

POLICY BRIEF

Building on Momentum: Recommendations from the GSI for Fossil Fuel Subsidy Reform at the G20

June 2016

Key Messages:

1. **Strength in numbers.** Fossil fuel subsidy reform can be challenging. Joining an international peer review process can increase transparency, provide an opportunity to share experiences and insights, and strengthen bilateral relations between peer review partners.
2. **Fix a date for action.** An international commitment, including an ambitious timetable for action, elevates the level of discussion and helps address domestic political economy challenges.

Progress on Voluntary Peer Review

Both Asia-Pacific Economic Cooperation (APEC) and the G20 have established peer review processes to help members meet their commitments to phase out inefficient fossil fuel subsidies that promote wasteful consumption. The first G20 peer review partnership (between the United States and China) is due to publish details of its findings. Within the G-20 and APEC, China, Chinese-Taipei, Germany, Mexico, New Zealand, Peru, the Philippines, the United States and Vietnam have all agreed to undergo peer review in order to increase transparency around domestic fossil fuel subsidies. Many countries have also undergone regular self-reviews of fossil fuel subsidies.

Before the G20 peer review process started, APEC countries explored the road ahead. In 2013, APEC leaders agreed to establish an APEC Voluntary Peer Review (VPR) process on the reform of inefficient fossil fuel subsidies. Over the course of 2014 and 2015, peer reviews were published for Peru and New Zealand. A further review for the Philippines has been conducted.

Countries can sometimes be hesitant to submit themselves to reviews that might result in negative feedback from peers or civil society, particularly when strong differences in viewpoint are already known to exist in some areas. The G20 and APEC peer review processes have been developed to allow each country under review wide freedom to define how the review is conducted and with which peer review country



partners. This aims to ensure that discussions can take place with respect to policies that all parties agree could fit the definition of “inefficient” or promoting “wasteful consumption.” Such an approach is also a valuable opportunity for national governments to articulate their views on which subsidies should be reviewed with respect to these criteria, contributing to public debate in this area.

IISD-GSI encourages countries to take a broad approach to reviewing subsidies—this ensures that no inefficient or wasteful policy will inadvertently be overlooked, as well as maximizing the information that can be used to inform public discussion on energy subsidies. Further, IISD-GSI encourages all G20 and APEC members to strive for increased transparency around fossil fuel subsidies and to volunteer for the next round of peer review commencing in 2017. Within the G20, the United States, China, Germany and Mexico deserve praise for having volunteered to rounds one and two of the peer review process. Who will be next?

Experience of Peer Review in APEC and the G20

APEC’s reviews have been conducted by experts from other APEC economies and relevant institutions with expertise in energy issues, fossil fuels, finance and economics. The decision of whether a subsidy should be deemed “inefficient” was determined as an output of the peer review process led by each national government.

As part of New Zealand’s peer review, a six-person panel was established. It included five country experts from China, Indonesia, the Philippines, Thailand, and the United States along with one expert from the OECD. The review was conducted according to APEC’s voluntary fossil fuel subsidy reform peer review mechanism and covered eight measures or policies (including support to a state-owned enterprise, production tax exemptions and funding). The peer review panelists were selected from economies who had expressed an interest in engaging in their own peer review process (either through the G20 or APEC) in order to build further support for—and comfort with—the peer review process. An OECD representative was included due to the OECD’s work on government support to fossil fuels. The peer review panel concluded that none of these measures were inefficient subsidies that resulted in wasteful consumption. A number of specific recommendations were made to help ensure that subsidies continue to be monitored, reviewed and reformed where necessary.¹

Peru selected three policies for review: a VAT exemption for the Amazon region, the Fuel Stabilization Fund and the Social Inclusion Fund. A peer review panel was established with representatives from Indonesia, Cambodia, New Zealand and the United States. The review focused on the effectiveness of the subsidies. The review concluded that the VAT exemption and the Stabilization Fund were not effective and should be removed in the long term. The Energy Fund for Social Inclusion was considered beneficial to the recipients and the panel suggested that it should be considered for expansion.²

China and the United States will soon present a peer review of each other’s fossil fuel subsidies (with panels including experts from the OECD and IMF) based on a process proposed by a G20 working group. The process is designed to evaluate fossil fuel subsidies and identify inefficient ones that countries are proposing to phase out under G20 implementation strategies, in addition to other measures as agreed within each peer review group. Peer review groups are also free to decide how the findings of the review will be disseminated.

