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RADIX

CENTRE FOR  
BUSINESS  
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SOCIETY

FROM FOSSIL FUEL  
SUBSIDIES TO  
AN EFFECTIVE  
TRANSITION





"PUBLIC POLICY IS A  
STUDY IN IMPERFECTION.  
IT INVOLVES IMPERFECT  
PEOPLE, WITH IMPERFECT  
INFORMATION, FACING  
DEEPLY IMPERFECT  
CHOICES."

Jake Sullivan

"THERE IS NOTHING MORE  
DIFFICULT TO TAKE IN  
HAND, MORE PERILOUS  
TO CONDUCT, OR MORE  
UNCERTAIN IN ITS SUCCESS,  
THAN TO TAKE THE LEAD IN  
THE INTRODUCTION OF A  
NEW ORDER OF THINGS."

Niccolò Machiavelli

# FROM FOSSIL FUEL SUBSIDIES TO AN EFFECTIVE TRANSITION

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## ABOUT RADIX

The RADIX Centre for Business, Politics and Society is a non-aligned, non-for-profit think tank focused on aligning public policy with responsible business. We are a platform for innovative, radical public policy approaches that help business be a positive force in our societies.

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Radix Brand and Layout:  
Mark Huddleston

CONTACT US at  
[Ron.Soonieus@radixcbps.org](mailto:Ron.Soonieus@radixcbps.org)

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RADIX remains, of course, solely responsible for the overall content, analyses and recommendations in this report.

### RADIX Project Team

**David Boyle, Fritz Lietsch, Kai Platz, Ben Rich, Nick Silver, Ron Soonieus, Mike Tuffrey, Leon Wansleben, Lesley Yarranton, Joe Zammit-Lucia**

### UK

#### **Duncan Brack**

Former special advisor at the Department for Energy and Climate Change. Associate Fellow, Chatham House Environment and Society Programme

#### **Sir Ed Davey MP**

Leader of the Liberal Democrats and former Secretary of State for Energy and Climate Change

#### **Sir Vince Cable**

Former Secretary of State for Business, Innovation and Skills. Professor in Practice, London School of Economics and Political Science

#### **Chris Huhne**

Former Secretary of State for Energy and Climate Change. Chairman, Europe, Zilkha Biomass

#### **Craig Mackinley MP**

Chair of the Conservative Net-Zero Scrutiny Group

#### **Valerie Marcel**

Associate Fellow at Chatham House. Government adviser on petroleum and energy policy

#### **Baroness Kate Parminter**

Spokesperson for Environment, Food and Rural Affairs in the House of Lords

#### **Benny Peiser**

Director of Global Warming Policy Foundation and of Net Zero Watch

#### **Jack Richardson**

Senior Climate Programme Manager for the Conservative Environment Network

#### **Nigel Topping**

Key UK negotiator and UN champion of environmental activity at COP26

#### **Unnamed\***

Non-Executive Director for the Department of Business, Energy and Industrial Strategy

#### **Unnamed\***

Adviser to the Department of Business, Energy and Industrial Strategy

## GERMANY

#### **Andreas Burger**

Federal Environmental Agency. Author of report on environmentally harmful subsidies

#### **Nadine Heselhaus**

Social Democrat Party. Committee on the Environment, Nature Conservation, Nuclear Safety and Consumer Protection

#### **Dieter Janecek**

Green Party. Committee for Climate Protection and Energy

#### **Carlos Kasper**

Social Democrat Party. Member of the Bundestag

#### **Andreas Lenz**

CSU. Committee for Climate Protection and Energy

#### **Barbara Metz**

Executive Director Deutsche Umwelthilfe (German Environmental Aid)

#### **Simone Neumann**

CSU. Leader of informal group advising the party on energy transition questions

#### **Ingrid Nestle**

Green Party. Committee on the Environment, Nature Conservation, Nuclear Safety and Consumer Protection

#### **Bastian Neuwirth**

Greenpeace. Climate expert

#### **Franzjosef Schafhausen**

Former Head of Department for Climate Protection, Federal Ministry for Environment.

