integrity and compliance with the GCF requirements, NTNC has adopted key measures to safeguard our own financial integrity, as well as that of our partners and recipients of funds. During project planning, we conduct due diligence on both the project and the implementing organisations, starting with a comprehensive feasibility study, then a risk assessment, so we can develop mitigation strategies to minimise potential challenges. We also carry out a legal and regulatory review to ensure compliance, and an environmental impact assessment to ensure sustainability.

Identifying reliable partners

We assess an executing entity's ability to deliver the project successfully, examining its capacity, resources and financial track record to determine its stability and past performance. We evaluate its experience and the project team's expertise to ensure the necessary skills and knowledge to handle the project effectively. Checking references and evaluating the entity's reputation in the sector provides insights into its past performance and credibility. We also examine its legal compliance and organisational structure, governance and management practices. Identifying any potential conflicts of interest is critical, as these may affect the entity's ability to act impartially in executing the project.

Recognising indicators of integrity violations

During the due diligence process, we look out for red flags – indicators that raise concerns and warrant further investigation. These include significant financial instability, lack of experience in executing similar projects, or a history of project failures. Conflicts of interest, legal violations or disputes, and lack of transparency in financial reporting or decision-making processes require further scrutiny. Inadequate resources, capacity or skills to execute the project effectively are clear red flags. It's also important to take into account poor references or negative feedback from previous clients or stakeholders.

Knowing an entity in-depth in this way enables us to make informed decisions about how we allocate climate finance for maximum positive impact."



Protection against money laundering and terrorism financing

The GCF emphasises the highest ethical standards in its [Anti-Money Laundering and Countering the Financing of Terrorism Policy](#). This outlines the minimum internal control standards which you must maintain to mitigate risks of financial and reputational loss through involvement in financial structures designed for money laundering or terrorism financing. Your due diligence must be consistent with [Financial Action Task Force \(FATF\) recommendations](#), and you must also apply these standards to entities implementing your projects

to ensure that GCF finance is not linked with illegal financial flows or funding terrorist activity. Your entity should implement a continuous risk-based approach and adopt appropriate mitigating measures to ensure all transactions meet legal requirements and international standards to prevent money laundering and terrorism financing.

In particular, AEs are encouraged to review and assess all the beneficial owners of a company or organisation, identifying the natural persons who ultimately own or control an entity, or on whose behalf transactions are being conducted.



Beneficial Ownership: The importance of “knowing your customer”

Understanding the beneficial ownership of organisations you might invest in, lend to, partner with or buy from will help your entity identify who to work with – and who to avoid.

Anonymous companies and trusts can be used to hide the identity of the organisation, group or person involved in a transaction. They can become vehicles to launder and transfer money, exercise undue influence or operationalise corrupt deals. This makes it vital that you know the beneficial owners of any entity you partner or spend money with, or disburse funds to. These are the natural persons who ultimately own or control an entity, or on whose behalf transactions are being conducted – and their identity may not be immediately obvious.

As the first step in due diligence, AEs are required to identify ultimate ownership and control of organisations they work with, and verify this information, to avoid being involved in relationships structured for money laundering or terrorism financing. To carry out “know your customer” checks, you must assess implementing entities’ purpose, economic rationale and integrity framework – including anti-money laundering measures and procedures for countering the financing of terrorism – and identify and verify their beneficial owners.

The primary source of information should be a country’s central beneficial ownership registry. In jurisdictions where such information is not recorded by the authorities, AEs should oblige organisations they work with to disclose their beneficial owners, and should make every effort to verify the information independently. A country’s risk level for misuse of climate funds or for money laundering offers additional information to help determine mitigation strategies and how extensive checks should be – for example, are effective oversight agencies in place? Transparency International recommends that entities should require any company or organisation bidding for public contracts or purchasing property to disclose on whose behalf they are operating, and to be transparent about who is ultimately in control of their organisation, even if it is incorporated in a foreign jurisdiction. This reinforces your message that companies must operate transparently in order to qualify to work with your entity.

Intermediaries and red flags

Corrupt companies and officials often seek the help of financial institutions and professional intermediaries such as corporate service providers, lawyers and accountants, who may knowingly or negligently enable corruption by handling dirty money or setting up anonymous companies for clients. They may also serve as nominee shareholders or directors, keeping the real owner confidential. These entities and professionals are considered “gatekeepers” of the financial sector, occupying a privileged position to prevent and identify suspicious activities and raise any red flags with the authorities.

When conducting due diligence, look out for red flag warning signs, such as overly complicated organisational or project structure, overseas companies or multiple intermediaries, which can make it hard to understand who is really behind an enterprise, undermining accountability. Scrutinise these for risks, for example, interests held by politically exposed persons (PEPs) or connections to companies debarred by multilateral organisations. If your entity or one you are assessing is based in more than one jurisdiction, ensure you have mechanisms to share information on beneficial ownership.

