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POLICY BRIEF

Prioritizing Fossil-Fuel Subsidy Reform in the UNFCCC Process: Recommendations for short-term actions

Virginia Benninghoff

Key Recommendations for Parties to the United Nations Framework Convention on Climate Change (UNFCCC):

- Propose options for addressing fossil-fuel subsidy reform—for example, through technical workshops and discussions—in country submissions on increasing pre-2020 ambition to the Ad Hoc Working Group on the Durban Platform for Enhanced Action (ADP-Workstream 2).¹ (Next submissions are due September 1, 2013.)
- Explore the possibility of developing fossil-fuel subsidy reform as a Nationally Appropriate Mitigation Action (NAMA). Interested developing countries can consider communicating to the Secretariat that they intend to implement fossil-fuel subsidy reform as a NAMA and request support.
- Raise fossil-fuel subsidy reform in submissions to the Subsidiary Body for Scientific and Technological Advice (SBSTA), requesting methodological issues related to reform be added to the agenda or discussed in a dedicated workshop.
- Include fossil-fuel subsidy reform on the agenda of the proposed ministerial meeting on energy efficiency and renewable energy at the 19th session of the Conference of the Parties to the UNFCCC (COP 19) in Warsaw, pointing out how it can reduce barriers to energy efficiency and renewable energy deployment.
- Voluntarily report on fossil-fuel subsidies and steps toward reform as part of national communications, biennial reports and biennial update reports.

¹ The ADP created two workstreams for addressing its mandate: Workstream 2 is occupied with options for increasing mitigation ambition pre-2020 to bridge the gap between reductions pledges and the mitigation necessary for staying within the 2°C goal (see the second section of this policy brief). Workstream 1 is concerned with the agreement (a protocol or other legal instrument) that will be adopted in 2015 and enter into force in 2020. See <http://unfccc.int/bodies/body/6645.php> for more information on the ADP.

How will fossil-fuel subsidy reform contribute to climate change mitigation?

Scientists say we are on track to see average temperatures rise between 3.6°C and 5.3°C above pre-industrial levels, with most of the increase by the end of this century (International Energy Agency [IEA], 2013). Global temperature increases of this magnitude will likely create climate feedbacks that further drive warming, exacerbating the polar ice-sheet loss, frequent and intense storms, sea-level rise, heat waves and droughts already being experienced. A rise of more than 2°C will significantly inhibit humanity's ability to adapt to climate change.

The IEA recently released its *World Energy Outlook Special Report, Redrawing the Energy-Climate Map*, which outlines four policies that—if adopted right away—would give the world another chance at limiting the increase to 2°C, at no economic cost.² The report highlights energy-efficiency measures, scaling down the use and proliferation of low-efficiency coal-fired power plants, mitigating methane emissions from upstream oil and gas production, and “accelerating the (partial) phase-out of subsidies to fossil-fuel consumption” (IEA, 2013, p. 2). According to the IEA, a 25 per cent reduction in fossil-fuel subsidies by 2020 in net exporting countries would reduce carbon dioxide emissions by 360 million tonnes (Mt) in 2020 relative to its New Policies Scenario (which assumes a total phase-out in fossil-fuel importing countries by 2020).³

Clearly, the potential of fossil-fuel subsidy reform to mitigate climate change cannot be ignored.

Why should Parties to the UNFCCC prioritize the reform of fossil-fuel subsidies?

Recognizing the significance of the 2°C threshold, Parties to the UNFCCC have agreed to a goal of keeping average temperatures from rising more than 2°C above pre-industrial levels. However, Parties' current mitigation pledges do not add up to the emissions reductions necessary to achieve that goal. To address this problem, the 17th UNFCCC Conference of the Parties in Durban (COP 17) established Workstream 2 of the Ad Hoc Working Group on the Durban Platform for Enhanced Action (ADP) in order to increase pre-2020 mitigation ambition (UNFCCC, 2012).

In recent submissions to the ADP, many parties have identified the phasing out of fossil-fuel subsidies as an option for enhanced mitigation ambition and acknowledged the wide-ranging benefits, from the diffusion of new technologies to the correction of market distortions. Most recently, the technical paper *Compilation of Information on Mitigation Benefits of Actions, Initiatives and Options to Enhance Mitigation Ambition* (UNFCCC, 2013), produced by the Secretariat based on Parties' submissions, listed fossil-fuel subsidy reform as one of eight thematic areas with mitigation benefits.⁴

In addition to reducing emissions, phasing out harmful fossil-fuel subsidies improves country fiscal balances, minimizes market distortions, encourages private investment, reduces the unfair accrual of subsidies to the wealthier classes and special interests, and frees up scarce resources for better uses. These positive budgetary and economic effects—along with the climate benefits—are commanding the attention of policy-makers and international

² The IEA selected only measures that were GDP-neutral. Under the four policies chosen, GDP growth averages 4.1 per cent annually from 2012–2020, and, after 2020, the measures foster additional economic growth. The net economic benefits are derived from two qualities the policies all share: (1) They are market-proven, and are ready and available to be deployed today; (2) When taken together across a range of countries, they deliver overall savings (IEA, 2013).

