

## Annex IX: Risk appetite statement

### I. Objective

1. The objective of the risk appetite statement is to provide direction to guide and steer the overall level of risk-taking and proactive risk management across GCF operations, while aligning with the objectives outlined in the updated Strategic Plan for the GCF 2024–2027. The risk appetite statement is part of the robust and comprehensive GCF risk management framework (RMF). Specifically, the risk appetite statement:
  - (a) Highlights key risks across various aspects of GCF operations that could compromise the ability of the GCF to achieve its strategic mandate;
  - (b) Describes acceptable risk levels and, where required, steers mitigation of such risks; and
  - (c) Fosters a cohesive and shared understanding of risk tolerance and risk-taking within GCF and among stakeholders, facilitating informed decision-making.
2. The risk appetite statement sets the foundation for further review, revision and development of other policies, guidance and parameters within the RMF, and future policies or reviews of additional policies and frameworks in the GCF policy suite.

### II. Description of risk tolerance levels

3. In addition to zero tolerance for defined behaviours and activities, GCF has three levels of risk tolerance, from low risk tolerance to considerable risk tolerance:
  - (a) “low risk tolerance”: risks accepted when unavoidable for which appropriate mitigants to minimize the likelihood and/or impact will be applied;
  - (b) “moderate risk tolerance”: risks to be carefully managed and mitigated to reduce the likelihood and/or impact; and
  - (c) “considerable risk tolerance”: risks required to be taken to deliver the GCF mandate, that will be managed, monitored and, where practicable, mitigated, and only accepted if compensated through impact.

### III. Risk appetite statement

#### 3.1 Context

4. As the world’s largest dedicated climate fund serving developing countries, GCF faces a dynamic risk landscape, including financial and non-financial risks at the institutional level and within its supported projects, programmes and partners. These risks continue to evolve as the Fund expands in size, sophistication, portfolio and partners, and adopts innovative financial instruments and structures to achieve the objectives of its strategic plans. On the programming side, in order to achieve its strategic mandate of promoting a paradigm shift towards low-emission and climate-resilient development pathways, GCF is prepared to take risks that other investors do not take to support projects and programmes with significant climate impact potential, crowd in other investors, improve project financial viability, and work with partners to reach the most vulnerable, including in fragile and conflict-affected areas.
5. Externally, GCF and its partners navigate an increasingly volatile economic and political risk environment. These realities, coupled with the need to improve access and increase speed

and programming levels to address urgent climate challenges, require a commensurate risk appetite, including for potential reputational impacts. The GCF will adopt a proactive approach to managing and monitoring these risks to maximize climate impacts at the portfolio level.

### 3.2 Overall statement of risk appetite

6. GCF will uphold the highest level of integrity in conducting its operations. It has zero tolerance for a range of behaviours and practices and will promptly respond to allegations or incidences of related violations.

7. GCF seeks to maintain a stable and manageable institutional risk profile enhancing its ability to help ensure the adequacy and predictability of financial resources; maintain a well-balanced portfolio of projects and programmes consistent with a country-driven approach and in response to guidance from the Conference of the Parties to the United Nations Framework Convention on Climate Change and the Conference of the Parties serving as the meeting of the Parties to the Paris Agreement; and operate in a transparent, accountable and efficient manner by implementing Committee of Sponsoring Organizations of the Treadway Commission (COSO) internal control framework.<sup>1</sup>

8. To realize significant impact and promote a paradigm shift to meet its strategic objectives, GCF is willing to accept considerable risks in its programmes and projects in return for impact potential, to be evaluated on a case-by-case basis, recognizing the specifics of each funding proposal. GCF will strive to understand, monitor and manage project, programme, partner and external risks, providing essential support and reasonable assurance to fulfil its mandate and strategic objectives.

9. A cornerstone of the GCF risk management approach is proactive risk management, including risk identification, assessment, appropriate mitigation, monitoring, reporting and appropriate actions to minimize, reduce and respond to risks, both directly and through partners that are implementing GCF projects and programmes.