¹ Asia-Pacific Economic Cooperation (APEC). (2015). Peer Review on Fossil Fuel Subsidy Reforms in New Zealand (Final Report). Retrieved from <http://www.mbie.govt.nz/info-services/sectors-industries/energy/international-relationships/pdf-document-library/peer-review-fossil-fuel-subsidy-reforms-nz.pdf>

² Asia-Pacific Economic Cooperation (APEC). (2015). Peer Review on Fossil Fuel Subsidy Reforms in Peru (Final report). Retrieved from http://www.ewg.apec.org/documents/Peru_peer_review_of_fossil_fuel_subsidy_reforms_Nov102014_FINAL.pdf



International Momentum Building Behind Fossil Fuel Subsidy Reform

At COP21 in Paris, John Key, the Prime Minister of New Zealand, presented an international Communiqué endorsed by 40 countries (Box 1), including Canada, Chile, France, Germany, Italy, Malaysia, Mexico, New Zealand, Peru, the Philippines, the United Kingdom and the United States, (from the G20 and APEC), associations representing 91,000 businesses and investors, as well as NGOs and international organizations. The success of the Communiqué has been driven by the Friends of Fossil Fuel Subsidy Reform, an informal group of nine non-G20 countries³ working to build political consensus on the importance of fossil fuel subsidy reform.

In May 2016, G-7 countries “committed to phasing out inefficient fossil fuel subsidies that encourage wasteful consumption, and encourage all countries to do so by 2025,” a significant statement leading up the G20 Energy Ministerial Meeting in June.

Box 1: The Fossil Fuel Subsidy Reform Communiqué

The Friends of Fossil Fuel Subsidy Reform launched the Fossil Fuel Subsidy Reform Communiqué in April last year. The Communiqué has since received considerable support from more than 40 countries and thousands of businesses. It was presented by World Leaders to the UNFCCC at COP 21 in Paris, to call for accelerated efforts to phase out subsidies to fossil fuels as a major contribution to climate change mitigation.

The Communiqué,* which remains open for further endorsements, encourages the international community to advance fossil fuel subsidy reform through three principles.

- Increased transparency around fossil fuel subsidies,
- Ambitious reform, and
- Targeted support to ensure reforms are implemented in a manner that safeguards the poorest.

The Friends are supporting the following language (or variations of) for adoption by G20 countries in relevant G20 statements (e.g., the June Energy Ministers’ Communiqué) in 2016: “We will promote efficient energy use supported by fiscal policies and public finance practices consistent with our shared climate objectives. Notably, G20 countries commit to phase out inefficient fossil fuel subsidies that encourage wasteful consumption by 2025, recognizing the need to provide targeted support to the poorest.”

*The Communiqué (along with more information about country endorsements) is available at www.fffisr.org.

In July 2015, the issue of fossil fuel subsidy reform was included within the Addis Ababa Action Agenda, namely “to rationalize inefficient fossil-fuel subsidies that encourage wasteful consumption.” In September 2015 the issue was included within the Sustainable Development Goals as part of Goal 12 on sustainable consumption and production patterns as a Means of Implementation, again to “rationalize inefficient fossil-fuel subsidies that encourage wasteful consumption.” More recently, in a statement delivered to G20 Finance Ministers ahead of the Energy Ministerial Meeting in June, more than 200 civil society organizations (CSOs) urged G20 governments to take action on fossil fuel subsidy reform (see Box 2).

Growing momentum on the issue is demonstrated through country and business endorsements of the Communiqué, the commitment from the G-7 to phase out fossil fuel subsidies by 2025. The request from CSOs for the G20 to commit to phase out by the earlier date of 2020 indicates broader social momentum from the bottom up. Overall, three principles are emerging to convert high-level commitments into actions on the ground:

1. Communication and Transparency about the merits of subsidy policies and reform timetables, including through engagement and communication with country peers (and more broadly with general public and civil society stakeholders) to ensure a smooth, inclusive, bottom-up approach to reform.
2. Ambition in the scope and timeframe for implementing reforms.
3. Targeted support to ensure reforms are implemented in a manner that safeguards the poorest.