³ In its *World Energy Outlook 2011*, the IEA projects that the complete phase-out of fossil-fuel subsidies by 2035 would cut energy-related carbon dioxide emissions by 5.8 per cent, relative to subsidy policies remaining unchanged (IEA, 2011).

⁴ Parties that raised fossil-fuel subsidy reform in their submissions to the ADP include: Norway; the EU; the U.S.; Nepal on behalf of least-developed countries; New Zealand; Japan; the group of Liechtenstein, Mexico, Monaco and Switzerland; and the group of Bangladesh, Cameroon, Costa Rica, Dominica, Dominican Republic, Gabon, Guyana, Honduras, Kenya, Nigeria, Papua New Guinea, Republic of Congo and Uganda. The submissions may be found at <http://unfccc.int/bodies/awg/items/7398.php>.

organizations such as the Organisation for Economic Co-operation and Development (OECD) and the World Bank, and helping fossil-fuel subsidy reform gain traction in international forums such as the G-20 and the Asia-Pacific Economic Cooperation forum (APEC).

Despite recognition of its many benefits, it is not easy to implement fossil-fuel subsidy reform, and progress can be slow. Many countries need increased access to best practices, financial and technical assistance, and help overcoming public and private opposition. Parties to the UNFCCC can and should take an active role in advancing fossil-fuel subsidy reform. Countries do not need to wait for a negotiated agreement to act, as fossil-fuel subsidy reform can be incorporated into UNFCCC processes right away. Doing so will build on the international momentum and facilitate partnerships among countries committed to fossil-fuel subsidy reform.

EXTRA CASH

Phasing out fossil-fuel subsidies frees up public funds for other uses. As developed countries have struggled to raise the promised billions for adaptation and mitigation funds, some have suggested that fossil-fuel subsidy reform is also an answer to this problem. The savings that result from reform in developed countries could be redirected through various financial mechanisms to help developing countries with mitigation and adaptation. To read more, see the 2010 *Report of the Secretary-General's High-level Advisory Group on Climate Change Financing*.⁵

How can Parties best incorporate fossil-fuel subsidy reform into the UNFCCC process?

The UNFCCC provides an important forum for extending this initiative to as many countries as possible and for bringing to the table new mechanisms for implementing fossil-fuel subsidy reform. While members of the G-20 and APEC have already committed to rationalizing and phasing out inefficient fossil-fuel subsidies, there are many more countries that could benefit from reform.⁶ In order to galvanize even broader support and ensure all countries have the means to take action on fossil-fuel subsidy reform, the Global Subsidies Initiative (GSI) recommends that Parties to the UNFCCC:

- **Emphasize subsidy reform as an effective option for climate change mitigation under ADP Workstream 2.** The next deadline for submissions to the Secretariat is September 1, 2013. Parties should include fossil-fuel subsidy reform in their submissions to encourage its addition to the ADP's agenda. Furthermore, we recommend that Parties call for a workshop on fossil-fuel subsidy reform under the auspices of the ADP at COP 19 in Warsaw (November 2013). The workshop could focus on the exchange of information and experience and include presentations from external Parties such as the World Bank, IEA, OECD or GSI.
- **Explore the possibility of developing fossil-fuel subsidy reform as a NAMA.** Interested developing countries can consider communicating to the Secretariat that they intend to implement reform as a NAMA. Starting now to develop fossil-fuel subsidy reform into NAMAs will lay the groundwork for the post-2020 timeframe, when NAMAs will presumably be fully scaled up and partnerships providing external technical and financial assistance will potentially be established.⁷

⁵ Available at http://www.un.org/wcm/webdav/site/climatechange/shared/Documents/AGF_reports/AGF%20Report.pdf. See also Kretzmann, 2011.

⁶ In the outcome document adopted by the 193 member states and one observer state of the UN Conference on Sustainable Development, countries that had already committed to phasing out fossil-fuel subsidies reaffirmed their commitment and encouraged others to also consider fossil-fuel subsidy reform, but no new commitments were undertaken. See United Nations, 2012.

⁷ In fact, the NAMA Facility (jointly established by the U.K. Department of Energy and Climate Change and the German Federal Ministry for the Environment, Nature Conservation, and Nuclear Safety) has issued its first call for project outlines of NAMAs seeking financial support. For more information on the application and selection process, see <http://www.international-climate-initiative.com/en/issues/nama-facility/>.

