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**GREEN
FISCAL POLICY
NETWORK**

Issue 3 – July 2015

Fiscal Policy and Deforestation

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1. Welcome Message from the Green Fiscal Policy Network Secretariat

In this issue, we continue the theme of fiscal policy and climate change in the build-up to COP21 in Paris later this year. In particular, this issue focuses on the role of forests, the ecosystem services they provide that are important for mitigating climate change and the adverse impacts of deforestation from harmful subsidies for agricultural commodities.

The value of forestry resources to sustainable development is well-established. Forests perform key ecological services such as absorbing carbon from the atmosphere, thus helping to counter the effects of greenhouse gas emissions responsible for climate change. They are also sources of employment and livelihood in many countries and provide products important for health and human wellbeing. While the Reducing Emissions from Deforestation and Forest Degradation (REDD+) initiative has mobilized significant amounts of international public financing for forests, agriculture subsidies in some countries are undermining the efficiency of public financing by driving the expansion of agricultural commodities such as palm oil and timber that are associated with deforestation. These subsidies even outpace funding for forestry conservation. While data on the scale, intent and impact of the subsidies is imperfect, preliminary research undertaken by the Overseas Development Institute indicates that reforming subsidies to agricultural commodities is a key first step to enhancing the efficiency and coherence of public financing. This article provides a synthesis of this research.

We hope you will enjoy the issue and contact us if you would like to contribute to forthcoming issues!

Joy Kim (UNEP), Ian Parry (IMF) and Tobias Zeller (GIZ)

2. Guest Article: *Improving the efficiency of financing for REDD+: addressing the perverse effect of agricultural subsidies*

by William McFarland, Shelagh Whitley, Gabrielle Kissinger



Shelagh Whitley is a Research Fellow in Climate and Environment at the Overseas Development Institute (ODI). Shelagh's research focuses on private climate finance and the role of subsidies in shaping private investment. Prior to joining the ODI, she worked in carbon markets, clean energy finance, and climate policy development within the public and private sectors.



Gabrielle Kissinger is a consultant to the UNEP and the UN-REDD Programme, and also principal of Lexeme Consulting based in Vancouver, Canada. She focuses on strategies for linking science into policy and decision-making in the areas of global land-use and climate change, REDD+, climate-smart agriculture, finance and investment that supports sustainable land use, government affairs and business solutions to sustainability.



William McFarland is the Climate and Environment Programme Manager, as well as a researcher in the green growth team. His research covers the political and economic influences over management of forests and other environmental issues.

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Need for up-scaling REDD+ finance

Commitments of REDD+ finance are an important contribution to wider pledges on climate finance under the UNFCCC, whereby developed countries have agreed to mobilise \$100 billion annually from public and private sources to address the needs of developing countries by 2020. This will include support in reducing deforestation and forest degradation (forest loss). Deforestation threatens to undermine the many benefits

provided by forest resources, such as supplying freshwater, supporting biodiversity, protecting soil quality and storing carbon. Deforestation and forest degradation account for 20% of global greenhouse gas emissions, second only to the energy sector, thereby exacerbating climate change.¹ Over half of total global forest loss between 1990 and 2010 occurred in Brazil and Indonesia (FAO, 2010), with Brazil losing an average of 2.7 million hectares per year during the period and Indonesia losing 1.2 million hectares. After peaking in 2004, rates of forest loss in Brazil have fallen significantly.² In contrast, the rate of forest loss in Indonesia has continued to rise over the same time period, and may now surpass that of Brazil (Hansen et al, 2013; Margono et al., 2014). Between 2008 and 2012, forest loss accounted for 61% and 28% of greenhouse gas (GHG) emissions in Indonesia and Brazil, respectively (WRI, 2014).

While there are different patterns of forest loss across each region of the world and within countries, agriculture is widely acknowledged to be the largest driver of forest loss globally, linked to 80% of forest loss (Geist and Lambin, 2002; Gibbs et al., 2010; Kissinger et al., 2012; Hosonuma et al., 2012; Houghton, 2012). Commercial timber extraction has also been identified as a key driver of forest loss, accounting for over 70% of forest degradation in Latin America and Asia (Hosonuma et al., 2012). In addition, the drivers of forest loss in large parts of Africa include: mining, infrastructure development, urban expansion, uncontrolled fire, fuel wood collection and charcoal production (Hosonuma et al., 2012).