#### **Unnamed\***

Member of Bavarian State Parliament

#### **Unnamed\***

Member of the Bundesrechnungshof (German Court of Auditors)

## OTHER

#### **Dr Roland Kupers**

Author - 'Complexity and the Art of Public Policy' and 'A Climate Policy Revolution: What the science of complexity reveals about saving the planet'. Global Advisor UNEP - International Methane Emissions Observatory.

#### **Maria van der Hoeven**

Was Vice Chairwoman of the former High-level Panel of the European Decarbonisation Pathways Initiative within the European Commission. Senior Fellow, Clingendael International Energy Programme.

\*Due to the sensitive nature of their current positions, these individuals agreed to speak to us on condition that they were not specifically named.

# 1. SUMMARY AND CONCLUSIONS

The objective of this project was to investigate why 'fossil fuel subsidies' exist, are so sticky and, in some cases, increasing. This despite the cost to governments and continuing pressures from climate activists for their removal. Our findings are based on a combination of analysis of existing data and the practical experiences and opinions shared with us by those with real-world experience of dealing with these questions at the policy level. Our conclusions represent a synthesis of these investigations and conclusions and inferences we have drawn from our inquiry many of which go beyond the narrower questions surrounding fossil fuel subsidies.

There is little doubt that the climate movement has been successful in raising climate change up the political agenda. In both the UK and Germany (the countries of focus of this analysis), and likely in other countries, the challenges lie in:

- *navigating the practical, on the ground, country-by-country implementation given the political realities and the different political imperatives, practicalities, trade-offs and compromises necessary in different countries*
- *improving and maintaining public support for climate-friendly action given other, more immediate and more acutely felt voter concerns as well as voter resistance to the practical implementation of some climate policies*
- *ensuring that environmental issues are not approached through the narrow lens of 'environmentalism' but through an understanding of their interaction with multiple other policy areas*

The elimination of fossil fuel subsidies is one of the elements facing these challenges.

However, the challenges apply to most aspects of climate policy. They will likely apply with even more force to other environmental issues such as biodiversity preservation and restoration given that 'biodiversity' remains even more of an abstract concept than climate in voters' minds.

The current energy crisis offers significant opportunities to achieve an energy transition over the medium to long term. Success requires a significant shift in the overarching narrative and supplementing current actions and approaches with significantly more granular and politically workable approaches on a country-by-country basis. Extending the excellent technical and technocratic work that already exists to add approaches that facilitate political pathways to change.

## 1.1 THE FRAMEWORK

The war in Ukraine has brought to the fore what have always been government priorities in the energy market. In order of priority for policy making:

1. ***'Keep the lights on' (supply, distribution, energy security)***
2. ***Protect vulnerable groups and industries***
3. ***Maintain broad public support***
4. ***Do the above in as an environmentally friendly way as possible***

The 'energy trilemma' – security of supply, affordability, sustainability is challenging to navigate and has been thrown into disarray by geopolitical developments.

IF INFLUENCING PUBLIC POLICY IN ENERGY MARKETS IS TO BE SUCCESSFUL, ACTIONS AND SUGGESTIONS NEED TO ALIGN WITH THE ABOVE POLICY FRAMEWORK

## 1.2 'FOSSIL FUEL SUBSIDIES' DO NOT STAND ALONE

From a policy perspective, fossil fuel subsidies (FFS) do not stand alone. They are part of a complex mix of energy, industrial, social and environmental policies. Politically and practically, this implies multiple trade-offs and pressures coming from different interests and government departments that often pull in different directions.

These issues are more marked in Germany where power is more dispersed, coalitions are the norm, ministers have to balance their own party's demands with national policy initiatives, and individual government departments have stronger veto powers. In the UK power is more concentrated in the Treasury and with the Prime Minister – which has its own issues.

In the UK, the term 'fossil fuel subsidies' has very little resonance in policy circles. Rather the subsidies in place are seen as a part of social policy (eg. supporting particular groups such as farmers and fishermen) or fiscal/economic policy (eg. subsidies for North Sea oil exploration are seen as producing greater fiscal/economic returns than the cost of the subsidies). Nevertheless, the UK has made more progress towards net-zero goals than have most other comparable countries.