³ Friends countries are Costa Rica, Ethiopia, New Zealand, Norway, Sweden, Switzerland, Denmark, Finland and Uruguay.



Box 2: Civil Society Organization Statement

A letter signed by more than 200 CSOs from over 30 countries urges G20 governments to work to a deadline of 2020 for the phase out of fossil fuel subsidies and for an end to public finance for fossil fuels at the 2016 G20 Summit. The letter requests that the G20:

- Sets a clear timeline for the full and equitable phase-out by all G20 members of all fossil fuel subsidies by 2020, starting with the elimination of all subsidies for fossil fuel exploration and coal production.
- Sets a clear timeline for the phase-out of domestic and international public finance for oil, gas and coal production by 2020, except in extreme cases where there is clearly no other viable option for increasing energy access to the poor.
- Commits all G20 members to be fully transparent from 2017 onwards about all fossil fuel subsidies in a consistent format that is publicly available on an annual basis. The OECD inventory should be strengthened and expanded to include all G20 countries (based on the current OECD model for tracking agricultural subsidies). The G20 should simultaneously increase transparency of reporting on investment in and finance for fossil fuel production by G20 majority publicly owned financial institutions and state-owned enterprises.

The letter proposes the following wording to the G20:

- *We reinforce our commitment to phase out and rationalize fossil fuel subsidies by 2020, recognizing the need to support the poor, and supported by transparent and publicly available annual reporting. Fossil fuel subsidies encourage wasteful consumption, reduce our energy security, impede investment in clean energy sources and undermine efforts to deal with the threat of climate change.*
- *We commit to strengthening green and low-carbon policies and regulations with a view to ending public investment in oil, gas and coal projects both domestically and internationally by 2020, starting with the elimination of public finance for fossil fuel exploration and coal, supported by transparent and publicly available annual reporting.*

Communication and Transparency

One of the main reasons that subsidies to fossil fuels persist is that stakeholders (including the public) are not aware of their existence, their cost and other impacts, and who benefits from them. This is also the case in many G20 countries. Enhancing transparency through regular measurement and reporting is a prerequisite for open and informed debate. Where subsidies are openly discussed and debated, inefficient and wasteful policies are more likely to be recognized as such and eventually phased out.

While there is certainly a role for analysis from international and civil society organizations, government-led subsidy analysis and evaluation carries a special weight in public discourse. For many countries, it is hard for the public to even find basic data on subsidy expenditure. The voluntary peer review processes can shine a powerful light on subsidies, providing official information that can feed into national debates.

Ambition

Countries should be ambitious in terms of both the timeframe and the scope of reform.

A key opportunity for G20 members to show ambition in 2016 is to outline a specific timescale within which the commitment to “rationalize and phase out over the medium term inefficient fossil fuel subsidies that encourage wasteful consumption” will be met. Since 2009, the G20 commitment has been targeting subsidy reform over the “medium term.” The “medium term,” however, has yet to be defined. Now is the time.

Once a deadline is defined, G20 countries will need to consider criteria for the measuring of and reporting on subsidies which is a prerequisite for tracking their elimination. Likewise, it will be necessary to consider what kind of institutional setup, resources and national planning would be needed to support this arrangement.



Targeted support

The peer review process does not simply identify subsidies that are inefficient or that promote wasteful consumption. A key aspect of the process is reviewing the effectiveness and efficiency of subsidies, establishing their objectives and analyzing their performance against these stated objectives. As an example, in many cases the goal of subsidies is to provide energy access to the poorest, while in reality most of the benefits are often captured by the richest. The peer review process offers a valuable opportunity to evaluate whether subsidies are effectively targeted and to promote policies that are of greatest benefit to the intended recipients.