A recent report recommends that developed countries provide at least \$5 billion per year to finance REDD+³ in developing countries (New Climate Economy, 2014). However, between 2006 and March 2014, global public and private finance pledged for REDD+ was on average only \$1 billion per year, with almost 90% coming from the public sector, led by the EU and Norway (Norman and Nakhooda, 2014). The focus of most REDD+ spending to date has been on capacity building and readiness⁴ to prepare countries to access larger flows of REDD+ finance (ie. through the development of forest cover baselines and monitoring systems), activities which in the near term do not directly reduce greenhouse gas emissions. In addition, commitments have slowed since 2011, which has been attributed to challenges in delivering REDD+ and the impact of the financial crisis on public sector finances (UN-REDD, 2013; Norman and Nakhooda, 2014).

Currently, efforts are underway to address this growing finance gap while recognising that additional resources must be brought to bear alongside those of governments. By scaling up existing public support and developing new incentives, governments and international organisations believe that additional private finance can be mobilized to support REDD+. Examples of interventions proposed to mobilise private investment include: concessional finance for sustainable land use; payments for carbon, biodiversity and watershed services; development of criteria and institutions for certification of commodities and secondary products; and new investment vehicles including impact bonds and climate or green bonds⁵ (UN-REDD, 2013; Norman and

¹ According to the UN-REDD Programme, <http://www.un-redd.org/aboutredd>, accessed 18 June 2015

² Despite a year-on-year increase in forest loss from 2012-2013, and uncertainty over the change in 2014, overall forest loss in the Amazon has dropped by 80% since 2004 (Mongabay, 2014).

³ REDD+: reducing emissions from deforestation and forest degradation; conservation of forest carbon stocks; sustainable management of forests; and enhancement of forest carbon stocks (IPCC, 2014).

⁴ REDD-Readiness is a national strategy to prepare for a REDD+ payment mechanism by understanding and addressing gaps that may exist between a country's existing social, technical and institutional capacities and those that may be required for participation in an eventual REDD+ mechanism (Johns, Johnson and Greenglass, 2009).

⁵ Impact bonds are relatively new financial instruments that allow for up-front finance linked to future payment for performance (ie. positive social or environmental impact). Climate and green bonds on the other hand are traditional debt instruments that have been screened to ensure that the projects or companies who issued them are having positive environmental or climate impacts.

Nakhooda, 2014). What has received little or no attention, however, is the degree to which existing public spending undermines or works at cross-purposes to REDD+ finance.

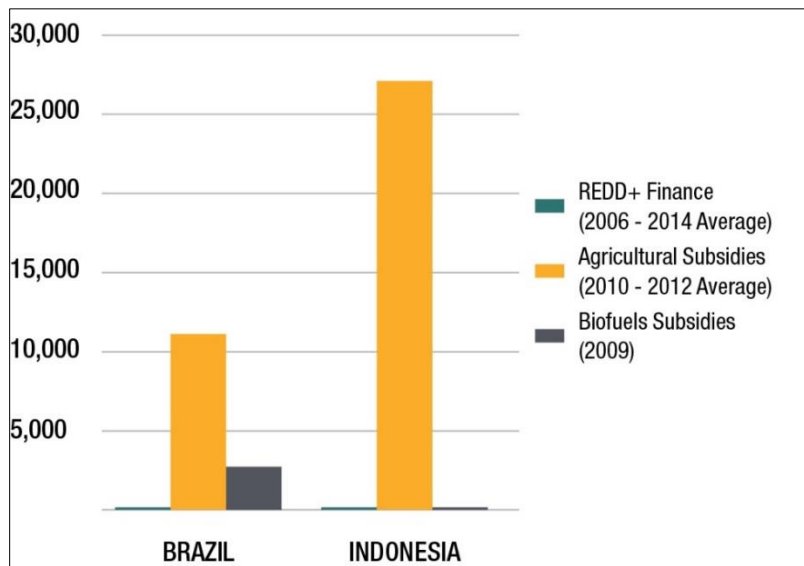
Role of agriculture subsidies in driving forest loss