In Germany, FFS are explicitly part of the policy discussion and have been addressed in multiple reports from various governmental and non-governmental sources. Despite that, at around €35bn, FFS in Germany (direct subsidies and tax expenditures) remain significantly higher than in the UK (around £14bn)<sup>1,2</sup>. This is significantly but not exclusively driven by the greater degree of industrialization in Germany where energy subsidies for industry are seen as essential to maintaining industrial competitiveness.

○ AN APPROACH THAT IS PERCEIVED AS 'ENVIRONMENTAL ACTIVISM,' NARROWLY FOCUSED AND TRYING TO PRIVILEGE ENVIRONMENTAL POLICY OVER OTHER POLICY OBJECTIVES WILL HAVE LOWER CHANCES OF SUCCESS

## 1.3 BETTER CAMPAIGNING

### A. Improving the Political Framing

It needs to be recognized that policy making is, ultimately, a political exercise not a purely technocratic one. It involves difficult trade-offs between multiple and often conflicting areas of policy. Success depends on successfully navigating political pathways to action – pathways that differ in different countries and at different times.

*"You need to think about the politics - the fact that losers scream more than winners applaud,"* said one former UK minister.

○ POLICY MAKING IS PRIMARILY A POLITICAL PROCESS AND NEEDS TO BE APPROACHED AS SUCH TO BE SUCCESSFUL

○ TO BE EFFECTIVE, CAMPAIGNING AND POLICY WORK NEEDS TO SHIFT THE FOCUS FROM FFS (AND ANTI-FOSSIL FUEL RHETORIC IN GENERAL) TO PRACTICALLY AND POLITICALLY VIABLE WAYS TO ACHIEVE AN ENERGY TRANSITION THAT ALSO MEETS THE OTHER POLICY GOALS THAT GOVERNMENTS ARE TRYING TO ACHIEVE

1 UK and German figures are, for various reasons, not directly comparable and should only be considered to compare broad orders of magnitude.

2 All figures exclude recently announced energy support payments in response to the energy crisis sparked by the conflict in Ukraine

Largely due to the historical strength of environmental movements, the Green Party's success, and significant industry interests in the renewables sector, environmental campaigning and lobbying in Germany is more sophisticated than it is in the UK where environmental activism, while much improved, remains somewhat on the outside looking in when it comes to public policy. The number of UK Members of Parliament who take environmental issues up as their main area of interest remains small. Some others have made scrutiny of 'excessive' environmental action an area of focus.

Performative activism (Extinction Rebellion, etc.) has an important role to play in maintaining climate issues on the political agenda. The challenge is to calibrate such activism so that it works to maintain and increase public and political support for policy intervention rather than alienating voters and making individual politicians cautious about publicly supporting such action. What social psychologists have long called 'the activists' dilemma.'

- ENERGY POLICY IS COMPLEX AND POLITICALLY HIGHLY CHARGED
- THE CHALLENGE FACED IS TO IMPLEMENT PRACTICALLY VIABLE ENERGY TRANSITION POLICY THAT ALSO MAINTAINS PUBLIC SUPPORT
- BOTH IN GERMANY AND THE UK, ENVIRONMENTAL ISSUES (AND ACTIONS) STILL NEED TO BE FRAMED BETTER POLITICALLY IF INDIVIDUAL POLITICIANS ARE TO SEE THEM AS A POLITICAL PLATFORM THAT WILL APPEAL TO THEIR VOTERS COMPARED TO OTHER VOTER CONCERNS
- WHILE VOTERS SUPPORT CLIMATE POLICY IN THE ABSTRACT, THEY ARE OFTEN OPPOSED TO SPECIFIC POLICIES THAT ADVERSELY IMPACT THEIR EVERYDAY LIFE
- THAT SAID, AS MORE COMPANIES HAVE INCREASING STAKES IN ALTERNATIVE ENERGY SOURCES BOTH IN THE UK AND GERMANY, FORCES DRIVING FOR CHANGE CONTINUE TO INCREASE
- THE OVERALL RESULT IS THAT WHILE THERE IS A HIGH DEGREE OF AGREEMENT ON THE OVERALL OBJECTIVE (TO REACH NET-ZERO), THERE IS MUCH LESS AGREEMENT ON THE SPECIFICS OF CONCRETE ACTIONS – FROM THE DISTRIBUTION OF COSTS, TO TECHNOLOGICAL CHOICES, TO THE DESIGN OF ENERGY MARKETS, TO THE ROLES OF PUBLIC VERSUS PRIVATE ACTORS IN KEY TRANSITION PROCESSES
- THERE IS A NEED TO ENGAGE WITH THE CONFLICTS INHERENT TO DIFFERENT AREAS OF POLICY ACTION RATHER THAN POINTING POLICY MAKERS TO THEIR FAILURES IN MEETING HIGHLY ABSTRACT, AND TO SOME EXTENT DECOUPLED, CLIMATE POLICY OBJECTIVES.

