Technical expert group on fossil fuel subsidy indicator for SDG12c

Rome, 29th September 2017

Opening Remarks and G7/G20 updates on Fossil Fuel Subsidies

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Rome, 29th September 2017

Environmental Fiscal Reform and Sustainable Development

- 50. We recognize and support effort by G7 and other countries interested in examining and removing incentives, particularly inefficient **fossil fuel subsidies, not coherent with sustainability goals.**
- 51. We recognize the benefits of **monitoring progress in the phasing out of incentives**, including subsidies, not coherent with the sustainability goals, such as inefficient fossil fuel subsidies which encourage wasteful consumption and we support existing initiatives underway such as the **G20 voluntary peer review process**.

EFR and SD (2)

- 52.We take note of the **OECD work** on these issues, and we recognize that OECD is considering further work for improving understanding of incentives, including subsidies.
- 53.We support G7 and all countries interested in exploring approaches to better **align fiscal systems with environmental goals.** In particular we intend to contribute to the implementation of the **commitment of our Heads of State and Government adopted in Ise-Shima in 2016** for the elimination of inefficient fossil fuel subsidies that encourage wasteful consumption **by 2025**.
- 54. Furthermore, we consider the **need to exchange views and information**, to better understand the impact of fiscal policies and measures on the achievement of our sustainability goals.

G7 Italian Environment Presidency

OECD: EFR

OECD: Employment & Green Growth

UNEP: Sust. Finance for SMEs

OECD: Phasing out EHSs

WRI: Financing the Energy Transition

UNEP: Financial Centres for Sustainability

G7 Preparatory Meetings and Side Events

- Mobilising G7 Financial Centres for Sustainability (Milan, 23-24 February 2017)
- Environmentally Harmful Subsidies (EHS) and Environmental Fiscal Reforms (EFRs) (Rome, 14-15 March 2017)
- Multilateral Development Banks supporting the implementation of the Paris Agreement and the Agenda 2030 (Rome, 28-29 March 2017)
- Green Finance for Small and Medium Enterprises (SMEs) (Venice, 5-6 April 2017)
- Mainstreaming the work of the Regional Sea Programmes towards the better implementation of the G7 Action Plan and the achievement of the global commitments on marine litter (Rome, 20-21 April 2017)
- Universities for Sustainable Development (Bologna, 11th June 2017)
- Firms for Sustainable Development (Bologna, 11th June 2017)
- Carbon Market Platform (Rome, 27-28 September 2017)
- Fossil Fuel Subsidies indicator UNEP SDG12c (Rome, 29 September 2017)
- Article 6 Informal Forum (Rome, 29-30 September 2017)
- Carbon Market Ministerial Declaration (Rome, 1 October 2017)
- Resource Efficiency Alliance (Rome, 29-30 November 2017)

G7 Environment 2017 topics

- UN 2030 Agenda for Sustainable Development and SDGs
- Climate Change
- Resource Efficiency, Circular Economy, 3Rs, Sustainable Materials Management
- Sustainable Finance – Financial Centres - SMEs
- MDBs for the implementation of the Paris Agreement and 2030 Agenda
- Environmental Fiscal Reform and Environmentally Harmful Subsidies
- Marine Litter
- Information Centre for Climate – Environment Cooperation in Africa
- Universities for Sustainable Development
- Firms for Sustainable Development

INEFFICIENT

FOSSIL FUEL SUBSIDIES

THAT ENCOURAGE WASTEFUL CONSUMPTION

INEFFICIENT ?
Economic ? Environmental ? Social ?
descriptive…

FOSSIL FUEL SUBSIDIES

THAT ENCOURAGE WASTEFUL CONSUMPTION
and production ?
descriptive…

G20 Communiqué

14. We reaffirm our commitment to rationalise and **phase out**, over the medium term, inefficient **fossil fuel subsidies** that encourage wasteful consumption, recognising the need to support the poor. Furthermore, we encourage all G20 countries which have not yet done so, to **initiate as soon as feasible a peer review** of inefficient fossil fuel subsidies that encourage wasteful consumption.