At present, little attention has been paid to the role that government support plays in driving forest loss. In particular, little effort has been made to understand and reform existing subsidies that contribute to make forest loss profitable. For instance, subsidies to agricultural commodities are often justified as a way to boost agricultural yields, supplement farm income, manage the supply of agricultural commodities, and influence the cost and supply of such commodities. In reality, however, by reducing the price of a natural resource below the marginal cost to society, such subsidies can have far-reaching impacts (positive or negative) on both investment and consumption patterns. For instance, subsidies to agricultural commodities can accelerate environmental degradation through resource inefficiency, overcapitalisation, over consumption and by depriving the state of resources to support sustainable management (New Climate Economy, 2014). Agricultural subsidies are often designed without consideration for how those subsidies will impact forest or water resources, and yet these impacts not only exist, but can be significant. The provision of REDD+ finance is not conditional on addressing agriculture subsidies (Salvini et al, 2014), and yet the possibility exists to better define how governments can support agriculture production while sparing forests, and therefore ensure that REDD+ finance has the greatest impact.

A recent study on [*Subsidies to Key Commodities Driving Forest Loss: Implications for Private Climate Finance*](#) (ODI, 2015) shows that subsidies for agriculture and biofuels dwarf current climate finance in support of REDD+, both globally and in countries with high levels of forest loss such as Brazil and Indonesia (see Figure 1). Brazil and Indonesia collectively provide on average \$41 billion per year in subsidies to agriculture and biofuels, compared to an average of \$323 million per year in REDD+ financing. In spite of the significant levels of agriculture subsidies in these countries and the need for reform, measurement challenges have proved to be key obstacles to progress. The study identifies 48 different domestic subsidies to support the leading causes of deforestation - palm oil and timber industries in Indonesia and beef and soy industries in Brazil – although it only uncovered estimates of the value of these subsidies for a little over half of them (see Table 1).

A recent review of REDD+ readiness finance to these countries found that there is not enough focus on identification, estimation and reform of these subsidies (Salvini et al, 2014). The majority of subsidies are not clearly identified in standard government budget documents and to date there is no detailed inventory of subsidies to key commodities driving forest loss in all countries. While some data exists on global agricultural subsidies, it is difficult to pinpoint agricultural subsidies specifically targeted at one commodity or to specifically identify subsidies that drive forest loss. It is even more challenging to find information on the value of subsidies to the forestry sector.

Figure 1. Domestic agriculture and biofuel subsidies as compared with REDD+ finance commitments (average annual \$ million)



Preliminary findings on subsidies to agricultural commodities linked to forest loss

The preliminary findings of the ODI report (2015) show that subsidies to beef and soy production in Brazil, and timber and palm oil production in Indonesia are major drivers of tropical forest loss, and their demand within global supply chains are growing. In addition it finds that subsidies are provided through a wide range of government tools, and that they are rarely specifically targeted at the commodity, but at wider economic objectives and a diverse set of beneficiaries. A summary of these findings, including where these subsidies are provided along the supply and demand chain (Figure 2) are outlined in Table 1.