Given the large mitigation potential of fossil-fuel subsidy reform, Parties should recognize that some countries may find it to be an appropriate and effective method of emissions reduction and should help ensure assistance is available to those countries requesting reform be a supported NAMA. There are many forms this assistance could take. Among them might be: providing expertise and tools for modelling impacts; help in rolling out social welfare programs to minimize negative impacts on vulnerable groups; resources for expanding public transport networks; funding for energy-efficiency improvements and renewable energy deployment so that subsidy reform does not compromise energy access; and recommendations on effective communications strategies.

- **Raise fossil-fuel subsidy reform in submissions to the SBSTA, requesting methodological issues related to reform be added to the agenda or discussed in a dedicated workshop.** The discussions on short-term ambition (ADP Workstream 2) and a long-term agreement (ADP Workstream 1) both benefit from the concurrent activities of the SBSTA, which provides expert advice on everything from technology transfer to monitoring, reporting and verification for domestically supported NAMAs. The SBSTA's work on fossil-fuel subsidy reform could include developing guidelines and methodology for subsidy inventories, measuring mitigation impacts of reform and liaising with expert institutions that are researching the issue. Such technical advice would help ensure any decisions made by the Parties on subsidy reform (such as those suggested in this policy brief) are implemented effectively.
- **Include fossil-fuel subsidy reform on the agenda of the proposed ministerial meeting on energy efficiency and renewable energy at COP 19 in Warsaw.** Phasing out fossil-fuel subsidies can catalyze improvements in efficiency and deployment of renewable energy technologies. One important outcome of this meeting would be formal, high-level recognition that fossil-fuel subsidy reform must be advanced to support goals for renewable energy deployment and efficiency improvements.
- **Voluntarily report fossil-fuel subsidies and any efforts toward their reform as part of national communications and/or biennial reports and biennial update reports to the UNFCCC Secretariat.** Reporting increases transparency and can start both the internal conversations and external awareness raising necessary at the beginning of the reform process. In fact, the UNFCCC document outlining the reporting format for Annex I Parties' National Communications, FCCC/CP/1999/7, specifically suggests reporting energy subsidies (UNFCCC, 2000). With biennial reporting starting in 2014, Parties should consider including the state of their fossil-fuel subsidies and reform in their biennial reports (for developed countries) and biennial update reports (for developing countries). For Parties that choose to develop subsidy reform as a NAMA, biennial update reports will be an important way to track progress.

We suggest more resources be developed to inform Parties how fossil-fuel subsidies and progress toward their reform should best be included in reports. Reporting is an area where capacity building will be essential for countries unable (or unsure of how) to collect accurate data on their subsidies and the effects of reform. Suggested guidelines on reporting based on current guidance from the UNFCCC website are below.



HOW TO REPORT FOSSIL-FUEL SUBSIDIES

Annex I Countries

- Collect data on subsidies or use inventories from the OECD,⁸ IEA⁹ or GSI.¹⁰
- For **national communications** (UNFCCC, 2000):
 - Include subsidies data in “National Circumstances Relevant to Greenhouse Gas Emissions and Removals.” Categorize fossil-fuel subsidies under the energy sector.
 - AND/OR include a description of current subsidies as part of the introduction to the “Policies and Measures” (PaMs) section.

Non-Annex I Countries

- Collect data on subsidies or use inventories from the IEA, OECD or GSI.
- For **national communications** (UNFCCC, 2003):
 - Include current policies and data as part of the “National Circumstances.” Energy-related circumstances, such as fossil-fuel subsidies, fall under the economy category.
 - AND/OR include current subsidies in the introduction to “Measures to Mitigate Climate Change” under the “General Description of Steps Taken or Envisaged to Implement the Convention.”

HOW TO REPORT EFFORTS TO REFORM FOSSIL-FUEL SUBSIDIES

Annex I Countries

- For **national communications** (UNFCCC, 2000):
 - List fossil-fuel subsidy reform efforts under “Policies and Measures” (PaMs), classifying by sector (energy) and gas (carbon dioxide).
 - Describe the reform’s structure, policy-making process and impact, comparing effects to a reference case (i.e., business as usual).
 - Report any work on reform with developing Parties in “Education, Training, and Public Awareness” and/or “Financial Resources and Transfer of Technology” (depending on the partnership’s goals).
- For **biennial reports** (UNFCCC, 2012):
 - Under “Progress in Achievement of Quantified Economy-Wide Emission Reduction Targets and Relevant Information,” report reform efforts in “Mitigation Actions and their Effects,” classifying by sector and gas.
 - (For Annex II Parties) List support for reform efforts in developing countries in “Provision of Financial, Technological, and Capacity-Building Support to Developing Country Parties.”

