



## TEN GUIDING PRINCIPLES FOR FINANCING COAL RETIREMENT MECHANISMS

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An increasing number of governments and financial institutions recognize the science showing that there is no way to keep 1.5°C alive without shutting down coal power within the next two decades. Yet the emerging coal retirement mechanisms (CRMs)<sup>1</sup> in Asia and Africa have made little progress in turning pledges into funding, and on agreeing how these funds should be spent. We present ten key guiding principles for CRM finance to ensure that these initiatives meet their climate goals while protecting communities and workers.

Coal power generation is the world’s single largest source of greenhouse gas emissions. Even as the world’s existing coal fleet would push the world past the critical 1.5°C limit, the amount of new coal-fired capacity in the pipeline would increase the current fleet by a quarter.<sup>2</sup> Meanwhile renewables are now the fastest growing and cheapest form of power generation almost everywhere in the world.<sup>3</sup> The IEA states that to stay under 1.5°C, in addition to rapidly reducing the use of oil and gas, coal power must be completely phased out in OECD countries by 2030 and the entire world by 2040.<sup>4</sup>

Fortunately, many governments and financial institutions have recognized the urgency of shutting down the world’s coal fleet. Several types of CRMs have been created to address the issue. The Just Energy Transition Partnerships (JETPs), launched at COP26 in Glasgow, have gotten much of the attention, with tens of billions of dollars pledged to coal JETPs in South Africa, Indonesia, and Vietnam. There are also other mechanisms with similar goals,

<sup>1</sup> This document uses "Coal Retirement Mechanism" to refer to any early retirement mechanism for coal whether this would be at an individual or multiple plant/project-level, or a utility- or sector-wide level.

<sup>2</sup> See data from Urgewald, [2023 Global Coal Exit List: Failing the phaseout](#), 19 October 2023

<sup>3</sup> IRENA, [Majority of new renewables undercut cheapest fossil fuels on cost](#), 22 June 2021

<sup>4</sup> IEA, [Net Zero Roadmap: A Global Pathway to Keep the 1.5°C Goal in Reach – 2023 Update](#), p.92, September 2023

such as the Asian Development Bank's Energy Transition Mechanism (ETM), and the World Bank's Climate Investment Funds-Accelerating Coal Transition (CIF-ACT) fund.

Unfortunately, no CRM is yet moving forward with any degree of success.

- South Africa's JETP, the first to be announced, has gotten bogged down in the deep problems of the South African power sector, including an ongoing energy crisis and the severe financial and management problems of its debt-ridden power utility.<sup>5</sup>
- Indonesia's JETP faces a serious credibility problem as the latest policy roadmap for the JETP only proposes to retire two plants totaling 1.7 GW of on-grid coal power. Meanwhile 14.4 GW of "captive" off-grid coal power capacity for minerals processing and other heavy industries is still proposed or under construction.<sup>6</sup>
- In Vietnam, no plants have yet been identified for closure, and the government has imprisoned some of its leading civil society voices on coal.<sup>7</sup>
- In the Philippines, one of the biggest coal developers doubled its shareholding in the first coal project chosen under the CIF-ACT while talks were ongoing. This developer has commissioned two coal plants in the last four years and is planning to construct more – raising serious concerns over the potential of CRMs to reduce coal's share in the national energy mix.<sup>8</sup>

One of the key barriers to the progress of CRMs is that only an insignificant proportion of the tens of billions of dollars pledged by governments and private financial institutions has been made available. Furthermore, it appears that the funders intend for most of the financing to be provided as non-concessional loans, thus raising concerns about CRMs adding to already substantial national debt burdens.<sup>9</sup> Other challenges include the lock-in structure of long-term take-or-pay power purchase agreements (PPAs), and the unwillingness of lenders and investors to take 'haircuts' for their past coal investments.<sup>10</sup>

### Will private finance walk the talk?

The Glasgow Financial Alliance for Net Zero (GFANZ) intends to play a lead role in mobilizing private finance for JETPs. It remains unclear, however, which, if any, GFANZ members might be willing to provide significant finance for closing coal plants at concessional rates.<sup>11</sup>

GFANZ has issued a [draft paper](#) on financing CRMs in the Asia Pacific region. The draft has positive elements, such as recognizing the dangers of "emission leakage" whereby one coal plant is closed but others are operated more often to make up for lost generation, or old plants are closed to shore up government finance for PPAs with new coal plants that are otherwise uneconomic; and the moral hazard issue of CRMs encouraging more coal to be built so that it can benefit from compensation under early closure programs. The draft