One significant danger on the horizon is that climate change risks becoming an issue of political identity and becoming enveloped in the current culture wars. If allowed to happen, this will make climate policy more politically challenging.

## B. Greater Granularity and Realism

While it is true that issues like climate change are global problems, in the end, all policies have to be interpreted and implemented nationally (see below). The hard work of how this can happen – particularly to include the political and practical compromises that inevitably have to be made – could do with receiving more attention.

One high-level climate negotiator we spoke to urged a move away from ‘generic abstracts’ as these are ‘not helpful’ for policy. He describes ‘lazy campaigning’ and ‘not doing homework’.

Much work in the environmental field is technically detailed and highly sophisticated. Where improvement would be helpful is in looking at the issues through a broader set of lenses, integrating the demands of other, overlapping policy areas that may pull in opposite directions, and focusing on how suggested initiatives can be shown to improve voters’ lives in the short term as well as benefiting future generations.

Of course, the temptation is to believe that environmental issues are so existential in nature that they should take precedence over other areas of policy. Some have even suggested that environmental policy should be ‘independent’ of political considerations along the same model as the ‘independence’ granted to monetary policy. In a democracy, there is no mileage in such an approach. Trade-offs are inevitable. The skill is in pre-working such tradeoffs to improve the result.

One also has to take account of the administrative mechanisms that are in place when considering policy options. For instance, many economists claim that if one is to support, say, farmers, then it is more economically efficient to give them cash subsidies rather than, as in the UK, subsidise their diesel.

While that may be true in the world of economic theory, the realities are that it is administratively much more practical to subsidise their fuel than to implement individual cash subsidies – an action that would also raise its own political difficulties.

In addition, there is the risk of becoming captured by one’s own biases and beliefs that may not reflect the political and practical realities on the ground.

### FALSE MEMES

Germany still subsidises travel to and from work using automobile transport. A favourite meme is that this is due to the lobbying power of the auto industry. The reality is that a clause in the German constitution is interpreted as establishing such subsidies as a right. Changing constitutions is not straightforward.

In the UK, there is a widespread belief that action on climate is held back by the lobbying power of the fossil fuel industry. This is simply untrue. As a former Secretary of State put it “I found discussions with the oil industry generally sensible and productive. Politically we were much more concerned by groups such as road hauliers that have the power to bring the country to a halt, much like the *gilets jaunes* did in France.”

- ENVIRONMENTAL CAMPAIGNING SHOULD EXPLORE FRAMINGS THAT ARE MORE POLITICALLY APPEALING AND ABANDON FALSE MEMES THAT, WHILE APPEALING TO CAMPAIGNERS, ARE PRACTICALLY INEFFECTIVE
- FUTURE WORK NEEDS TO BE SIGNIFICANTLY MORE GRANULAR AND GROUNDED IN THE POLITICAL AND PRACTICAL REALITIES OF LOCAL CONDITIONS
- THIS APPLIES NOT ONLY TO CLIMATE BUT ALSO TO OTHER, EVEN MORE CHALLENGING AREAS SUCH AS BIODIVERSITY



### C. Trans-National Issues Also Require Local Action

Some issues need to combine a trans-national focus with the practicalities of local implementation.

