Reforming Fossil Fuel Subsidies to Mobilize Climate Finance

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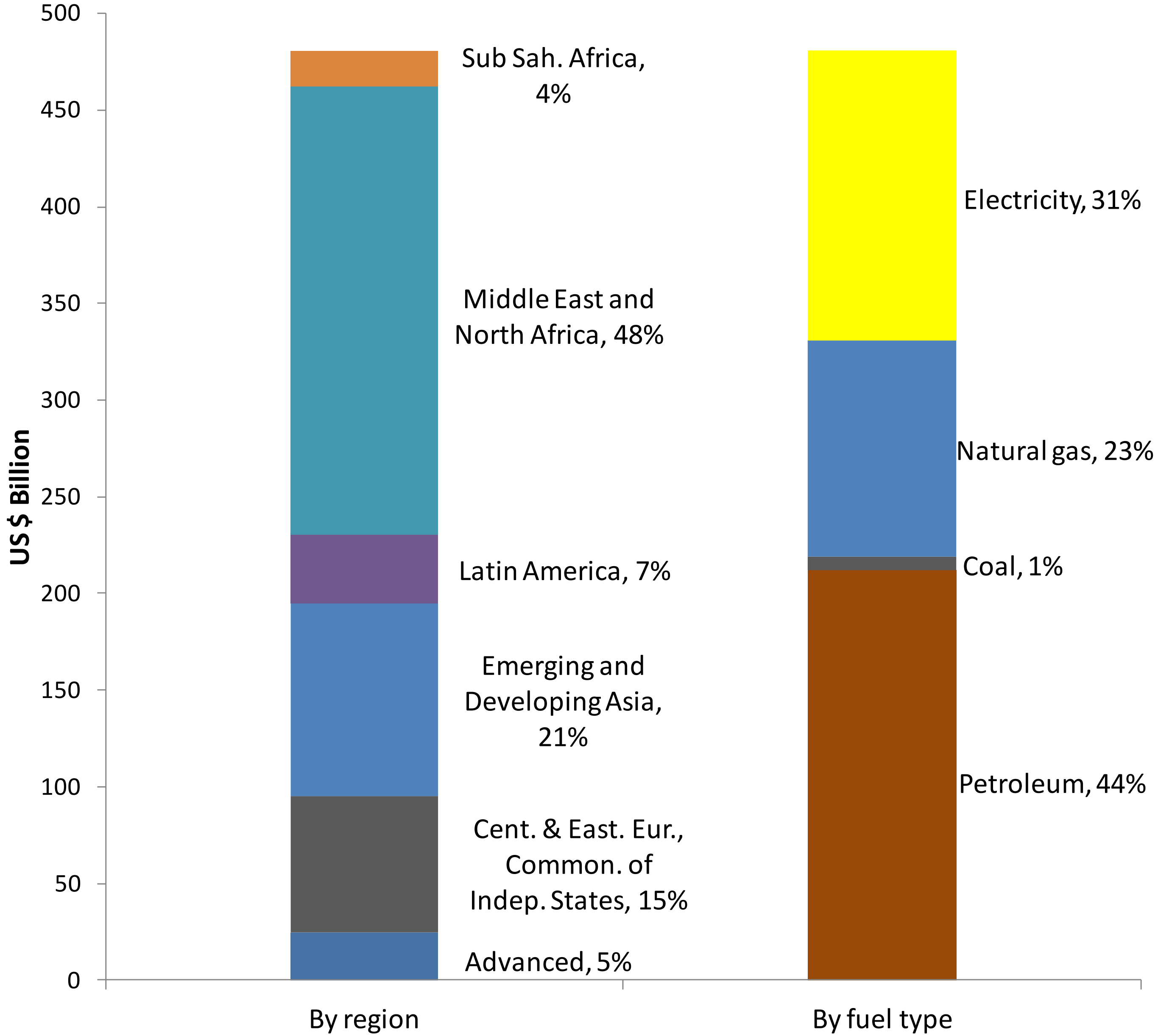
Plan of talk

- Fossil fuel subsidies deter climate finance
- Issues
  - definition and size of subsidies
  - how to move forward

