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The Track Record of the Group of 20 (G20) on Eliminating Fossil Fuel Subsidies

INTRODUCTION

In 2012, the total cost of global subsidies for fossil fuels was in the range of $775 billion to $1 trillion. These subsidies are not only a burden on national budgets, but also encourage the inefficient use of fossil fuels, contribute to global warming, and discourage the use of renewable "green" technologies. Supporters of "green" technologies demand that the elimination of subsidies for already established fossil fuel technologies, since they distort the playing field for emerging, clean technologies.

At their 2009 Pittsburgh Summit, G20 Leaders agreed to phase out fossil fuel subsidies "over the medium term." But, since then, little progress has been made.

This paper offers an overview of the G20's role in phasing out fossil fuel subsidies. After a short introduction about the benefits of a phase-out, the paper presents a more detailed definition of fossil fuel subsidies. Then, the G20's promises are recounted as well as the reasons for the lack of progress towards their fulfillment. Policies and initiatives are identified that could expedite the phase-out of subsidies. Finally, an analysis of the current G20 "troika" (Russia, Mexico, and Australia) and its interests will reveal the prospects for greater progress.

THE DESTRUCTIVE NATURE OF FOSSIL FUEL SUBSIDIES

Environmental

In environmental terms, the phase-out of fossil fuel subsidies is a crucial endeavor because these subsidies encourage wasteful and inefficient consumption of oil, gas, and coal, which raises emissions of greenhouse gases (GHG) and other health-damaging substances, such as fine particulates. The abolition of fossil fuel subsidies could cut carbon emissions by 4.7% in comparison to a baseline scenario in which the level of fossil fuel subsidies remains unchanged by 2020[1]. In addition, the International Energy Agency (IEA) has estimated that, solely by abolishing fossil fuel subsidies, the level of additional emission reductions needed to ensure that the rise in global temperatures does not exceed the critical 2°C limit would be cut in half.

BACKGROUND INFORMATION

How are Fossil Fuel Subsidies defined and measured?

There are many definitions of the term "subsidy": Consumption subsidies aim to lower the price paid by consumers for fossil fuels. Producer subsidies lower the cost of fossil fuel energy extraction or production, or raise the price received by energy producers.
In practice, subsidies may represent direct payments to producers, the use of loan guarantees to cut product prices, underpricing of government-provided fuels, or reduced tax rates for producers. Indirect subsidies also exist, such as public health costs borne by the government due to fossil fuel use, or military spending to protect fossil fuel assets.

Different methodologies are used to measure the level of subsidies. Comprehensive approaches try to calculate all government subsidies and opportunity costs by looking into state budgets and similar kinds of data. As it is very difficult to obtain all relevant information on governmental support, a price-gap approach can be a simple alternative. It matches domestic prices with an international market price benchmark and calculates the governmental support as the margin between the two. The greatest disadvantage of this model is its inability to capture producer subsidies.

Economic & Social

As mentioned above, governments spend nearly $1 trillion per year to subsidize fossil fuels. At the same time, most governments are attempting to cut their budget deficits. Cutting fossil fuel subsidies can be a win-win policy -- helping countries cut their deficits and boosting investment in clean energy without the need to increase overall spending.

In addition, even though consumer subsidies are often established with the intention of helping poorer households, they largely do not meet this goal, disproportionately benefiting higher-income households with higher average levels of fossil fuel consumption. The IEA showed that only 8% of consumption subsidies benefited the poorest 20% of income groups. Removing the subsidies and allocating financial support to vulnerable societal groups through other channels can be effective, even though implementation can be difficult, especially in countries which lack much institutional capacity.

1 International Energy Agency. (2011). World energy outlook 2011.

Energy Transition

By abolishing fossil fuel subsidies, the economic environment will help to level the playing field for clean sources of energy, which are often newer and emerging technologies, to compete with established fossil fuel sources. This "virtuous cycle" can help decrease countries' budgetary expenditures.

SUPPORT FOR ABOLISHING SUBSIDIES

The support for abolishing fossil-fuel subsidies is far-reaching. Supporters range from the G20 to the Business 20 (B20), UN Secretary General Ban Ki Moon, "Friends of Fossil-Fuel Subsidy Reform", a group of non-G20 countries (e.g., Sweden, New Zealand, Ethiopia), and civil society groups.

OBSTACLES FOR ABOLISHING SUBSIDIES

Despite the benefits of subsidy removal and the widespread support for it, there are a number of obstacles in the way. First, subsidies create dependency among the interest groups that receive them. Since these groups have a lot to lose, they will resist any change in the status quo[2]. Companies that are accustomed to receiving support for production of fossil fuel energy will fight to keep their economic advantage and, in some countries, they spend massively to influence the political process in their favor. Consumers, particularly the lowest income consumers, may be dependent on the lower price of fuel for basic energy needs. Second, as noted above, some countries lack the institutional capacity to replace consumption subsidies with direct benefits for vulnerable groups. Finally, production subsidies are difficult to abolish, since those first to do so diminish their own competitive advantage, thus creating a "prisoner's dilemma." The G20 could be a forum for overcoming these obstacles, since its member countries have among the highest levels of fossil fuel subsidies.

THE ROLE OF THE G20

2009-Pittsburgh (US) Summit. At the 2009 Summit, the U.S. proposed and the G20 agreed to phase out fossil-fuel subsidies. In its momentous agreement, the G20 pledged "[t]o phase out and rationalize over the medium term inefficient fossil fuel subsidies while providing targeted support for the poorest"[3]. The statement also acknowledged the negative outcomes of fossil fuel subsidies that "encourage wasteful consumption, reduce our energy security, impede investment in clean energy sources and undermine efforts to deal with the threat of climate change". But, while making this political promise was relatively easy, little progress has been made in implementing the reforms.

