

# **UNITED NATIONS CONFERENCE ON SUSTAINABLE DEVELOPMENT**

## **Tax and Subsidy Reform for a Greener Economy: Experiences and Lessons from the Asia and Pacific Region**

**Rio De Janeiro  
21 June 2012**

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**ADB**

# Introduction

After the *Stockholm Conference* of 1972 and especially after the Rio *Earth Summit* of 1992, most countries of the region have put in place institutions, laws, and regulations to protect the environment.

Most of these have been of a **command-and-control nature**. Despite these institutional steps Asia's growth remains resource and energy intensive with severe **environmental degradation** processes.

There is increasing recognition that implementation of C&C measures and regulations should improve. Further, there is wide support to expand the use of market based instruments .

Several countries have piloted/adopted economic instruments esp. in the last 2 decades. New initiatives and studies – some supported by the Asian Development Bank – have taken place.

This presentation presents a summary of key messages from a brief review of this experience.

# **Tax and Subsidy Reform in Asia and Pacific: Key Messages**

## **Message 1**

**The political economy associated with tax and subsidy reform is multi-faceted and complex.**

**By disturbing the status quo, tax and subsidy reform will have different impacts (some positive, some negative) on different groups of people**

# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 1

### Korea cap and trade

On May 2 of this year, South Korea has adopted a cap-and-trade program to reduce greenhouse gas emissions (starting in 2015).

The objective is to reduce these emissions by 30% by 2020 compared to a business-as-usual scenario.

The Federation of Korean Industries and the Korea Chamber of Commerce & Industry asked the government to delay introducing the plan, saying it will increase costs and make industry less competitive against countries that don't impose charges on emissions.

Most permits are expected to be distributed free of charge.



# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 1

### Fuel subsidies

	<b>Average subsidization rate (%)</b>	<b>Subsidy as % of GDP</b>
<b>Bangladesh</b>	<b>46.1</b>	<b>4.8</b>
<b>China</b>	<b>3.8</b>	<b>0.4</b>
<b>India</b>	<b>13.5</b>	<b>1.4</b>
<b>Indonesia</b>	<b>23.2</b>	<b>2.3</b>
<b>Malaysia</b>	<b>20.0</b>	<b>2.4</b>
<b>Pakistan</b>	<b>28.9</b>	<b>4.2</b>
<b>Philippines</b>	<b>7.3</b>	<b>0.6</b>
<b>Thailand</b>	<b>20.7</b>	<b>2.7</b>
<b>Turkmenistan</b>	<b>65.1</b>	<b>19.3</b>
<b>Uzbekistan</b>	<b>57.1</b>	<b>30.5</b>
<b>Viet Nam</b>	<b>14.4</b>	<b>2.8</b>

# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 1

### Indonesia: Fuel subsidies

Fuel subsidies cost government budget USD 15 billion in 2010, representing approximately 15% of the country's budget.

On January 30, 2012, the government announced a plan to reduce fuel subsidies and raise the price of gasoline and diesel by 33% by April 1, 2012.

On March 31, the price increase was made contingent on conditions which are unlikely to be met in the short-term.



# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 2

**Tax and subsidy reform: Necessary but not sufficient to achieving a green economy.**

**Mix of instruments is needed, including among others:**

- regulation;
- economic (market-based) instruments;
- voluntary compliance measures;
- green procurement policies; and
- information-based tools.

**Role of the judicial system, such as:**

- Green Benches (Thailand);
- Environmental courts (Philippines).

**Challenge: To identify the appropriate mix of instruments.**

## **Tax and Subsidy Reform in Asia and Pacific: Key Messages**

### **Message 3**

**Tax and subsidy reforms have generally not been adopted for the explicit purpose to create incentives for environmental protection investments and the promotion of resource use efficiency.**

**Key interest is potential contribution to state budget: Increasing fiscal revenues in the case of instruments such as pollution discharge fees or taxes; or reduced fiscal expenditures in the case of the removal of perverse subsidies.**



# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 3

Pollution fees have been adopted in many countries of the region.