Figure 2: Supply and demand chain

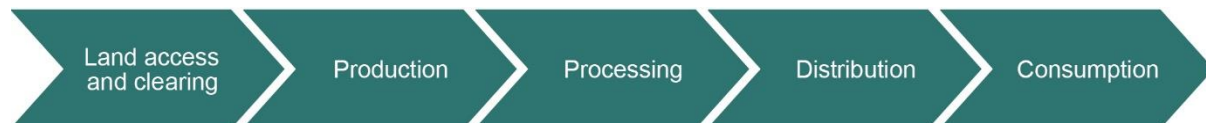


Table 1: Summary of Findings⁶

	Brazil - beef	Brazil - soy	Indonesia - palm oil	Indonesia - timber
Number of current domestic subsidies identified	8	16	19	10
Number of subsidies with value attributed	7	9	9	4
Number commodity specific	0 Wider focus on: family farming, agriculture, poorer regions, transport	1 Wider focus on: biofuels, family farming, agriculture, poorer regions, and infrastructure.	5 Wider focus on: biofuels, fertilizer, cooking fuel, agriculture and plantations, and infrastructure.	5 Wider focus on: transport, infrastructure and job creation.
Stated objectives of the subsidies identified	Regional development, reducing rural poverty and inequality, increasing productivity, strengthening family farming, accelerated investment in infrastructure.	Regional development, reducing rural poverty and inequality, increasing productivity, strengthening family farming, accelerated investment in infrastructure, energy security and reduced climate impact of energy use.	Job creation and investment, increasing domestic value added, reducing (rural) poverty, protecting local industry, increasing productivity, national fuel security, reducing users' costs.	Plantation development, forest protection, job creation.
Intended beneficiaries of the subsidies identified	Cattle farmers, marketers and processors, and investors in infrastructure.	Soy farmers, biofuel processors, soy marketers and processors, seed developers, and investors in infrastructure.	Palm oil producers and processors, oil crop producers, biodiesel industry, domestic fuel users, energy and cooking oil consumers, smallholders, and state-owned enterprises.	Plantation developers and forest concessionaires.
Type of subsidies (see figure 6)	Economic instruments: lending (debt including concessional loans), insurance, tax expenditure, direct spending.	Economic instruments: lending (debt including concessional loans), insurance, tax expenditure, direct spending. Information instruments: government funded R&D, voluntary certification Regulation instruments: fuel blending mandate).	Regulatory instruments: quotas, licenses, fuel blending mandate and planning laws. Economic instruments: lending (debt including concessional loans), tax expenditure, direct spending.	Regulatory instruments: licenses, property rights, planning laws, and quotas. Economic instruments: access to resources (concessional or for free), lending (debt), direct spending, tax expenditure.
Stage of 'supply and demand chain' (see figure 7)	Focused on production and processing, except the government investment in transport improvement (distribution).	Focused on production with some processing and also examples of distribution and support for consumption.	Focused on production, but examples found at all stages	Predominantly land access and clearing, with examples of production, and distribution.
Examples of subsidy reform (which may support REDD+)	Linking credit availability for farmers to adherence with environmental and legal criteria (BS.1).	Linking provision of subsidies to biofuel producers on conditionality of purchasing from, and providing technical assistance in sustainable techniques to, smallholders (BS.9). Linking credit availability for farmers to adherence with environmental and legal criteria (BS.1).	Proposed amendments to the EU biofuel blending mandate will set stretching indirect GHG emissions targets for biodiesel sector (IP.25).	Scrutiny of the Ministry of Forests' finances by independent bodies reforms levies (IT.6). Indonesia's timber plantation policy introduced to move investment into plantations and reduce commercial pressure on natural forests.

Opportunities for agricultural subsidy reform

The findings also highlight some measures that could reduce subsidies to agricultural commodities and create fiscal space for REDD+ initiatives. For example, Brazil has already reformed some of its agricultural subsidies, including to beef and soy, in order to address forest loss and improve environmental performance. Specifically, a legal provision, Resolution 3545, was introduced in 2008 that made the provision of rural credit subsidies contingent on meeting environmental regulations. The reform led to \$1.4 billion not being loaned between 2008 and 2011 – loans that previously would have granted to farmers that were breaking environmental regulations. Another approach is to improve revenue administration and fiscal governance in order to ensure that revenues due to the government are fully collected, thereby diminishing any subsidy effect resulting from unpaid or uncollected taxes and fees. In Indonesia, for instance, greater co-ordination between the Ministry of Environment and the Ministry of Finance could contribute to the removal of subsidies that have historically been available to Indonesian timber producers through non-collection of royalties, uncollected loans, and low levy rates on timber harvesting.

These initial country experiences could be the basis for additional reform efforts. Other opportunities for reform of agricultural subsidies could be explored. For instance, subsidies to agricultural commodities are provided through a wide range of economic and regulatory tools – such as direct spending, provision of concessional loans and tax exemptions – which can be applied in a manner that is conditional on or tailored to decreasing, rather than increasing, forest loss. In addition, subsidies could be better

⁶ The report *Subsidies to Key Commodities Driving Forest Loss: Implications for Private Climate Finance* provides detailed information on domestic subsidies identified for each commodity (beef and soy in Brazil, and timber and palm oil in Indonesia) including: number of subsidies with value attributed; type of government support (regulatory, economic, and information instruments); targeted beneficiaries; intended purpose; qualification of whether the subsidy is current or historic; year the subsidy was effective from; qualification of whether there are any lessons for reform; source (within government); annual value (\$); point applied on domestic 'supply and demand chain' (see Figure 2); and qualification of whether the subsidy is specific to the commodity, or general.

targeted so that they help increase productivity while avoiding additional forest loss, for instance by scaling up distribution of improved crop varieties and ensuring that smallholders and family farmers have access to techniques and inputs required to increase productivity such as drought tolerant crops, while limiting expansion into forests.