IISD-GSI calls on policy-makers to apply these principles to the discussions of fossil fuel subsidy reform within the G20. As one of the first international bodies to commit to phasing out “inefficient” subsidies that promote “wasteful consumption,” the G20 has always been a leader in this field. In 2016 there is an opportunity to make significant progress against all of these principles.

Recent Progress on Fossil Fuel Subsidy Reform Internationally

Fossil fuel subsidy reform is no longer a fringe issue. It has entered the mainstream. Over the year 2015/16:

- The IEA’s World Energy Outlook listed the phase out of fossil fuel subsidies as a recommendation if the world is to achieve its target of limiting global warming to 2 degrees.⁴
- The IMF stated that fossil fuel subsidy removal and appropriate taxation would generate “very substantial” gains for the environment, revenue collection and welfare, and that it should therefore begin immediately.⁵
- The updated OECD support to fossil fuel inventory⁶, stating that support to fossil fuels undermines global efforts to mitigate climate change and aggravates local pollution, causing further damage to human health and the environment.

Few issues generate such a high level of agreement that immediate action is required.

Many recent reform efforts have been driven by economic opportunism, triggered by low international oil prices. But countries also continue to recognize the adverse role of subsidies, particularly in terms of their opportunity costs—the spending that they take away from investments in people and economies by constraining budgets in areas as diverse as health, education and infrastructure. It is also clear that subsidies to oil, gas and coal contribute to CO₂ emissions. IEA estimates a 10 per cent reduction in energy sector emissions by 2030 from accelerating the partial phase-out of subsidies to fossil fuel consumption.⁷

A global review of recent efforts to reduce fossil fuel subsidies shows that more than 25 countries have implemented some kind of subsidy reform since 2014. Although some efforts are more ambitious than others, it underlines the fact that times are changing.

Another important development is the shift in attitudes to fossil fuel subsidy reform among many oil exporting countries. Recently, countries such as Saudi Arabia, the United Arab Emirates and Venezuela have raised fossil fuel prices to consumers in order to bring in revenue and balance budgets. The map below provides an overview of some of the countries that have implemented some kind of subsidy reform since 2014.

⁴ International Energy Agency (IEA). (2015). Energy and climate. Paris: IEA/OECD. IEA. (2015b). World energy outlook 2015. Paris: IEA/OECD.

⁵ Coady, D., Parry, I., Sears, L., & Shang, B. 2015. How large are global energy subsidies? (IMF Working Paper 15/105). IMF. Retrieved from <https://www.imf.org/external/pubs/ft/wp/2015/wp15105.pdf>

⁶ Organisation for Economic Co-operation and Development (OECD). (2015). OECD Companion to the Inventory of Support Measures for Fossil Fuels 2015. Paris: OECD Publishing. DOI: <http://dx.doi.org/10.1787/9789264239616-en>

⁷ International Energy Agency (IEA). (2015a). Energy and climate. Paris: IEA/OECD.

MANY COUNTRIES HAVE REFORMED THEIR FOSSIL-FUEL SUBSIDIES SINCE 2014.



Figure 1: Countries that have undergone some form of fossil fuel subsidy reform since 2014

Source: IISD, 2015 based on IEA, WEO 2014 and 2015 and GIZ.

Recommendations

1. Undertake peer review of domestic fossil fuel subsidies. Peer review has the potential to catalyze the reform of inefficient subsidies that promote wasteful consumption of fossil fuels.
2. Adopt an ambitious timeline for G20 countries to phase out inefficient fossil fuel subsidies.
3. Make subsidies to fossil fuels transparent, ambitious in their reform, and provide targeted support to mitigate impacts on the poorest.

Links and Further Resources

See website www.fffsr.org to contact the Friends of Fossil Fuel Subsidy Reform.

GSI: rbridle@iisd.org

The following data sets are available on fossil fuel subsidy figures:

GSI: <http://www.iisd.org/gsi/interactive-maps>

IEA: <http://www.worldenergyoutlook.org/resources/energysubsidies/fossilfuelsubsidydatabase/>

IMF: <http://www.imf.org/external/pubs/ft/survey/so/2015/NEW070215A.htm>

OECD: <http://www.oecd.org/site/tadffss/data/>

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Global Subsidies Initiative (GSI)

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