### Existing fees include:

Malaysia (mid-1970s)

China

- 27 localities (1979)
- Nationwide (1982)

Philippines

- Laguna Lake (1997)
- Nationwide (2004)

Viet Nam (2005)

### Possible fees include:

Thailand (Royal Decree on Economic Instruments on Pollution Control – with ADB support)

Lao PDR (Decree on Environmental Taxation)

Viet Nam (Circular on air pollution fees)

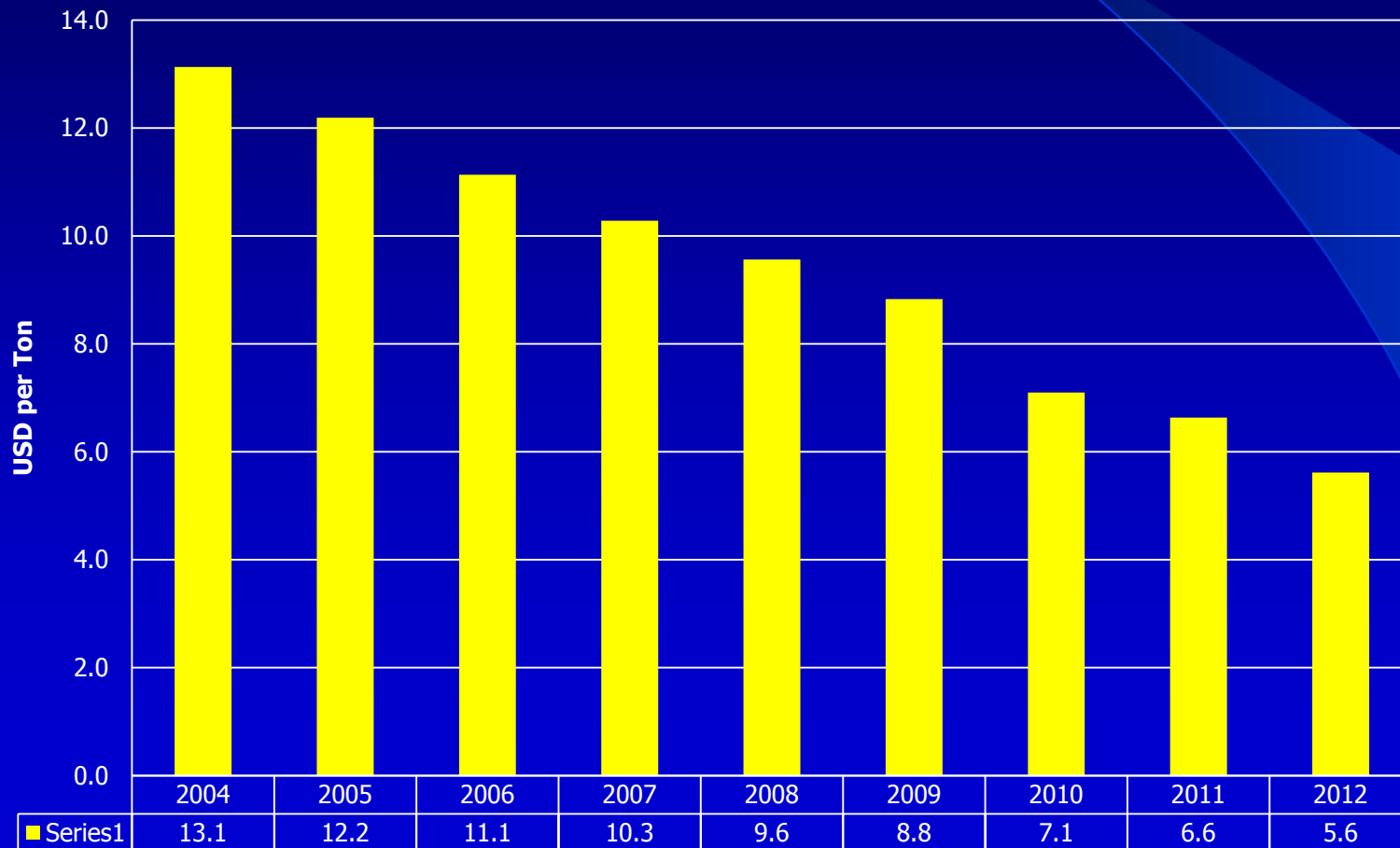
Indonesia (identifying most promising instruments)

However, fees are: (1) too low; or (2) not adjusted for inflation; or (3) not strongly implemented.

# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 3

Wastewater Fees in Viet Nam (TSS): USD/ton 2004 dollars



# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 3

**Insufficient attention to ensuring the effective implementation of economic instruments once signed into law.**

**Effective implementation of many EIs requires:**

- **Institutions which are adequately resourced;**
- **Institutions which can act independently from the political process;**
- **Reliable reporting mechanisms; and**
- **Strict penalties for non-compliance.**

**In other words: the adoption of economic instruments cannot be a substitute or alternative to strong and capable institutions.**

# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 4

No revenue-generating economic instrument for pollution control has thus far been implemented with the explicit purpose of using the generated revenues to reduce other forms of distorting taxes, as suggested by the double dividend literature.