### 3.3 Zero tolerance behaviours and activities

10. GCF has zero tolerance for Prohibited Practices in Fund-related Activities.<sup>2</sup>

11. GCF has zero tolerance for sexual exploitation, sexual abuse or sexual harassment in Fund-related Activities.<sup>3</sup>

12. GCF has zero tolerance for working with parties and engaging in activities subject to sanctions imposed by the United Nations Security Council.<sup>4</sup>

13. GCF will seek to minimize the risk of occurrence of such behaviours and activities. GCF will promptly respond to allegations or incidences of behaviours and activities for which it has zero tolerance and will take appropriate action.

---

<sup>1</sup> The COSO framework was approved by the Board in decision B.BM-2015/06 as the internal control framework for GCF, to provide reasonable assurance regarding the achievement of objectives relating to operations, reporting and compliance.

<sup>2</sup> As further set out in the GCF Policy on Prohibited Practices adopted in decision B.22/19, as may be amended by the GCF Board from time to time.

<sup>3</sup> As further set out in the GCF Revised Policy on the Prevention and Protection from Sexual Exploitation, Sexual Abuse, and Sexual Harassment in decision B.BM-2021/08, and as set out in Principle IV (k) (“Zero-tolerance of SEAH”) of the GCF Revised Environmental and Social Policy in B.BM-2021/18, as may be amended by the GCF Board from time to time.

<sup>4</sup> As further set out in the GCF Anti-Money Laundering and Countering the Financing of Terrorism Policy and Standards adopted in decisions B.18/10 and B.23/15, as may be amended by the GCF Board from time to time.

## 3.4 Institutional risk

### 3.4.1. Funding contribution uncertainty risk and liquidity risk

14. Predictable funding and sufficient liquidity are essential for GCF to achieve its objectives. GCF has low risk tolerance for funding contribution risk and liquidity risk.
15. GCF will take necessary actions to protect the predictability of its financial resources, including diversifying sources of contributions across a range of contributors and managing cancellations, postponements and other changes in contribution payment schedules to minimize risks associated with asset–liability cash flow mismatches.
16. GCF seeks to maintain sufficient liquidity to preserve its commitment capacity and meet its cash flow obligations. GCF will maintain a liquidity reserve equivalent to its anticipated net funding requirements for the upcoming one (1) year period. Currently, GCF does not use planned project reflows to reduce net funding requirements. The Secretariat will review the net funding requirements and the use of project reflows in consultation with the Risk Management Committee (RMC) in the future once reflows become a more relevant and predictable part of planned inflows.

### 3.4.2. Funds held in trust risk

17. GCF has low risk tolerance for risks related to funds held in trust. GCF will manage its liquid asset portfolio through the Trustee and the applicable investment strategy in accordance with evolving investment policy of GCF. The eligibility criteria for the liquid asset portfolio securities will also be guided in the same manner. GCF will maintain a prudential risk profile, limiting the investment universe of its liquid asset portfolio to investment grade securities with appropriate duration, as specified in the relevant policies, and will refrain from making investments that go against its mandate.

### 3.4.3. Foreign exchange risk

18. GCF faces two (2) primary sources of foreign exchange (FX) risk:
  - (a) Programming-side FX risk: Investments of GCF that implement funding proposals with local currencies are subject to a risk of repayment in holding currencies. GCF maintains a moderate risk tolerance for such risk, providing the Board with a broader set of investment options in line with its mandate and its mission to promote a paradigm shift towards low-emission and climate-resilient development pathways. GCF shall seek to understand, manage and monitor this risk through relevant risk management policies, procedures and systems; and
  - (b) Funding-side FX risk: GCF receives contributions from countries in currencies that may not match the currency of future funding proposals, creating potential currency mismatch challenges. It maintains a low risk tolerance for the funding-side of FX risk. To manage FX risk, contributions received may be converted to holding currencies to minimize mismatch. Any hedging will be in accordance with applicable Board-approved policies and risk management arrangements.