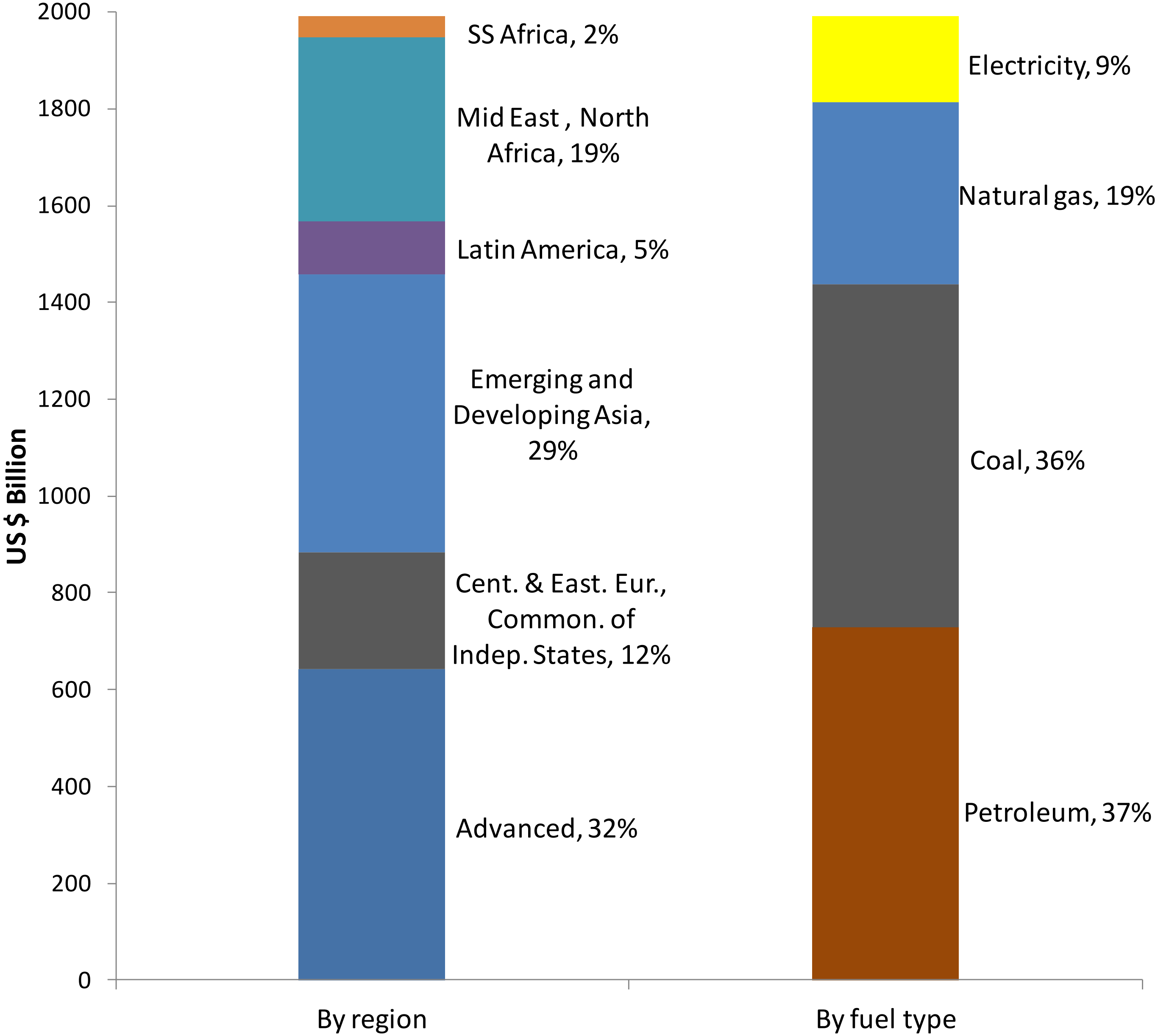
Defining Energy Subsidies

- 2 types of energy subsidies
  - ‘pre-tax’ subsidies—domestic price < supply cost
  - ‘post-tax’ subsidies—also includes implicit subsidy from failure to charge for environmental damages
- Measured in IMF (2013) by
  - price gap approach
  - first-pass extrapolation of damages from case studies
- Eliminating post-tax subsidies (i.e., getting prices right) is critical for mobilizing green investment

