Subsidies to fossil fuels in South Africa

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Introduction to fossil fuel subsidies

- subsidies are technically and politically complex
- Historically, we have built the high coal dependency seen in South Africa through active choices to support producers
- Often framed as vital or strategic investments to support economic development - not subsidies to fossil fuels.
- Scale of subsidies is not well known, and much of the detail is obscured or hidden. (long running and lack of data transparency)
- Hence no national debate around their role in economic development (contrasted against mitigation policies such as carbon taxes or REIPPPP)
- Since not defined as fossil fuel support, the implications are not always clear in terms of costs/benefits, trade offs, emissions, etc

https://www.cambridge.org/core/books/politics-of-fossil-fuel-subsidies-and-their-reform/B8CB7D383F33AD9AF9CC82EB50A74DE5

Definitions for different purposes

- **Price gap approach (IEA)**

The IEA (1999) defines an energy subsidy as "any government action that concerns primarily the energy sector that lowers the cost of energy production, raises the price received by energy producers or lowers the price paid by energy consumers."
E.g. does the subsidy change prices compared to international markets? Calculate the total difference e.g. oil producers who provide below market fuel (opportunity cost or subsidy?)

- **vs Inventory (OECD or WTO)**

List of mechanisms used for subsidisation (e.g. a tax credit; direct transfers, government support etc)
OECD: producer, consumer and total support estimates
- resource limits constrain this analysis

- **Vs. IMF approach**

highly divergent; looks at externalities like air pollution, congestion, accidents, etc: $5trillion or so of which coal is 44%

WTO Agreement on Subsidies and Countervailing Measures (ASCM)

A subsidy shall be deemed to exist if:

(a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as “government”), i.e. where:

(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);

(ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);

(iii) a government provides goods or services other than general infrastructure, or purchases goods;

(iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments; or

(a)(2) there is any form of income or price support in the sense of Article XVI

of GATT 1994;

and

(b) a benefit is thereby conferred.

Definitions – political challenges

- Highly divergent depending on chosen definition and much disagreement
- A narrow(er) definition has less disagreement methodological uncertainty
- Internationally, highly political (trade law)/legally binding
- Existence of a subsidy and it’s efficiency and welfare evaluations should be separated (eg LPG or FBE consumer subsidies may exist, but may actually confer a public benefit)
- “The interest groups that demand subsidies are usually well organized and the provision of a subsidy usually makes those groups even more aware of their interest in sustaining the subsidy policy” (Victor, 2009: 10).
- Versus widespread social benefits conferred from different/new subsidies?

Definitions – technical challenges

- No agreement on definition or estimation techniques
- Once defined, still need agreement on consistency of calculation – e.g. how to treat interest rates, what portion of x is a subsidy, etc.
- Arcane and complex debates in teams on e.g. how to cost concessional loans and the counterfactuals, while data limitations mean partial or prevents some kinds of analyses
- Complex interactions between subsidies making beneficiaries difficult to disentangle (e.g. in SA: production and consumption hodge podge in Eskom)
- Not collected by government: SA claims “no inefficient subsidies” at G20
- ENE, budget reviews, income tax acts/amendments, annual reports (gov deps and firms) – tracing requires man-years to analyse and track and calculate

Historical support

- The history of coal mining, Eskom, large energy users, and Sasol are littered with support measures and **management of rents for economic development**
- key drivers of subsidies include apartheid-era industrial and energy policies that have become locked in over time
- Prescribed assets, regulatory guarantees, import parity pricing plus, windfall profits never taxed, uplift for CTL production, government guarantees for Eskom foreign loans in 1980s, etc
- (plus low social or environmental compliance costs during apartheid)
- And more opaque – coal contracting models and allocations
- These have persisted in various forms

https://open.uct.ac.za/handle/11427/27233

https://www.cambridge.org/core/books/politics-of-fossil-fuel-subsidies-and-their-reform/sustaining-carbon-lockin/9AC7F2DA4AB31EB649EE84EA58C3708B

Direct transfer or potential direct transfer of funds	Government revenue foregone	Government-provided or government-purchased goods or services	Income or price support, or relief from normal costs or procedures
Direct payments	Tax expenditure: reduced tax rates, exemptions, rebates	Under-pricing of government-provided goods or services	Above-market rate prices for producers via government regulations or import barriers
Grants	Accelerated depreciation allowances	Government-provided infrastructure specific to the sector	Consumption mandates
Government loans provided at below-market rates	Reduced royalty payments		Export taxes or restrictions
Guarantees for loans, security or credit			Relief from costs enterprises normally bear in the course of business (eg social or environmental)
Government spending on research and development Assumption of liabilities for closure and post-closure risks			

Subsidy estimates 2007-2015

And what about public finance?