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<sup>5</sup> Reuters, [South African utility Eskom pollutes more in bid to keep lights on](#), 27 September 2023

<sup>6</sup> Center for Research on Energy and Clean Air and Global Energy Monitor, [Emerging captive coal power: Dark clouds on Indonesia's clean energy horizon](#), p.3, 20 September 2023

<sup>7</sup> Reuters, [In Vietnam, climate arrests spark calls to halt energy transition deal](#), 20 October 2023

<sup>8</sup> Business World, [Aboitiz firm gets 69% of STEAG State Power](#), 6 June 2023; Department of Energy Philippines, [List of Existing Power Plants \(Grid-Connected\), Luzon Grid](#), 31 August 2023; [List of Existing Power Plants \(Grid-Connected\), Mindanao Grid](#); 31 August 2023; Inquirer.net, [Aboitiz eyes expansion of Cebu coal plant](#), 14 August 2023

<sup>9</sup> See articles by Financial Times, [South Africa warns \\$8.5bn climate package risks fueling debt burden](#), 4 November 2022; and Eco-Business, [JETP in Indonesia: funding solution or energy transition debt trap](#), 17 July 2023

<sup>10</sup> RMI, [Financing the Coal Transition](#), p.13, November 2021

<sup>11</sup> Asia News Network, [Coal phase-out scheme draws minimal JETP funding](#), 14 November 2023

GFANZ paper, however, is overly bullish on the potential of carbon offsets in providing a revenue stream for CRMs, while ignoring the reality that selling carbon offsets from CRMs would negate the climate benefits from retiring coal plants by giving a pass to buyers of offsets to not reduce their own emissions.

GFANZ has [expressed concerns](#) that financial institutions may be dissuaded from financing CRMs as this would increase the institutions' financed emissions – although they have not provided data to show that financed emissions from CRMs would indeed significantly increase total financed emissions for any bank or investor. In addition, major investment banks have lobbied to exclude certain aspects of their underwriting activities from net-zero carbon targets, which potentially derails from decarbonization targets.<sup>12</sup> In any case, this issue can be dealt with by creating a distinct category of "phaseout emissions" – provided that CRMs adhere to the principles articulated here.

### **TEN GUIDING PRINCIPLES FOR CRM FINANCE**

It is vital that we establish universal guiding principles on financing CRMs now while these mechanisms are still in their infancy. Reclaim Finance, together with 11 organizations from Southeast Asia, South Africa, Europe, and North America, believe that CRMs must follow the ten principles listed below:<sup>13</sup>

1. **All phaseouts must align with 1.5°C no- or low-overshoot emission pathways with limited reliance on negative emissions, such as those described by the [International Energy Agency \(IEA\)](#).** The IEA is also clear that all coal power in OECD countries must be retired by 2030, and all unabated coal generation must close by 2040 globally.<sup>14</sup>
2. **All finance for coal expansion, including for new, expanded, or refurbished grid-based power plants, captive plants, mines, and related infrastructure, must stop immediately.** Developers who are still actively planning and building new coal plants or other coal projects should not be eligible for any CRM finance to avoid incentivizing companies to continue expanding coal in the hopes of receiving lucrative payouts from CRMs in the future.<sup>15</sup>
3. **Power generation lost from phasing out coal power plants must be replaced by [sustainable renewables](#), in particular solar and wind power (and related grid upgrades with energy storage), and energy efficiency measures.** In instances where CRM entails the financing of the development of new power capacity, it must be mandated that renewables are the technology of choice. Coal power must not be replaced by high-carbon alternatives such as methane gas or blue hydrogen, as is proposed under Japan's Asia Energy Transition Initiative (AETI). New renewables

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<sup>12</sup> See Financial Times, [Investment banks squabble over carbon footprint of underwriting deals](#), 7 July 2023

<sup>13</sup> These brief principles build on existing more comprehensive principles and guidelines for CRMs and JETPs. See Reclaim Finance and Urgewald, [How to Exit Coal: 10 criteria for coal phase-out plans](#), December 2021; Trend Asia, [Principles and Guidelines for an Equitable and Just Energy Transition in Indonesia](#), 20 October 2022; Germanwatch, [Principles for Just Energy Transition Partnerships in the African context](#), October 2022; and Climate Bonds Initiative, Climate Policy Initiative, and RMI, [Working Paper on Guidelines for Financing a Credible Coal Transition](#), November 2022

<sup>14</sup> IEA, [Net Zero Roadmap: A Global Pathway to Keep the 1.5°C Goal in Reach – 2023 Update](#), p.92, September 2023

<sup>15</sup> The moral hazard issue is addressed in a working paper by Climate Bonds Initiative, Climate Policy Initiative and RMI, [Guidelines for Financing a Credible Coal Transition](#), p.10, 2022

financed under CRMs must replace power lost by closing coal plants, and not be used to power new industrial infrastructure.