The UK, for example, supported a plan by the International Civil Aviation Organisation (ICAO) to create a level playing field on emissions and tax equalisation, but the EU (and individual Member States) has been hesitant, and the key initiatives were blocked by the USA and China. These same trans-national tensions are ever-present in successive COP meetings – and seem to be becoming more antagonistic every year.

Such issues cannot be resolved exclusively through top-down pressure exerted by global bodies. Nor is castigating the laggards particularly effective – especially when the laggards are as powerful as the US and China. Such issues can only be unblocked (when they can) by working at the local level with those countries and finding approaches that work for them.

This creates a tension between the headline that climate is a global problem that can only be resolved globally and the reality that such a headline may not resonate in individual countries and, in some cases, is used as an excuse for local inaction (what we do is not worth it if others are not doing it too).

THERE IS A NEED TO COMPLEMENT THE TOP-DOWN APPROACH OF BROAD, GLOBALLY-FOCUSED TRANS-NATIONAL VISION AND POLICY IDEAS WITH MORE DETAILED BOTTOM-UP EFFORTS TARGETED AT INDIVIDUAL NATION STATES UPON WHICH TRANS-NATIONAL AGREEMENTS CAN BE BOTH BUILT AND IMPLEMENTED<sup>3</sup>

### 1.4 THE OPPORTUNITY CREATED BY THE ENERGY CRISIS

*“Vladimir Putin’s abhorrent war in Ukraine and rising energy prices across the world are not a reason to go slow on climate change – they’re a reason to go faster”*

**Rishi Sunak, UK Prime Minister**

In the short term, the energy crisis created by the Ukraine conflict has led to increased subsidies and other support for fossil-fuel driven energy. This is inevitable given the acute situation and the practical reality that we still live in a largely fossil fuel driven world.

It may even appear that we are going backwards when, for instance, Germany has just razed to the ground an onshore wind farm to make way for a new coal mine.

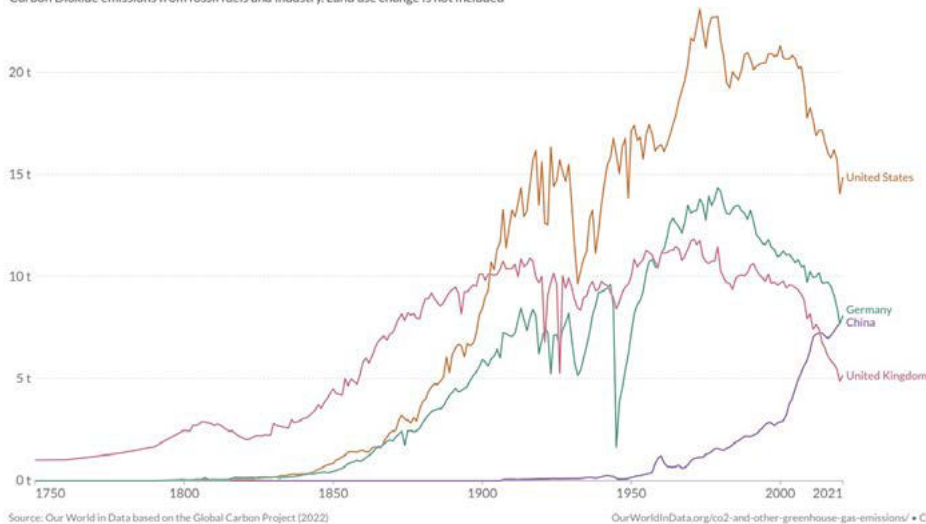
While the energy crisis remains acute with many individuals and families risking energy poverty and industry facing significant pressures, the environmental movement would be wise not to resist such short-term panic measures if it is not to lose public support.

It should also be recognized that both the UK and Germany have made considerable progress in reducing per-capita CO<sub>2</sub> emissions even as GDP has continued to grow. That may be a function of the different time frames of industrialisation in different countries and the more recent shift towards service-based economies in the West, while China and other countries become the manufacturing hubs. In other words, we may be exporting our increased emissions rather than decreasing them. (See figure, next page)

<sup>3</sup> Note that this also applies to work at EU level where, in spite of the ability of the European Commission to try to push for EU-wide solutions, these can only work with the support of individual Member States – as we have seen recently with the proposed energy price cap.