Table 13.1 *Annual subsidy estimates by category for South Africa*

Subsidy category	2007	2008	2009	2010	2011	2012	2013	2014	2015
Direct transfers	–	830	830	1,001	169	134	12.8	17.0	1,707
Government revenue foregone	24.3	18.8	126	397	506	512	566	578	267
Sasol market price support	[a]	[a]	[a]	[a]	[a]	127	[a]	[a]	[a]

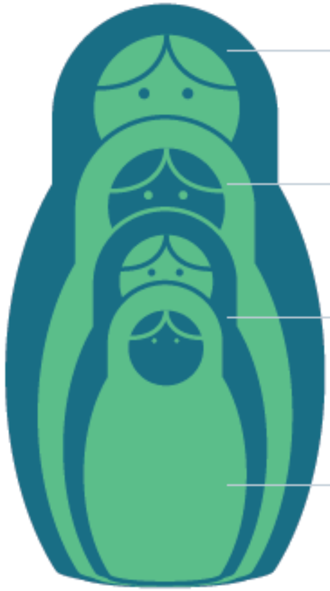
Note: All amounts in 2016 USD million.
[a] No transfers for that subsidy in a given year or lack of data.
Source: Authors' calculations; Lott 2016; see Lott et al. 2016 for assumptions.

https://www.cambridge.org/core/books/politics-of-fossil-fuel-subsidies-and-their-reform/sustaining-carbon-lockin/9AC7F2DA4AB31EB649EE84EA58C3708B

IISD analysis on production support in liquid fuels: historical and current

Figure 1. **Subsidies to Sasol**

Support Measures for Sasol



Support measure	Years	Type	Amount (in billion rands)	Source
Carbon Tax Exemption	2019	Non-internalized externalities	6.7- 6.9	IISD, 2020
Fuel pricing	2012 - 2019	Market Price Support	12.6	IISD,2020; Lott, 2017
Windfall profits of Equalisation Fund	1989 - 1995	Taiiff Protection	3.7	Rustomjee et al., 2017
Main Supply	1970 - 2003	Market Access guaranteed by the Government	NA	Sasol Limited, Eugen Limited, Petronas International Corporation Limited and Sasol Oil (Pty) Ltd, Eugen Ltd. (2006).

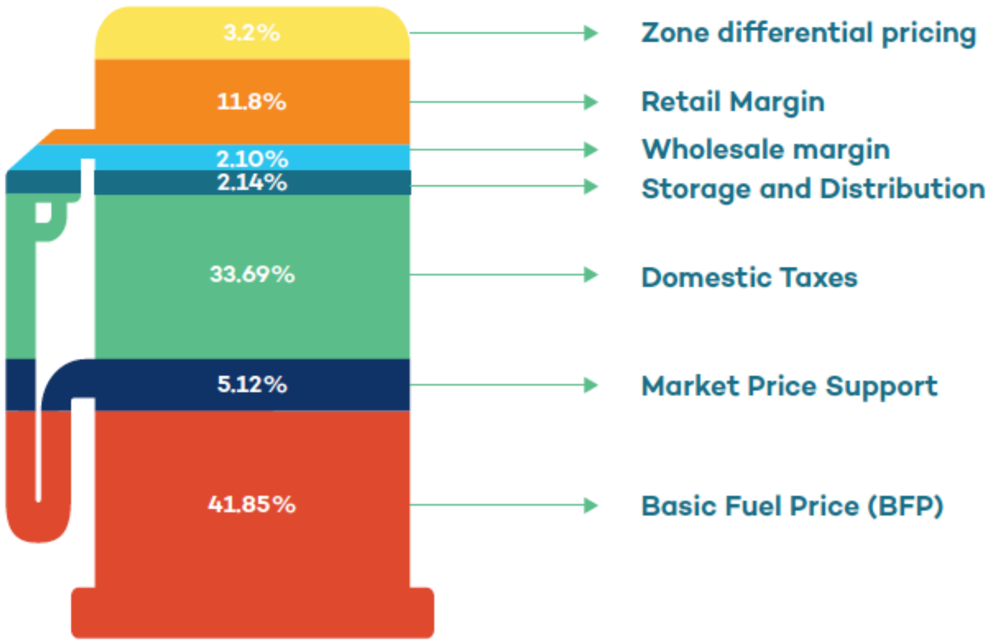
https://www.iisd.org/publications/subsidies-south-africa-coal-based-liquid-fuel-sector

Market price support

Table 1. MPS to Sasol

Year	MPS (billion rand)	MPS (million USD)
2019	1.55	107
2018	1.55	117
2017	1.60	115
2016	1.64	107
2015	1.63	123
2014	1.61	142
2013	1.57	116
2012	1.50	110
Total	**12.65**	**938**