As noted in a report of the UN ESCAP, in almost all cases, fiscal revenues generated through the adoption of environmental fees or taxes have been earmarked to:

- recover the costs of providing an environmental service (such as solid waste fees being used to fund solid waste collection and disposal);
- support capacity building of environmental agencies; or
- provide financial assistance to environmental investments through the creation of environmental funds.

## **Tax and Subsidy Reform in Asia and Pacific: Key Messages**

### **Message 5**

**In the context of climate change and the mitigation of greenhouse gases, Asia and the Pacific region is showing leadership with the implementation of market-based instrument.**

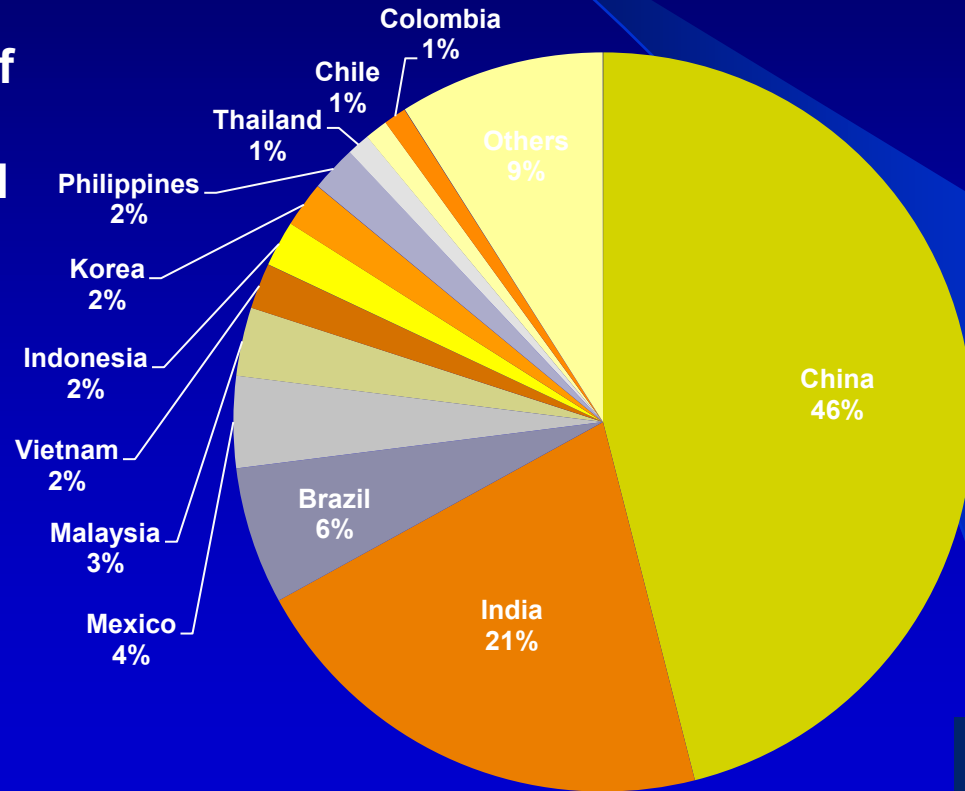
**Countries of the region have been key partners of the CDM. ADB is working closely with UNFCCC and other partners to build CDM access capacity of our least developed member countries, including through the management of 2 carbon funds.**

# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 5

Countries of the region have been key partners of the CDM. ADB is working closely with UNFCCC and other partners to build CDM access capacity of LDCs, including through the management of 2 carbon funds.

## Regional Distribution of CDM Projects (by Host party)



Source: CDM Annual Report (2011)

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# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 5

**REDD+:** New market-based approach to forest conservation. It's particularly important to a few Asian countries like Indonesia and PNG, as the majority of their GHG emissions come from deforestation and land use change.



# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Message 5

**Carbon markets.** ADB is supporting China develop a cap-and-trade pilot project covering 7 provinces or municipalities leading to the introduction of a nation-wide carbon market by 2014.

China, India, Indonesia, Viet Nam and Thailand are members of the *Partnership for Market Readiness* supported by ADB. This program aims to prepare countries in future carbon market instruments and emissions trading mechanisms aimed at abating greenhouse gases.





# Tax and Subsidy Reform in Asia and Pacific: Key Messages

## Conclusions

The Asia and Pacific region is rich with policy initiatives consistent with tax and subsidy reform. The region is also a key global player in the on-going effort to implement market-based instruments

However, we cannot really talk of a clear and strong commitment to implement a structured agenda for tax and subsidy reform.

Even with a policy and economic framework geared towards green growth, actual tax and subsidy reform can still fall short due to such factors as institutional limitations.

Overcoming challenges of governance and management will require strong legal and institutional frameworks, backed by political will, leadership, and a governance environment that fosters transparency, accountability and stakeholder consultations.

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