Principle 3 – Effective Carbon Pricing: Early survey results

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London, 17 November 2019
Responses to Principle 3 survey

- Respondees (Belgium, Colombia, Denmark, Finland, Germany, Iceland, Latvia, Luxembourg, Mexico, Norway, Paraguay, Sweden, Switzerland, The Netherlands, Uganda):

  Thank you!

- Non-respondees (~35), including new countries:

  Please fill out the survey

  bit.ly/principle3survey
THE COALITION OF FINANCE MINISTERS FOR CLIMATE ACTION

HELSINKI PRINCIPLES

We, as Finance Ministers from around the world:

Cognizant that climate change poses a significant threat to our economies, societies, and environments, including risks to economic growth and macroeconomic stability, and that there is an urgent need to accelerate action;

Recognizing that climate change is also an opportunity, and that taking action can generate substantial benefits for our societies by stimulating technological innovation, improving human well-being, and accelerating economic growth;

Noting our unique position as Finance Ministers to help accelerate a just transition to a low-carbon and climate-resilient economy through macroeconomic and fiscal policy, public financial management and, where applicable, financial regulation;

Acknowledging that such policies and actions will support global collective action on climate change under the Paris Agreement;

Cognizant that Finance Ministers have a common purpose, and can benefit from a forum for sharing experiences and facilitating the adoption of best practices and policies for low-carbon and climate-resilient growth; and

Supported by technical assistance from development partners.

Hereby establish a Coalition of Finance Ministers to demonstrate our leadership in the response to climate change, wherein we will operate within our national frameworks, competencies, and mandate to support the following principles:

1. **Align** our policies and practices with the Paris Agreement commitments;

2. **Share** our experience and expertise with each other in order to provide mutual encouragement and promote collective understanding of policies and practices for climate action;

3. **Work** towards measures that result in effective carbon pricing;

4. **Take** climate change into account in macroeconomic policy, fiscal planning, budgeting, public investment management, and procurement practices;

5. **Mobilize** private sources of climate finance by facilitating investments and the development of a financial sector which supports climate mitigation and adaptation;

6. **Engage** actively in the domestic preparation and implementation of Nationally Determined Contributions (NDCs) submitted under the Paris Agreement.
“Effective carbon pricing means that countries adopt measures to achieve carbon price levels that are sufficient to incentivize the emission reductions needed to meet their own emission reduction targets, subject to their national circumstances and with a view to reaching carbon price levels consistent with the Paris Agreement’s long-term objectives.”
Why a survey?

Carbon prices remain well-below ‘effective’ levels

• existing carbon prices: <20% CO2 coverage, mostly <US$15 per ton of CO2¹
• needed for PA: 100% CO2 coverage, $40-80 by 2020, $50-100 by 2030²

Q. what’s holding countries back from implementing effective carbon pricing?

• Economic, societal, political economy, cultural/ideological, inter-departmental, international climate policy, technical, or other?

To help inform our technical workstream on Principle 3, we sought to find out:

• What is the current structure of fossil fuel subsidies and/or carbon taxes?
• What is the primary motivation for reform?
• What are the main obstacles to achieving effective carbon pricing?

Q. Are your country's environmental taxes high enough to...

- Sufficiently address environmental externalities (pollution)?
  - Yes
  - No
  - Prefer not to answer

- Raise sufficient revenues?
  - Yes
  - No
  - Prefer not to answer
Q. Do you have fossil fuel subsidies?

65% have fossil fuel subsidies
Q. Do you have a carbon tax (or charge)?

59% have a carbon tax/charge

- 35.3% Not in place
- 29.4% Under consideration
- 23.5% Already operational
- 11.8% Operational and willing to share experience
Reformers: Q. Was the carbon tax/charge deemed successful?
Non-reformers: Q. have you considered reforms?

Fossil fuel subsidies in place

- Yes: 60%
- No: 40%

No carbon tax in place

- Yes: 57.1%
- No: 42.9%
Q. Why did you consider reform?