Figure 2. MPS per litre of synthetic fuel

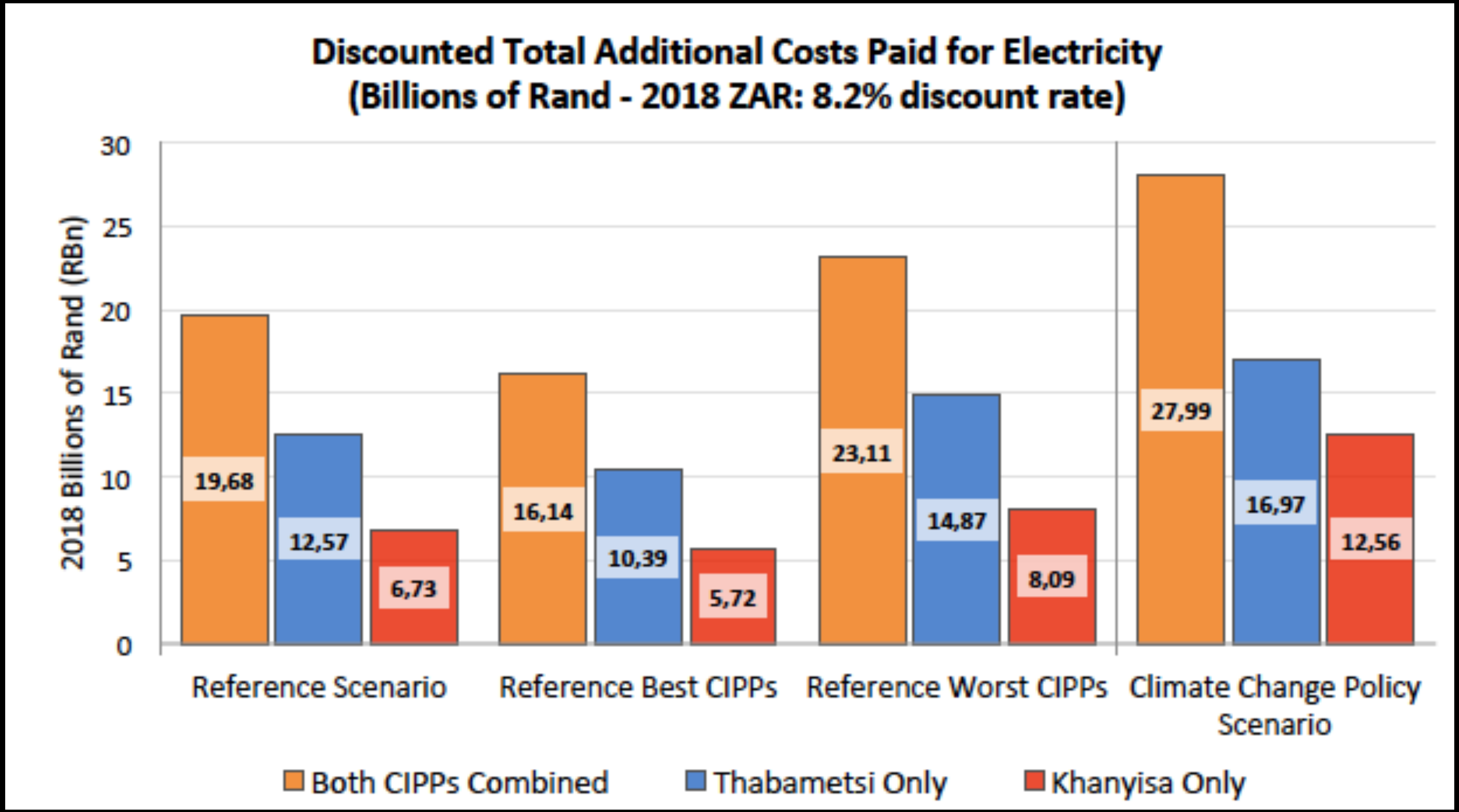


Source: PetroConnect, 2018.

https://www.iisd.org/publications/subsidies-south-africa-coal-based-liquid-fuel-sector

Coal IPPs

- Transfer from consumers to producers of between R19-28bn for coal IPPs (vs least cost and cost optimal low-PPD)
- A subsidy or is coal just more expensive?
- A policy adjustment above market prices via regulated process
- Policy-adjustment to support coal producers who could not otherwise enter the market and raises costs for consumers



https://cer.org.za/wp-content/uploads/2018/05/ERC-Coal-IPP-Study-Report-Finalv2-290518.pdf

How does this connect to Just Transition?

- The structure of the economy was actively built up over many years through the use of subsidies and regulations, carrots and sticks, and informal relations between the state and business
- Unpicking this is not politically easy –support for the existing subsidy regime persists (why? Not on the political agenda? Actively opposed? Too complicated?)
- Transition to a low carbon, climate resilient economy that is sustainable and inclusive means altering the structure of the economy and the flows of support that maintain the carbon-intensive, energy-intensive, and low-labour absorbing economy that we have today
- What is “vital” and “strategic” needs to be reframed. New subsidies may be more visible than the historical support that built these industries
- There is historical precedent for this but we need to actively pursue a new model of development that prioritises employment creation, socio-economic development, social protection, decarbonization, and economic diversification

Thank you

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