### 3.4.4. Operational risk

19. GCF has low to moderate risk tolerance for operational risks. GCF recognizes that daily operations carried out by its personnel through information systems and operational processes are susceptible to various internal and external risks that may jeopardize day-to-day operations, lead to financial losses, negatively impact the speed of programming delivery and damage its

reputation. Such operational risks include the failure of information systems, human errors, fraud and other internal compliance breaches, and cybersecurity threats.

20. GCF has low risk tolerance for fraud risk, the risk of non-compliance with internal policies and threats against the safety and security of GCF members and alternate members of the Board, Board advisers and GCF personnel in performing their functions for GCF. GCF has moderate risk tolerance for operational risks such as failure of information systems, human errors, information security or digital attacks.

21. GCF implements a proactive risk-based approach to prevent, mitigate and manage these risks through its internal control framework and by maintaining and updating the institutional risk register.

#### 3.4.5. Concentration risk

22. GCF has a moderate risk tolerance for concentration risk. To ensure that GCF optimizes the deployment of its financial resources to achieve its strategic priorities and climate impacts, GCF will maintain a diversified portfolio with respect to the amount of funding allocated to result areas,<sup>5</sup> countries, projects/programmes and accredited entities (AEs). The Secretariat will adopt a proactive approach by monitoring and assessing the Fund's exposure levels (in a nominal amount of cumulative funding approved for ongoing projects/programmes at a Fund level).<sup>6</sup> In addition, GCF will balance its deployment of funding instruments (e.g. grants, equity, loans and guarantees) and monitor the portfolio in accordance with the GCF investment and risk policies and procedures.

#### 3.4.6. Legal risk

23. GCF has moderate risk tolerance for legal risk, which, for the purposes of this section, is the risk of loss, including but not limited to financial loss, penalties, prosecutions, regulatory actions, loss of legal or contractual rights or reputational harm caused by or arising from:

- (a) Legally defective transactions or unenforceable legal agreements;
- (b) Programming in countries in which GCF has not secured privileges and immunities;<sup>7</sup>
- (c) Non-compliance with legal obligations under applicable laws or contracts; or
- (d) Litigation brought against or affecting GCF.

24. GCF will carry out appropriate diligence and monitoring to identify, carefully manage and mitigate legal risks to reduce the likelihood and impact thereof, including, where appropriate, by entering into legal agreements (including, for the avoidance of doubt, agreements to secure privileges and immunities) and incorporating risk mitigants in its legal agreements proportionate to the inherent legal risks. In addition, GCF will exercise its rights under its legal agreements appropriately to achieve its objectives. Notwithstanding paragraph 23(b) above, GCF will not establish a presence in countries that have not recognized its privileges and immunities.

---

<sup>5</sup> The results areas are: energy access and power generation; low-emission transport; building, cities, and industries and appliances; forestry and land use; most vulnerable people and communities; health and well-being, and food and water security; infrastructure and built environment; ecosystem and ecosystem services.

<sup>6</sup> The Secretariat will monitor and report to the Risk Management Committee (RMC) against the following thresholds: 25 per cent of the total committed amount into a single results area, 2.5 per cent of the total committed amount into a single proposal, and 10 per cent of the total committed amount into a single AE. The RMC will review annually whether to include a monitoring threshold for country concentration.

<sup>7</sup> Further information on the consequences of the absence of privileges and immunities is contained in "Thirteenth report of the Green Climate Fund to the Conference of the Parties to the United Nations Framework Convention on Climate Change" (document GCF/B.39/14, pp. 131–133)

## 3.5 Programme risk

### 3.5.1. Policy breaches by partners

25. GCF has low risk tolerance for non-compliance by partners of GCF policies (e.g. prohibited practices, anti-money laundering, environmental and social safeguards, Indigenous Peoples, gender, and monitoring and accountability). GCF will proactively manage and apply appropriate mitigants to minimize such risks. GCF relies extensively on a network of partners, including AEs, for all stages of its operations (i.e. project identification, due diligence, execution, governance and monitoring). GCF has established policies and will enter into legal agreements that set the standards and define the expected actions and responsibilities of AEs, executing entities and other partners. GCF partners are expected to fulfil such obligations.