Conclusion

In the run up to the two global summits in 2015, namely, Financing for Sustainable Development and the 21st Conference of Parties to the UNFCCC, the issue of efficient financing for REDD+ could send an important message to the broader communities concerned. In particular, the following deserves some considerations: 1) REDD+ readiness finance can be used to support the identification, estimation and reform of subsidies to key commodities driving deforestation; and 2) REDD+ finance could also be made conditional on agricultural subsidy reform. These measures are critical steps in a transition to economic development that increases agricultural productivity while avoiding forest loss if designed and reformed with these multiple values in mind. Further on, there is a need to identify how the opportunity of providing new sources of finance can help promote and embolden reform of current expenditure and incentives that work against REDD+.

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3. Quick Links

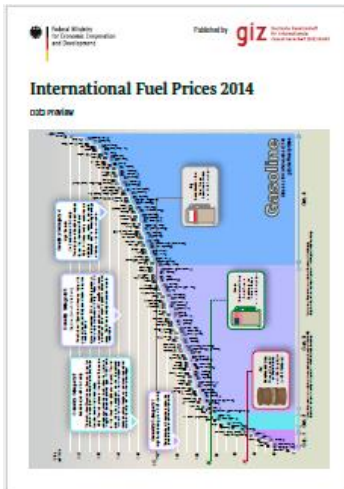
- [Green Fiscal Policy Network website](#)
 - [IMF Environment Page](#)
 - [United Nations Environment Programme \(UNEP\) Green Economy Initiative](#)
 - [GIZ Environment and Climate Change](#)
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4. What's New On The Network

Publications

The following reports are available for download on the website.

GIZ International Fuel Prices 2014



The 2014 International Fuel Prices Data Preview report provides an overview of the retail prices of gasoline and diesel in over 170 countries based on a GIZ survey undertaken in November 2014.

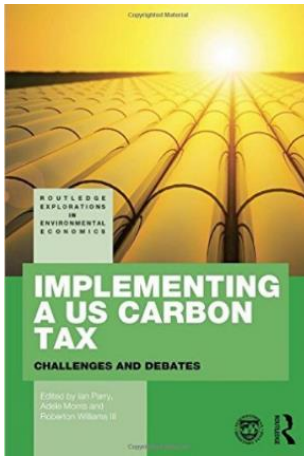
Financing Green Growth



This study highlights the role of the entire financial system in the transition to a green economy and reviews green financial sector policies in emerging and developing economies. It focuses on the political and legal framework conditions, which are essential for a successful financing for green growth. On the basis of ten case studies in emerging and developing countries, the study investigates which strategies, policies and specific policy instruments have been applied at the national level, and how these have directly or indirectly influenced the actions of organisations operating in the financial sector. The study aims to provide an analytical framework for key stakeholders (governments, donor institutions and the private sector), providing guidance before initiating and building a conducive framework for financing green growth.

Implementing a US Carbon Tax: Challenges and Debates

Although the future extent and effects of global climate change remain uncertain, the expected damages are not zero, and risks of serious environmental and macroeconomic consequences rise with increasing atmospheric greenhouse gas concentrations. Despite the uncertainties, reducing emissions now makes sense, and a carbon tax is the simplest, most effective, and least costly way to do this. At the same time, a carbon tax would provide substantial new revenues which may be badly needed, given historically high debt-to-GDP levels, pressures on social security and medical budgets, and calls to reform taxes on personal and corporate income.



This book is about the practicalities of introducing a carbon tax, set against the broader fiscal context. It consists of thirteen chapters, written by leading experts, covering the full range of issues policymakers would need to understand, such as the revenue potential of a carbon tax, how the tax can be administered, the advantages of carbon taxes over other mitigation instruments and the environmental and macroeconomic impacts of the tax. A carbon tax can work in the United States. This volume shows how, by laying out sound design principles, opportunities for broader policy reforms, and feasible solutions to specific implementation challenges.



How Large are Global Energy Subsidies? (IMF Working Paper)

IMF Working Paper

How Large Are Global Energy Subsidies?

by David Coady, Ian Parry, Louis Sears, and Baoping Shang

IMF Working Papers describe research in progress by the author(s) and are published to elicit comments and to encourage debate. The views expressed in IMF Working Papers are those of the author(s) and do not necessarily represent the views of the IMF, its Executive Board, or IMF management.