## PER CAPITA CO<sub>2</sub> EMISSIONS

Carbon Dioxide emissions from fossil fuels and industry. Land use change is not included



### A Positive Framing

In the medium and long term, the Ukraine crisis, other evolving geopolitical tensions, and increasingly challenging economic conditions offer the opportunity to frame low-carbon energy as the key to energy sovereignty and security and the green transition as a positive economic opportunity.

This comes at a time, when renewables have become much more cost-competitive and often generate electricity for lower prices than fossil fuels. There is, therefore, an increasingly compelling economic and security case for energy transitions that will prove more powerful than decarbonization arguments on their own.

Similarly, a focus on the health issues associated with the pollution from fossil fuel use may have more resonance with voters than what some may see, however mistakenly, as the abstractions of climate change. As one community campaigner put it to us, climate change has little resonance in his communities, but climate-friendly action can be achieved when framed in terms of issues that affect people in their everyday lives.

A renowned UK environmental campaigner suggests that it is time to supplement the current climate narrative with an increased focus on the practicalities of defining the

economic and social opportunities offered by the green transition. He argues for an 'upbeat, enthusiastic, can-do attitude' to replace the growing sense of hopelessness.

These issues will be even more relevant if progress is to be made in other, even more difficult areas such as biodiversity loss.

To be successful, such approaches need to fulfil the criteria outlined in this summary.

The renewables industry itself has a role to play. During the crisis, it cannot afford to squander political capital by being seen to be acting in its own narrow, short-term self-interest - for instance by trying to preserve its windfall revenues and margins even when its cost of energy generation is much lower than the prices it is being paid because such prices are tied to the spot market price of gas.

One thing that the energy crisis has brought to the fore is that energy markets in Europe have been poorly structured and need major reform with governments acting strategically given the changing geopolitical picture. This provides a golden opportunity for achieving an effective transition, with greater energy security and more cost effectiveness. But planning and implementation challenges are huge, from the question of storage to those of planning large-scale grids, due to the place-bounded and intermittent nature of renewable energy generation.

Those who wish to keep promoting the use of fossil fuels and are, however, also using the energy crisis to their advantage.

- DESPITE WHAT MAY SEEM TO BE SHORT-TERM SETBACKS, THE UKRAINE CRISIS OFFERS A GOLDEN OPPORTUNITY TO WORK TOWARDS A PARADIGM SHIFT IN ENERGY POLICY
- CREATING MOMENTUM TO FRAME THE SHIFT POSITIVELY AS ECONOMIC, INDUSTRIAL AND SOCIAL OPPORTUNITY AND A MEDIUM/LONG-TERM SOLUTION TO ENERGY SOVEREIGNTY AND SECURITY IS COMPLEMENTARY TO, AND LIKELY TO BE MORE EFFECTIVE THAN, AN EXCLUSIVE FRAMING AS THE PREVENTION OF LONG-TERM CLIMATE DAMAGE
- THERE ARE TENTATIVE SIGNS THAT ACHIEVING SUCH A POLITICAL SHIFT IN MINDSET IS STARTING TO HAPPEN AND CAN BE ACCELERATED THROUGH A WELL-STRUCTURED, SUSTAINED CAMPAIGN THAT ALSO WORKS THROUGH THE PRACTICALITIES OF LOCAL IMPLEMENTATION – SOMETHING THAT WILL TAKE TIME AND REQUIRES DILIGENT, DETAILED AND POLITICALLY SAVVY WORK
- THIS POLITICAL SHIFT SHOULD BE FACILITATED BY THE SEEMINGLY INCREASING WILLINGNESS OF BUSINESSES TO TACKLE THEIR OWN EMISSIONS – A DEVELOPMENT THAT COULD BE ENHANCED BY POLICY ACTION THAT GIVES ADVANTAGE TO BUSINESSES THAT MOVE FURTHER IN THIS DIRECTION
- WE SUGGEST THAT NEXT STEPS SHOULD FOCUS ON PRECISE PATHWAYS TO CHANGE, SEQUENCING OF INTRODUCING/ SUPPORTING ALTERNATIVES TO FOSSIL FUELS, MAYBE RAISING THE PRICE OF CO2 IN CERTAIN TARGETED SECTORS, AND EVENTUALLY REDUCING SUBSIDIES ALL NEED TO BE CAREFULLY SPELLED OUT TO ENSURE THAT ALL ENERGY POLICY OBJECTIVES (AS OUTLINED AT THE START OF THIS REPORT) ARE MET
- THE EARLIER SUCH WORK STARTS IN EARNEST, THE HIGHER THE LIKELIHOOD OF MEDIUM AND LONG-TERM SUCCESS