26. GCF is committed to growing the network of national and regional entities it works with to deliver climate finance in diverse country circumstances, including in fragile or conflict-affected situations. GCF will recognize the contextual risk environment in which its partners operate, and will support AEs, particularly direct access entities (DAEs), through capacity-building to meet best practice standards over time. In addition, GCF will take active adaptive measures during project implementation to manage such risk. GCF will assess and address cases of non-compliance and take appropriate actions, which may include remedial measures and capacity-building support to address capacity constraints, so that the risk of subsequent non-compliance is minimized.

### 3.5.2. Credit and equity investment risk

27. GCF has considerable risk tolerance for credit and equity investment risk in projects and programmes in order to meet its strategic mandate of promoting a paradigm shift towards low-emission and climate-resilient development pathways. GCF will support innovations, utilize a wide range of financial instruments to crowd in additional investors and enhance the financial viability of projects and programmes to meet its strategic mandate. GCF will seek to understand and, where practicable, mitigate the risk, and will balance such risk against the potential climate impacts and opportunities and assess concessionality for informed risk-taking and appropriate risk-sharing with partners. In addition, GCF will proactively manage the associated risk and closely monitor the credit and investment performance of its portfolio in accordance with its investment and credit risk management policies and procedures.

28. GCF has established a required cushion for loan loss reserves equivalent to 20 per cent (in grants) of the face value of the loan contribution provided to GCF by the loan contributors for non-performing loans. The adequacy of the cushion will be reviewed and updated periodically by the Secretariat in consultation with the RMC to ensure the ability of GCF to repay the loan contributions during the programming period.

### 3.5.3. Project and programme implementation risk

29. GCF has considerable risk tolerance for project and programme implementation risk, in order to achieve climate impacts and a paradigm shift. GCF will actively assess and manage this risk across various domains to maximize the likelihood of successful project execution and impact delivery. These domains include project governance, execution, political and macro-economic risks; partners' technical and institutional capabilities and track record in implementing GCF programmes; and community readiness (i.e. awareness, preparation, commitment).

30. GCF will recognize the contextual risk environment in which GCF partners operate and will support AEs, particularly DAEs, to build technical and institutional capabilities over time.

GCF will actively monitor partner performance in project and programme implementation and will take active adaptive measures during project implementation to respond to evolving risks and challenges to maximize the likelihood of successful project execution and impact delivery.

#### **IV. Implementation arrangements**

31. GCF will apply a multi-pronged approach to ensuring the successful implementation of the risk appetite statement, including a strong emphasis on proactive risk identification, assessment and mitigation, which may include:
- (a) A comprehensive communication plan to increase understanding of the risk appetite statement, its key principles and implications for programming and the operation of the institution;
  - (b) Integration of the risk appetite statement into existing processes, updating relevant guidance as needed; and
  - (c) Medium-term efforts to foster a proactive risk culture within GCF and make efforts to promote risk management practices across entities receiving GCF financing, including strengthening the linkages between decision-making and risk management; enhancing staff capabilities through adequate resourcing and training; and promoting open and transparent communication about risks at all levels.
32. The risk appetite statement will also inform revisions to the other components of the GCF RMF and its wider policy suite, ensuring a cohesive and aligned approach to managing risk across the institution.

#### **V. Monitoring and review**

33. GCF will use the updated risk dashboard to monitor aggregate risk levels across GCF. This dashboard will also facilitate identifying deviations from the established risk tolerance levels. Regular reports summarizing these findings will be submitted to the RMC by the Secretariat.
34. GCF will proactively monitor the implementation of the risk appetite statement by tracking its effectiveness in achieving the desired outcomes and delivering the anticipated benefits. If any updates are necessary to ensure continued alignment with the strategy, risk tolerance and evolving operational environment of GCF, the Secretariat will provide recommendations to the RMC.
-