In the aftermath of the Pittsburgh Summit, the G20 asked the several organizations – the IEA, the Organization of Petroleum Exporting Countries (OPEC), the Organization for Economic Cooperation and Development (OECD) and the World Bank -- to submit a common report to its June 2010 Summit in Toronto, Canada. It also created a working group and called for national implementation strategies at the same time.

2010 Toronto (Canada) Summit. In Toronto, the national implementation strategies of G20 countries were approved and disclosed shortly thereafter. Surprisingly, Japan and the United Kingdom did not submit a progress report and seven countries reported that they had no subsidies in place and, therefore, did not require any implementation strategy. This group included for example Australia and Saudi Arabia which, according to most definitions, have fossil fuel subsidies in place.

2010 Seoul (Korea) Summit. Leaders reaffirmed the G20's existing agreement.

2011 Cannes (France) Summit. A new progress report was published.

2012 Mexican Summit. The Leaders' Declaration reinforced the existing commitment and proposed a completely voluntary peer review of national efforts to phase out subsidies. The Summit failed to establish a deadline or interim benchmarks for the phase-out, leaving it more questionable than ever that the phase-out can be achieved "over the medium term". The latest report on implementation strategies is so far only available as a summary.

2013 Russian G20 Presidency: Finance Ministers' Communique. This document promises a report to the Leaders' Summit in September 2013 on progress over the medium-term to phase out fossil fuel subsidies and provide targeted support for the poorest. It pledges to report to the Leaders on the development of "methodological recommendations," including a voluntary peer review process.

WHAT MUST BE DONE?

Most G20 countries are reframing existing domestic decisions and presenting them as signs of progress. What must be done?

1. DEFINITION AND METHODOLOGY. The G20 should a) provide an unambiguous definition of "fossil-fuel subsidies." This would prevent G20 countries from adopting definitions that exclude their existing subsidies. As mentioned above, Saudi Arabia reported that it does not have fossil fuel subsidies, although on its domestic market, it sells fuel far below the level of world prices. However, because it sells fuel above domestic production prices, the country argues that it does not use subsidies.

b) adopt a methodology for measuring the level of fossil fuel subsidies, as recommended by the G20 Finance Ministers' Meeting in Moscow, as well as a unified and comprehensive data base on subsidies.

2. THIRD PARTY. At present, since current methodologies are inadequate, NGOs and international organizations are filling the gap through independent, third-party reporting.

The G20 should name a neutral, third agent, most likely an international organization or a newly founded secretariat to measure each country's progress toward a) cutting subsidies and b) implementing mechanisms to provide direct assistance to vulnerable and poor groups, particularly women. While third party review would be the most effective, it is not politically popular. Mandatory, transparent and independent reporting is needed since, without it, countries are likely to under-report their subsidies.

Yet, the G20 is considering different types of voluntary peer review processes, ranging from groups of countries reviewing each other's phase-out plans to third party reviews by think tanks, academic institutions and international organizations.

3. FINANCIAL SUPPORT. Developed countries should help finance the subsidy removal plans of developing countries.

4. TIMELINE. The G20 Leaders should establish a timeline for transparent processes to phase out fossil fuel subsidies, so that the progress could be more easily tracked and benchmarked.

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2 For an analysis of this please see IISD (2009). The Politics of Fossil-Fuel Subsidies.

3 G20 (2009). Leaders' Statement: The Pittsburgh Summit.

DISSAPPOINTING LEADERSHIP PROSPECTS

Although the U.S. government spearheaded the proposal to abolish fossil fuel subsidies, it has not taken action on its rhetorical commitment.

What leadership is being exercised by the current G20 leadership troika -- Mexico, Russia and Australia?

Mexico has made legal reforms that could facilitate the phase out of fossil fuel subsidies.[4] Yet, the 2012 Mexican G20 Summit disappointed most observers. Even though it reaffirmed the commitment to abolishing subsidies and Leaders' Declaration included the possibility of a voluntary peer review process, there was little progress toward fixing existing problems.

At present, Russia holds the G20's presidency. Russia is one of the countries that lack a working definition of fossil-fuel subsidies. In its last report, Russia claimed that it had no fossil-fuel subsidies, even though the IEA estimated that, in 2010, $39.3 billion in subsidies were in place[5].

In 2014, Australia will assume the G20 Presidency. While Australia has recently introduced an emission trading scheme which helps to increase the cost of using fossil fuels, it also has fossil fuel subsidies for producers in place, for example tax breaks for extractive industries. As is the case with Russia, Australia reports that it has no fossil fuel subsidies in place, even though the OECD reported the existence of subsidies estimated at $7.8 billion in 2010 and $8.4 billion in 2011.

Of the G20 troika members, only Mexico is exercising some leadership. Therefore campaigning must increase pressure on the G20 to translate its commitments into meaningful action.

CONCLUSION

The existing G20 agreement is insufficient. It incentivizes under-reporting of and misleading accounting for fossil fuel subsidies and, to date, has not created visible progress toward implementing existing national phase-out plans. The G20 can address these inadequacies by agreeing on: a) a methodology for reporting on the use of subsidies (including a definition of "subsidies"); b) a neutral third party to report on subsidy removal, c) provision of financing for the plans of developing countries to remove subsidies; and d) a timeline for abolishing subsidies. Considerable pressure on G20 governments is needed to ensure that they translate their commitment into action.

4 With the enactment of Mexico's new Climate Law in June 2012, Mexico became the first G20 country to make a serious move to eliminate fossil fuel subsidies, and laid the groundwork for further progress in the G20.

5 International Energy Agency. (2011). World energy outlook 2011. Paris: OECD/IEA.

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