INTERNATIONAL MONETARY FUND

This study provides a comprehensive, updated picture of energy subsidies at the global, regional, and country levels. It focuses on the broad notion of post-tax energy subsidies, which captures the failure to charge for the environmental damage from energy consumption as well as to tax energy consumption in the same way as other consumption goods to raise government revenues. The study also estimates the fiscal,

environmental and welfare gains from eliminating these energy subsidies.

Country Profiles

The following country profiles are now available on the website. These profiles provide an overview of the fiscal, social and environmental situation in each country and provides information on green fiscal measures currently in place.

[Cambodia](#)

[Malaysia](#)

[Tunisia](#)

Survey

Please help us improve our website by responding to a short, 5 minute survey on our website. Your answers will help us provide resources best suited to your interests and needs. Click [here](#) to complete the survey now.

5. Recent and Forthcoming Events

July 7- 10, 2015. Training Seminar on Environmental Fiscal Reform in Latin America and the Caribbean, Chile



Representatives mainly from Ministries of Finance, Economics and Environment from 8 countries in the region participated in a capacity-building training seminar Environmental Fiscal Reform, organized jointly by the UN Economic Commission for Latin America and the Caribbean (ECLAC) and the German International Cooperation (GIZ). During the seminar, participants deepened their knowledge on approaches to Environmental Fiscal Reform (EFR) and increased their capacity to discuss and design appropriate EFR strategies in their own countries.

The seminar was complemented by a workshop that focused on the status quo and potential of EFR in Latin America and the Caribbean, where experts and researchers from the region and Germany exchanged their experiences with green fiscal policies and discussed the challenges as well as possible strategies to overcome these challenges. This event was organized through the CEPAL-BMZ/GIZ project “*Structural change for a sustainable and inclusive development in Latin America and the Caribbean*”.

More details about the event can be found at:

<http://www.cepal.org/es/cursos/curso-elementos-para-una-reforma-fiscal-ambiental-conceptos-y-metodos>

<http://www.cepal.org/es/noticias/seminario-en-la-cepal-analizara-mecanismos-de-politica-fiscal-para-combatir-el-cambio>

More information about the CEPAL-BMZ/giz project is available here:

<http://www.giz-cepal.cl/>

July 1-3, 2015. 6th International Tax Dialogue (ITD) Conference on Tax and the Environment, Paris, France

The International Tax Dialogue (ITD), a joint initiative of the European Commission (EC), Inter-American Development Bank (IDB), International Monetary Fund (IMF), Organisation for Economic Co-operation and Development (OECD), World Bank Group and Inter-American Center of Tax Administrations

(CIAT), held its 6th global conference on the topic of Tax and the Environment on 1-3 July at the OECD headquarters in Paris. The ITD facilitates international dialogue on tax policy and administration. The conference brought together 300 senior tax and environment policymakers, tax administrators and experts from more than 90 countries. One of the key messages from the conference was that environmental taxes are one of the most potent policy instruments but are not used enough. Through presentations and discussions, the conference explored how environmental taxes could be better designed, targeted and applied and the potential distributional and competitive concerns that can arise from their use. For more information on the conference, including full presentations, please visit this website: <http://www.itdweb.org/2015conference/>.

UNEP Session on Fiscal Policy at the European Development Days, Brussels, 3-4 June 2015

At the 15th edition of the European Development Days (EDD15), held in Brussels, Belgium from 3-4 June, UNEP hosted a policy lab on *Fiscal Policies for an Inclusive Green Economy: Lessons Learnt from Africa*. This lab focused on green fiscal policy reforms in Africa based on two UNEP-commissioned country studies on Mauritius and Ghana, although the discussions drew on global experiences and was framed in the broad context of financing for sustainable development. The objectives of the session were to stimulate reflection and discussion on how fiscal policy reforms can mobilize domestic public resources for a green economy transformation. About 40 people participated in the session. See full event description [here:](http://www.unep.org/greeneconomy/News/UNEPSessiononFiscalPolicy/tabid/1060233/Default.aspx)
<http://www.unep.org/greeneconomy/News/UNEPSessiononFiscalPolicy/tabid/1060233/Default.aspx>

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- Send us information about recent and forthcoming events related to green fiscal policy
- Submit up-to-date information on initiatives and projects related to green fiscal policy in different countries
- Contribute a guest article to be featured in this newsletter

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