G20 Hamburg Climate and Energy Action Plan for Growth

F.2. Inefficient fossil fuel subsidies (IFFS) that encourage wasteful consumption **distort energy markets**, **impede investment in clean energy sources, place a strain on public budgets, and incentivise unsustainable infrastructure investments**. Providing those in need with essential energy services, including the use of targeted cash transfers and other appropriate mechanisms, however, is still important. The **US -Chinese peer review** on IFFS was concluded, the **German - Mexican peer review** is ongoing and **Indonesia and Italy** have announced the continuation of their respective voluntary processes.

1st Catalogue on Environmentally Harmful and Friendly Subsidies in Italy

- 131 measures for 41 billion €;
- 5 categories (Agriculture, Energy, Transport, VAT, Other);
- 75 tax expenditures and 56 direct subsidies;
- about 22 billion € tax expenditures and about 19 billion € direct subsidies;
- 16,2 billion € EHSs, 15,7 billion € EFS;
- 12,4 billion € FFSs

Definition of subsidy

A subsidy is…

…a **transfer** of money from the State to a private body

(WTO)

…a State action providing an **advantage** in terms of revenue (income or minor cost)

(OECD)

…a **difference** between the observed priceand the marginal social cost of production, meaning the cost that internalizes the impact to society

(IMF)

In our catalogue:

A subsidy is…

…a measure that keeps prices for consumers below market levels, or prices for producers above market levels, or that reduces costs for producers and consumers through direct or indirect support

(Source: OECD)

EFS
(Environmentally Friendly Subsidies)

EHS
(Environmentally Harmful Subsidies)

Subsidies' classification

Description	*Classification*	
Direct transfers of funds	On-budget	Direct subsidies
Potential direct transfers of funds		
Foregone revenues	Off-budget	Indirect subsidies (Tax expenditures, exemption, tax credit, etc.)
Regulatory support mechanisms		
Tax exemptions and rebates		
Selective exemptions of government standards		
Implicit income transfers resulting from a lack of full cost pricing		

Estimate of EHS (fossil fuels) in the world

The goal of EHSs identification is to remove or, at least, reform them in order to assure an efficient use of resources.
Their removal may allow for example the reduction of income and corporate taxes.

Some estimates:

- OECD: 160-200 billion $/year for the years 2010-2014 for fossil fuels (40 Countries);
- IMF: 492 billion $ in 2011 for fossil fuels (150 Countries);
- IEA: in 2014, 493 billions $ for fossil fuels (40 Countries).

National experiences (1)

UK

2013➔ The report of the Parliament on «energy subsidies in UK»
total energy subsidies: 12,7 billions of GBP

Ireland

2010➔ EEA Study on the potential reform of environmental taxation:
up to € 5 billions of extra revenue in 2015 (+ € 1 billions for EHS removal)

France

2012➔ "Sainteny report" identifies EHS linked to the biodiversity
(estimate: € 3 billions in 2010)

Germany

2007➔reform for a phasing out of coal subsidies within 2018
2014➔ EHS report: € 52 billions in 2010 (included guarantee schemes and implicit subsidies)

National experiences (2)

Portugal

1995-2010➔ environmental taxation: from 11,5% to <5% of total fiscal revenue

2010➔ EEA Study on potential reform of environmental taxation:

In 2016, environmental taxation + € 2,2 bl (+ € 0,2 bl from additional VAT + € 0,7 bl from EHS removal)

Mexico

2014➔ Starting of energy reform and introduction of a carbon tax on fuels (except natural gas and kerosene for aviation)

2016 ➔ Removal of fuel subsidies through the introduction of fixed excise tax on fuel for transport

USA

2016➔ First National Report on fossil fuels (G20): 17 inefficient fossil fuel subsidies worth US$ 8,2 bl/yr

China

2016➔ First National Report on fossil fuels (G20): 9 inefficient fossil fuel subsidies worth US$ 14,5 bl/yr

Breakdown of subsidies by categories (n°)

Breakdown of subsidies by categories (€)

Breakdown of subsidy by types (n°)

Breakdown of subsidy by types (€)

EHS per Categories (€)

Energy:
Tax expenditures = ca. € 11.2 bn (97%)
Direct Subsidies = ca. € 310 mn (3%)

VAT:
Tax expenditures = ca. € 3.5 bn

EHS Energy (€ bn)

- **VAT**: Tax Expenditures = ca. € 3.5 bn (100%)