Please state how important the following reasons that your country considered reforming fossil fuel subsidies or implemented a carbon tax/charge out of 5 (1 being not very important, 5 being very important):

- Reductions in local air pollution (e.g. PM2.5, NOx, SOx, etc)
- Reductions in road accidents & deaths
- Fiscal revenue savings
- Reductions in carbon emissions
- Reductions in local air pollution (e.g. PM2.5, NOx, SOx, etc)
- Reductions in road accidents & deaths
- Fiscal revenues raised
- Reductions in carbon emissions
- Reductions in local air pollution (e.g. PM2.5, NOx, SOx, etc)
- Reductions in road accidents & deaths
What are the economic obstacles?

fossil fuel subsidy reform

carbon taxes
What are the societal obstacles?

- Fossil fuel subsidy reform
- Carbon taxes
What are the political economy obstacles?

- fossil fuel subsidy reform
- carbon taxes
What are the cultural/ideological obstacles?

- Fossil fuel subsidy reform
- Carbon taxes

Cultural or ideological:

- Resistance to any form of tax increase (even if revenue-neutral)
- Suspicion that fossil fuel subsidy reform might impede the smooth functioning of the market
- Lack of belief that national fiscal policy change can make a substantive contribution to a global problem
- Belief that richer countries should mitigate and poorer countries should only or mostly adapt
What are the departmental obstacles?

- Fossil fuel subsidy reform
- Carbon taxes
What are the international climate policy obstacles?

- fossil fuel subsidy reform
- carbon taxes
What are the technical obstacles?

- Fossil fuel subsidy reform
- Carbon taxes

Technical obstacles to implementation:

- Lack of knowledge on optimal fossil fuel subsidy reform designs (e.g. revenue usage, complementary policies)
- Lack of knowledge on optimal carbon tax reform designs (e.g. revenue usage, fuel coverage, downstream/upstream, complementary policies)
Summary

• Caveat:

more responses needed! – bit.ly/principle3survey

• There are numerous **differences** across Members:
  • varying existing fiscal **systems** (fossil fuel subsidies and carbon taxes)
  • varying **attitudes** towards reform, including ideological priors (on taxes, market functioning, environmental effectiveness, and equity)
  • variable **concern** with potential for protests and political opposition, as well as effects on the fossil fuel sector and fuel smuggling
  • variable consideration of the possible **development co-benefits** of reforms (e.g. improvements in health due to reduced local air pollution and reduced road accidents)
Summary

• … but also similarities across Members:
  • agreement environmental taxes are too low (revenues & environmental effectiveness)
  • inter-departmental issues not important (albeit some concerns with earmarking)
  • fiscal revenues most important for fossil fuel subsidy reform
  • CO2 reduction more important for carbon taxes
  • concerns over macro effects of fossil fuel subsidy reform and carbon taxes, especially competitiveness, GDP, and employment, but not FDI
  • vulnerability of the poorest and distributional effects important
  • large methodological/knowledge gaps on estimating effects and designing optimal reform packages
Thank You!

[link: bit.ly/principle3survey]

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What is the Carbon Pricing Assessment Tool (CPAT)?

- a spreadsheet-based tool
- being developed by the World Bank and IMF jointly
- aimed at country economists in finance ministries and IFIs
- allows rapid estimation of effects of carbon pricing reforms on a variety of metrics of interest:
  - **macroeconomic** – employment, fiscal revenues, tax evasion
  - **energy & emissions** – energy consumption, local pollutants (PM2.5, NOx, SO2), global pollutants (CO2), distributional effects (across quintiles and urban vs. rural), oil & gas sector profits
  - **development co-benefits** – reductions in mortality and morbidity due to air pollution and road accidents, traffic congestion, and reductions in the shadow economy
- can help policymakers design & compare carbon pricing reforms, helping them achieve their climate mitigation goals (Paris Agreement NDCs) and development objectives (SDGs) jointly