Non-Annex I Countries

- For **national communications** (UNFCCC, 2003):
 - Report subsidy reform in “General Description of Steps Taken or Envisaged to Implement the Convention” under “Measures to Mitigate Climate Change.”
 - Participation in international partnerships can be reported under “Other Information” in “Activities Relating to Technology Transfer,” “Information on Education, Training and Public Awareness” and “Capacity-Building,” depending on the partnership. Inadequacies in assistance can be noted in these sections as well.

⁸ Available at <http://www.oecd.org/site/tadffss/>.

⁹ Available at <http://www.iea.org/subsidy/index.html>.

¹⁰ Available at <http://www.iisd.org/gsi/fossil-fuel-subsidies/fossil-fuels-what-cost>.

- Further elaborate on specific needs under “Constraints and gaps, and related financial, technical, and capacity needs” in “Financial, technical and capacity needs,” “Technology transfer” and “Capacity-building needs other than those identified.” List reform proposals needing funds in “Proposed projects for financing.”
- For **biennial update reports** (UNFCCC, 2012):
 - Report efforts to reform fossil-fuel subsidies as a “Mitigation Action,” including quantitative goals and progress indicators.
 - Describe aid already received for reform and remaining needs in “Finance, Technology, and Capacity-Building and Support Received.”

Will the UNFCCC process complement other international bodies' work on fossil-fuel subsidy reform?

Momentum is already building for the Parties to the UNFCCC to take up the issue of fossil-fuel subsidy reform. For instance, the Friends of Fossil-Fuel Subsidy Reform is a group of non-G-20 countries committed to championing this issue in international forums. Members of the group—Costa Rica, Denmark, Ethiopia, Finland, New Zealand, Norway, Sweden and Switzerland—came together in light of the G-20 and APEC commitments on phasing out inefficient fossil-fuel subsidies to support the expedient fulfillment of this goal. More recently, Friends members have also been raising the issue in their submissions to the UNFCCC Secretariat in advance of the various bodies’ meetings that take place each year. Other countries, such as Mexico, the U.K. and the U.S., have been promoting fossil-fuel subsidy reform in international forums, and should do so in the UNFCCC as well.

Since 2009, the G-20 and APEC have continued to reaffirm their commitment to fossil-fuel subsidy reform. Members have started reporting on reform efforts on a voluntary basis, and both groups are developing processes for fossil-fuel subsidy peer reviews. However, there is more to be done.

In its June 2013 Working Groups’ Recommendations (C-20, 2013), the C-20 (the G-20 Civil Summit) recommended implementing the peer review mechanism on country reporting more widely by offering further guidance and support for G-20 countries to help them identify, measure and evaluate their subsidies; increasing the priority of the issue within the G-20’s many areas of interest; and taking forward engagement, including during the Australian presidency into 2014. See GSI (2013) for a recap.

Progressing fossil-fuel subsidy reform within the UNFCCC would complement these initiatives by creating a vehicle (most likely using NAMAs), which may include partnerships resulting in technical and/or financial assistance to developing countries wanting to institute reforms. In addition, it would vastly increase the number of countries involved—with 195 Parties to the UNFCCC, the policy dialogue and expertise will reach a wider set of countries than is encompassed by the G-20 and APEC. Lastly, including fossil-fuel subsidy reform in the UNFCCC process will increase reporting on fossil-fuel subsidies and widen the breadth of the reports. Better reporting means more transparency, which will help build public support and political capital at home.

The GSI therefore encourages Parties to propose (by September 1, 2013 and in future submissions) that fossil-fuel subsidy reform be considered under the auspices of ADP Workstream 2, including through technical workshops and discussions. Parties should also consider the possibility of developing fossil-fuel subsidy reform as a NAMA, ask the SBSTA to include it in discussions and workshops, and include the issue in the ministerial discussion on energy efficiency and renewable energy. Finally, we encourage Parties to voluntarily report their fossil-fuel subsidies and steps toward their reform in either (or both) their national communications or biennial reports.

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Head Office
161 Portage Avenue East, 6th Floor, Winnipeg, Manitoba, Canada R3B 0Y4
Tel: +1 (204) 958-7700 | Fax: +1 (204) 958-7710 | Web site: www.iisd.org

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International Institute for Sustainable Development
Global Subsidies Initiative
International Environment House 2
9 chemin de Balexert, 1219 Châtelaine, Geneva, Switzerland
Tel: +41 22 917-8373 | Fax: +41 22 917-8054

For further information contact Kerryn Lang at: klang@iisd.org or +41-22-917-8920.