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Shifting Fossil Fuel Subsidies to Provide Energy Access and Climate Finance

The recent announcements that G20 and Asia-Pacific Economic Cooperation (APEC) nations will phase out support for fossil fuels presents an opportunity to redirect substantial portions of those subsidies into climate finance that will alleviate energy poverty. Savings from ending fossil fuel subsidies in the developed world can be used to provide funding for clean technologies and adaptation to climate change in developing countries. The concept is simple: stop funding the problem, start funding the solution.

Scale of Fossil Fuel Subsidies

The amounts of money currently going to fossil fuels in Annex 1/OECD countries alone would cover a significant amount of what is needed for climate finance, and the elimination of these subsidies also would also lead directly to greenhouse gas emission reductions in Annex 1/OECD countries. The current dollar amount of subsidies going to fossil fuels is a matter of debate, and this uncertainty highlights the need for transparency and an agreed reporting process.

Subsidy estimates	**IEA**	**WRI, UNDP**	**NGOs**	**Notes**
A1 (OECD) Fossil Subsidies	n/a	$57 billion / yr	$100 billion/yr	*Mostly producer subsidies (going to corporations). Excludes military costs (which are orders of magnitude greater).*
NA1 (non-OECD) Fossil Subsidies	$310 billion/yr	$94 billion/yr	$400 billion/yr	*Mostly consumer subsidies (going to reduce energy costs).*
IFI and ECA Fossil Subsidies			>$12 billion/yr	*Numbers vary annually.*
Per capita ($/cap)	NA1=$56	A1=$88 NA1=$35	A1 = $88 NA1=$54	*WRI numbers use 1998 population / NGO and IEA are 2008*
Emissions Reductions	10% by 2050	Not calculated	Higher emission rates and per capita subsidies in A1 could mean >20% reductions	
Notes	*From IEA Study that underlies G20 pledge. Only looks at twenty developing countries. Update ongoing in G20 process.*	*From paper by Jonathan Pershing. Sourced from UNDP, UNDESA, World Energy Council: World Energy Assessment 2004 Update. Data set: 1995-98*	*Based on GSI, IISD, BIC, ECA-Watch, Pacific Environment and Oil Change estimates.*	

Momentum and Developing Country Support

Internationally, the politics of ending fossil fuel subsidies are already intertwined with climate finance. Developing countries are legitimately concerned about access to energy for their populations, and the removal of subsidies can be seen as a threat to this – unless it is accompanied by increased climate finance. For example, nine World Bank Directors representing 90 countries recently stated that the U.S. Treasury's guidance note on halting Bank support for coal *"may have been acceptable if it had been accompanied by a US commitment to provide such enabling finance and technology".* This explicit linkage between ending subsidies and providing climate finance is new, and it is important, particularly in light of the World Bank's attempts to position itself as the key agency for climate finance.

The G20 have commissioned a report that is currently being compiled by the World Bank, the IEA, the OECD and OPEC. There are disagreements over the definition of fossil fuel subsidies and what will be quantified in the report, which will be presented at the G20 meeting in Toronto in June. Both export credit agencies and multilateral development banks may be considered as sources of fossil fuel subsidies that could in turn be targeted for phase out.

Sequencing, Trust and Linkage to Climate Finance

As the response to US Treasury's Coal Guidance Note shows, non-Annex 1 countries are unlikely to agree to phase out subsidies in the absence of new and additional finance that can meet the energy needs of their populations. Although a tentative agreement was reached in Pittsburgh regarding G20 subsidy removal, the implementation of that agreement is in doubt. This is in part because additional finance has not been put on the table.

Eliminating subsidies to fossil fuels on its own is not adequate to establish trust and build momentum. The removal must be sequenced, and linked to climate finance. Most feasible would be a phased removal of fossil fuel subsidies, gradually decreasing the level of support, and differentiated in time and by country income level.

For example, Annex 1 countries could commit to phasing out energy subsidies completely within five to seven years, and that finance could in turn be redirected to climate finance. Middle-income developing countries could aim for 10 years, and low-income countries could target a 50 percent reduction within 10 years and a complete elimination in 15 years. This strategy offers benefits to all parties:

- Annex 1 countries would take a significant step forward in reducing their emissions, while also finding needed funding for climate finance;
- Non-Annex 1 countries would benefit from reduced exposure to the fluctuations in the oil market as well as financial and technology transfers for mitigation. In addition, subsidy phase out could become a central part of nationally appropriate mitigation actions (NAMAs);

At the World Bank and other multilateral development banks, subsidy removal should be placed in the context of support for increased energy access for the poor and climate finance. This would mean:

- Prioritizing the energy needs of the millions of people living in areas not connected to the grid, and those dependent on non-electrical energy sources.
- Focusing on decentralized sustainable energy solutions that meet the energy needs of the poor in a cost-effective and energy efficient manner.
- Ending investments in fossil fuel extraction and use.
- Shifting the portfolio of the development banks to be based on efficiency and renewables.

Politics and Policy of Subsidy Shift

Coupling ending fossil fuel subsidies with a commitment to shift savings to improving energy access and climate finance is good politics, as well as good policy. *Domestically*, the message is that international climate finance must come from somewhere and therefore subsidy shift is a fiscally responsible solution in difficult economic times. *Internationally*, linking subsidy removal with increased climate finance quickly addresses the legitimate concerns that subsidy removal could decrease energy access. Developed countries can generate the trust and support from the developing world that is necessary for securing a global clean energy transition by committing to improving energy access globally through renewables while phasing out fossil fuel subsidies domestically and via export credit agencies and development banks.

From a policy perspective, it is important to note that actually shifting producer subsidies (which are often in the form of tax credits) and specifically redirecting them to international climate funds, poses some technical and accounting challenges. In practice, the climate finance might have to be appropriated separately from the budget lines that eliminate the subsidies. Another possibility is to create a new legislative vehicle that both eliminates subsidies and redirects them to climate finance.