Main results of the Catalogue

Subsidies / Categories	EHS	EFS	ENS	Uncertain	Total (€ mn.)	Total (%)
Agriculture	154	2.231		4.068	6.453	15,7%
Energy	11.550	12.145			23.695	57,6%
Transport	202	200		65	468	1,1%
Other	700	1.079	3.538	1.634	6.950	16,9%
VAT	3.561	25			3.586	8,7%
Total (€ mn)	16.167	15.679	3.538	5.767	41.151	100,0%
Total (%)	**39,3%**	**38,1%**	**8,6%**	**14,0%**	**100,0%**	

Ca. € 41 billion of Subsidies: Tax Expenditures (ca. € 22 billion) and Direct Subsidies (ca. € 19 billion).

Tax Expenditures 71% EHS
Direct Subsidies 76% EFS

The case the different fiscal treatment excise gasoline / diesel

- 2015 gasoline excise € 728.4 per 1.000 liters
- 2015 diesel excise € 617.4 per 1.000 liters

- The difference in excise tax relative to diesel fuel is not justified by the scientific literature and contrasts with the European legislation on emission standards.

What is still missing in the Catalogue….(1)

- **The main expenditure categories not included in this first edition:**

1. Structural funds linked to National Operational Programmes (PON) and Regional Operational Programmes (POR);

2. Direct subsidies managed by the Mninistry for Economic development, included those managed through regional authorities;
3. Direct subsidies autonomously provided by regional authorities.

What is still missing in the Catalogue…(2)

- **Other subsidies that are not considered in this edition...**

  - The new tax expenditure schemes identified by the Commission on tax erosion (so-called Marè Commission)

  - Implicit subsidies that could be assessed through external costs methods, for example

    - ✓ tax breaks on royalties;
    - ✓ concession fees on natural resources that do not cover the external costs (related to the unsustainable use of natural resources).

What is still missing in the Catalogue…(3)

→ **Other subsidies not considered in this edition…**

- Subsidies provided through fees on public services (electricity, natural gas, drinking water), due to a debate on their inclusion and quantification;
- Breaks on «general system costs» (electricity bill subsidies for renewables and energy efficiency) provided to companies with high energy consumption levels (as defined by article 2 of Decree of 5th April 2013);
- Crossed subsidies for the coverage of «general system costs» in electricity bill, that are presently included in the tariff systems for domestic and non domestic consumption categories.

Environmental concerns

- The Community legislation on emissions (euro standard limits) allows higher levels of emissions for diesel vehicles.

	NOx (mg/km)		PM (mg/km)	
	Gasoline	Diesel	Gasoline	Diesel
Euro 0	-	-	-	-
Euro I	-	-	-	140
Euro II	-	-	-	80
Euro III	150	500	-	50
Euro IV	80	250	-	25
Euro V	60	180	5	5
Euro VI	60	80	5	5

The computation of the difference in excise tax

	Excise 2015	Excise 2015 (Energy content)
	Euro/1000 liters	Euro/GJ
Petrol	728,4	22,35
Diesel	617,4	17,30

- The raw comparison considering the average excise in 2015 displays a 15% difference.
- A more correct approach, that is based on the energy content of fuels (see e.g. the 2011 Proposal for the Directive on energy taxation), displays a higher difference (23%).

The potential additional revenue due to excise alignment

Fuel	Consumption 2015 (tons)	Revenue for current rates (million EUR)	Consumption 2015 (GJ)	Potential revenue with diesel fuel tax rate equal to the gasoline (22,35 EUR / GJ) (million EUR)	Potential additional revenue (million EUR)
Petrol	7.822.000	7.692	344.168.000	7.692	-
Diesel	23.249.000	17.009	983.432.700	21.978	4.969
Totale	**31.071.000**	**24.701**	**1.327.600.700**	**29.670**	**4.969**

- The total revenue from excise on diesel fuel, without accounting for the tax expenditures on diesel recognized to road transport, would rise from about € 17 to € 22 billion in 2015, with a foregone revenue around € 5 billion.

How would the alignment look like

- In the current regulatory framework, the relative excise tax of diesel fuel should be € 757 euro per 1.000 liters (+ € 139,6 per 1.000 liters).
- Assumptions: we assume constant consumption with no change in consumers' behavior.
- Including VAT, we would have an additional € 1 billion foregone revenue, totaling € 6 billion.