4. **Financiers of CRMs must ensure that there is no emissions leakage.** Such leakage could result from increasing production at remaining coal plants to make up for lost generation from early retirements. It must be ensured that the closure of old coal power plants does not benefit newer coal or gas plants by reducing grid over-capacity issues, and in doing so improving the economics of the newer plants; or by shoring up government finances to pay for the PPAs of coal plants that are yet to come on-line. Using CRMs to improve the viability of recent coal investments will only hinder the clean energy transition.
5. **Coal plant closures must not be delayed with the future promise of retrofitting with technologies to supposedly lower their emissions.** Such technologies include efficiency upgrades; repurposing for co-firing with ammonia, hydrogen, or biomass; or carbon capture and storage.
6. **Donors must provide financing on concessional terms, and private financial institutions and project owners must treat CRMs as vehicles for living up to their climate responsibilities, not as opportunities for gaining public sector-guaranteed bailouts.** Where public financing is used for CRMs, there must be standards in place to ensure a measurable reduction in the operating lifespan of coal power plants. Ideally, CRMs would reduce the lifespan of a coal power plant by at least 10 years. For independent power producers, the end of a plant's operating lifespan should be assumed to be the end date of its PPA.
7. **Where CRMs entail the development of new renewable power capacity, financing must be provided mainly through grants for government- and community-owned decentralized systems, and through concessional loans to private companies.** This ensures that developing nations receive the financing owed to them to enable their energy transition without exacerbating their existing debt burden.
8. **Tradeable carbon offsets must not be promoted or used to fund CRMs.** Raising funds from tradeable offsets would reduce and potentially negate the climate benefits of closing coal plants. A mass of evidence from the past two decades of offsetting shows that the industry is rife with cheating.<sup>16</sup> Calculations of the volume of carbon offsets generated from CRMs would be based upon subjective estimates of what emissions would be if coal plants had not been retired. This is the type of counterfactual calculation that experience shows is wide open to gaming.
9. **CRM processes must be transparent and accountable to encourage market competition and to avoid corruption.** The selection for the early retirement of coal plants must take place through transparent processes, such as auctions, where companies can place bids to avoid over-priced compensation packages for plant

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<sup>16</sup> See a long and growing list of academic/analyst reports and media exposés dating back over two decades. Key articles published in 2023 include Guardian, [Revealed: more than 90% of rainforest carbon offsets by biggest certifier are worthless, analysis shows](#), 18 January 2023; [Airlines want you to buy carbon offsets. Experts say they're a 'scam'](#), Washington Post, 17 April 2023; A Chapman and D. Masie, [Are carbon offsets all they're cracked up to be? We tracked one from Kenya to England to find out](#), vox.com, 3 August 2023; [Error Log: Exposing the methodological failures of REDD+ forestry projects](#), Carbon Market Watch, September 2023; Carbon Brief, [Analysis: How some of the world's largest companies rely on carbon offsets to 'reach net-zero'](#), 27 September, 2023; H. Blake, [The Great Cash-For-Carbon Hustle](#), New Yorker, 16 October, 2023.

owners.<sup>17</sup> This simultaneously increases competition and reduces the risk of corruption.<sup>18</sup> Additionally, electricity users, especially residential consumers, must be shielded from any additional costs resulting from shortening the life span of coal projects.

10. **CRMs must ensure the remediation of social and environmental harms caused by projects to be retired.** CRMs should not in any way absolve coal companies of their responsibility for any violations of laws or regulations. Funding must be made available to retrain displaced workers and provide potential employment opportunities. Local communities, governments, and relevant stakeholders should also be a part of the consultative decision-making process, and the perspectives of local communities must be freely expressed. There must also be accessible and widely publicized grievance and accountability mechanisms whereby CRM authorities can be held responsible for their commitments.<sup>19</sup>

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<sup>17</sup> S Tiedemann & F Müller-Hansen. [Auctions to phaseout coal power: Lessons learned from Germany](#). March 2023.

<sup>18</sup> Policies such as coal price caps that inhibit the competitiveness of renewables, should be removed. See IISD, [Indonesia's Coal Price Cap: A barrier to renewable energy deployment](#), 5 May 2019

<sup>19</sup> See as guiding principles: [OECD Due Diligence Guidance for Responsible Business Conduct](#), 31 May 2018