Tip: *Transparency International recommends that entities keep independently verified registers of beneficial owners or ultimate controllers of companies and entities who they partner or disburse funds to, and make these publicly accessible in open data formats. This allows others to also scrutinise ownership, helping expose conflicts of interest and undue influence in climate finance allocation and expenditure.*





Independent, objective oversight

Comprehensive, independent oversight is an essential component of financial integrity, to deter, prevent and detect fraud and wrongdoing. The GCF requires that you appoint an independent audit committee to oversee the work of internal and external auditors in their review of financial statements, control systems and reporting. Internal auditing must provide independent, objective evaluation of an entity's risk management, control and governance processes, based on a documented description of the annual audit planning process that meets international standards. Your internal audit function should share information and coordinate activities with relevant internal and external parties, disseminate findings to senior management, and monitor the response to its recommendations. You should also carry out periodic internal and external quality assessments to review the overall effectiveness of the internal audit functions.

AEs must appoint an external auditor to ensure an independent review of financial statements and internal controls. External audits carried out by a national audit institution must be guaranteed independent and impartial. The external auditor must publicly issue an annual audit opinion on your entity's financial statements, including all financial resources received from the Fund.

Nepal's National Trust for Nature Conservation (NTNC) ensures a two-pronged external audit process, for extra oversight. "NTNC's statutory external audit is typically conducted by Nepal's Office of the Auditor General, but we also use an external accounting firm to conduct annual or semi-annual internal audits, as per our annual audit plan," says Dr. Manish Raj Pandey. "By conducting regular internal and external audits, we can evaluate the efficiency of financial management processes and controls, allowing timely identification and correction of weaknesses or issues."



Comprehensive monitoring and reporting

The GCF's Independent Integrity Unit (IIU) monitors implementation of the Fund's Anti-Money Laundering and Countering the Financing of Terrorism Policy, and supports AEs' own policy implementation. If an entity's staff or consultants encounter suspicious information or red flags indicating money laundering or terrorist financing activities, they are required to immediately and confidentially report this to the IIU. AEs must continuously review and update policies on anti-money laundering and terrorism financing, to address threats and reflect international standards as they evolve.

Tip: Ensure all staff members and consultants are familiar with relevant GCF processes and procedures for compliance with GCF anti-money laundering and countering the financing of terrorism requirements. Provide readily accessible information, regular training updates and newsletter bulletins so that they know how to promptly report to the IIU any red flags, suspicions or occurrences of money laundering or terrorism financing activities.

Ongoing monitoring of how funds are used is also essential for financial integrity. "To promote transparency and comply with GCF requirements, NTNC furnishes clear and accessible information on fund allocation and use, supported by regular financial reporting, ensuring accountability," says Dr. Pandey at Nepal's NTNC. "Capacity-building efforts enhance financial management skills among staff. Regular monitoring and evaluation of financial activities are crucial to guarantee the effective and intended use of funds, including assessing the impact of projects and programmes."

By adhering to these key principles, entities seeking GCF accreditation can enhance their financial integrity and best contribute to effective management of funding and impactful climate action.

Image: GIZ



KEY LESSONS FROM PEERS TO SUPPORT FINANCIAL INTEGRITY

- ▶ **Invest in a robust due diligence process:** Commit time and resources to develop and implement a thorough due diligence process for assessing potential partners or recipients of funds. This should cover financial, legal and risk assessments. The process should be fully documented for scrutiny.
- ▶ **“Know your customer”:** Identify and verify the ultimate beneficial owners of any entity you work with or allocate funds to. This helps protect your entity from being caught in financial arrangements that support malpractice, including money laundering or terrorist financing.
- ▶ **Tone from the top:** Ensure senior management emphasise integrity and transparency in all financial transactions and are fully accountable for the allocation and use of funds.
- ▶ **Ensure effective, independent oversight:** Regularly monitor and evaluate financial activities to ensure funds are used effectively and for their intended purposes, and carry out internal and external audits to provide independent assurance.
- ▶ **Ensure coordination between stakeholders:** Monitor all money transfers, resolving gaps and overlapping mandates between stakeholders, to strengthen coordination and accountability.
- ▶ **Stay updated:** Keep abreast of changes in GCF policies and international standards as they evolve over time. Regularly review and update your financial management practices accordingly, and invest in capacity building for staff and partners to enhance financial management skills and ensure compliance with GCF requirements.

FURTHER INFORMATION AND RESOURCES

- ▶ Green Climate Fund: [Anti-Money Laundering and Countering the Financing of Terrorism Policy](#) specifies the GCF’s requirements for preventing money laundering and terrorism financing, including for Accredited Entities.
- ▶ Green Climate Fund: [Initial Fiduciary Principles and Standards](#) lays out the principles of the Fund’s initial basic fiduciary standards for administrative and financial capacities, and the requirements needed to achieve them.
- ▶ [GCF Independent Integrity Unit information brochure](#) provides an overview of the IIU mandate and the GCF Integrity Policy Framework.
- ▶ Transparency International promotes [integrity in the global financial system](#), including [campaigning for beneficial ownership transparency](#) worldwide, with a dedicated [Climate Governance programme](#) promoting integrity in flows of climate finance.
- ▶ The U4 Anti-Corruption Helpdesk paper [The uses and impact of beneficial ownership information](#) demonstrates how stakeholders can use beneficial ownership information and development practitioners can engage with the beneficial ownership transparency agenda.
- ▶ The Financial Action Task Force (FATF) provides essential recommendations in its [International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation](#). The U4 Helpdesk also provides a useful [introduction to FATE](#) and its recommendations.

This brief is part of a series of **Peer-to-Peer Learning Alliance Integrity Briefs**. To find out more, visit the [Learning Alliance webpage](#).



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