Pre-Tax Energy Subsidies, 2011



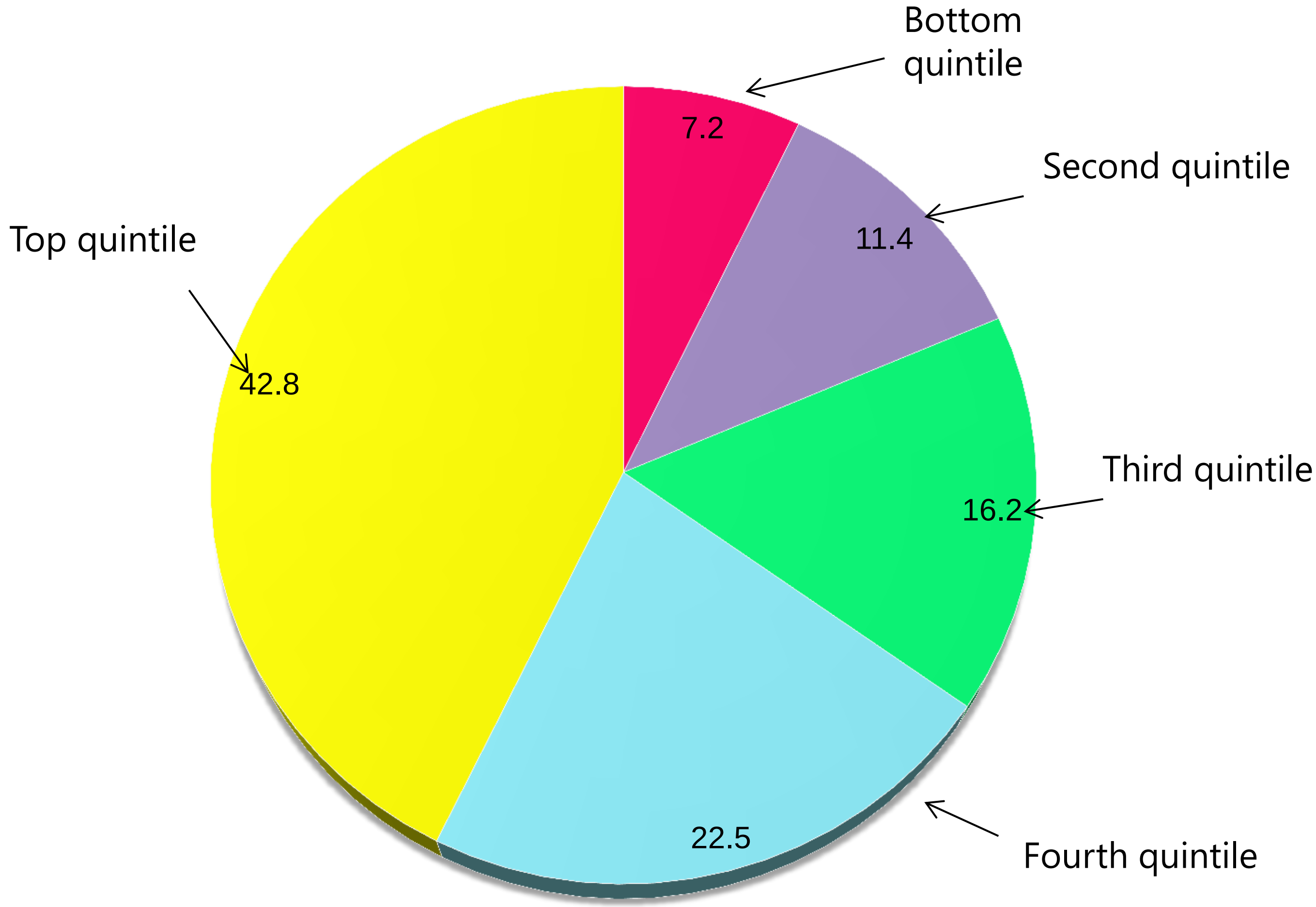
Post-Tax Energy Subsidies, 2011



Impacts of Subsidy Reform

- Large fiscal dividend
  - removing post-tax subsidies would raise revenues of 2.5% of GDP or 8% of tax revenue
- Reduce CO_2 emissions 13%
- Substantial health benefits
  - properly pricing energy would eliminate most 3.2 million premature deaths (e.g., through control technologies at coal plants)

Distribution of Petroleum Product Subsidies



Source: Arze del Granado et al. (2010)

Several Ingredients for Successful Reform

- Clarify long-term objectives (e.g., price liberalization)
- Communicate size of subsidies and benefits of reform
- Depoliticize energy pricing
- Compensate vulnerable groups
  - low-income households, trade sensitive firms
  - requires research on distributional effects (input/output tables, household spending data)

Using Donor (Climate) Finance

- Conventional (IMF) view
  - role in funding fixed costs of reforms (e.g., database, computers, pilot programs for social safety nets)
  - not for ongoing spending (e.g., transfer payments)--need to be self-sustaining from domestic revenues

- Maybe some role to reward good practice(?)
  - but first priority is to develop internationally acceptable metrics for comparing countries performance, like effective taxes on CO_2 (OECD 2013)