## 2. FOSSIL FUEL SUBSIDIES – WHY?

### 2.1 DEFINITIONS AND CONSTRAINTS

A great deal of confusion swirls around the word 'subsidies'. The same word can mean four different things:

1. *money handed directly to people or producers*
2. *some form of special taxation or tax credit or tax break (tax expenditures)*
3. *money given to preserve energy security*
4. *financial support where there is a 'learning curve' or research and development to sustain a technology until it reaches the point of financial viability*

All these are lumped together as 'subsidies', yet they are very different things.

**'SUBSIDIES' CAN MEAN MANY DIFFERENT THINGS**

We do not believe, given this variety, that the language of "distorting markets" – even though it often gets used in the context of subsidies – is appropriate here. Even so, by causing the playing field to be more uneven, there is a sense in which the existence of some subsidies – to airlines for example – simply make it necessary for competitor nations to bail out their airlines too.

The problem around how we define FFS matters because some subsidies are complex and may be useful in serving to bring net zero closer. We might, for example, in the future find ourselves attempting to reduce demand by subsidising home insulation. The UK government is already reducing fossil fuel demand by subsidising electric vehicles (for the moment).

THE PROBLEM AROUND HOW WE DEFINE FFS MATTERS BECAUSE SOME SUBSIDIES ARE COMPLEX AND MAY BE USEFUL IN SERVING TO BRING NET ZERO CLOSER.

Most subsidies are traditional tax breaks (tax expenditures), although since the invasion of Ukraine and fuel inflation around the world, government cash has flowed directly to citizens and into the energy companies in compensation for the price cap introduced in October. Some will be clawed back through taxation on windfall profits.

Some subsidies involve payments to essential workers like small-scale farmers or disadvantaged groups such as older people, ostensibly given as financial support, though they are clearly for the use of fossil fuels and lead, some would argue, to the 'overconsumption' of fossil fuels. Such support payments cannot reasonably be removed until viable clean energy alternatives exist.

There is, in some ways, a hierarchy of FFS. All subsidies are not necessarily bad. For instance, subsidies for fossil-fuel driven public transport systems can either be labeled as FFS or they can be labeled as 'good' environmental subsidies in that they shift usage from more polluting private vehicles. We will argue later that this blurring lies behind the fundamental problem of why FFS have proved so difficult to end.

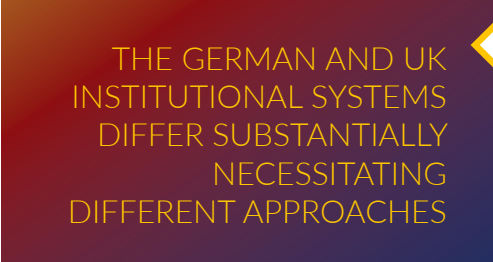
**NOT ALL SUBSIDIES ARE NECESSARILY BAD**

Germany has a very different, more consensual political system from the UK. Coalition government is the norm, and different ministerial interests, backed by their interest groups can have a stranglehold over the policy agenda. This leads to a corporatist style of policy making where compromise between the interests of different groups sets limits on the speed of progress.

For instance, those towards the right of the German political spectrum would prefer to back up renewable forms of energy with nuclear rather than coal while the origins of the Green Party as an anti-nuclear party makes it more difficult for them to back nuclear power – a position that may harm their own decarbonization agenda.

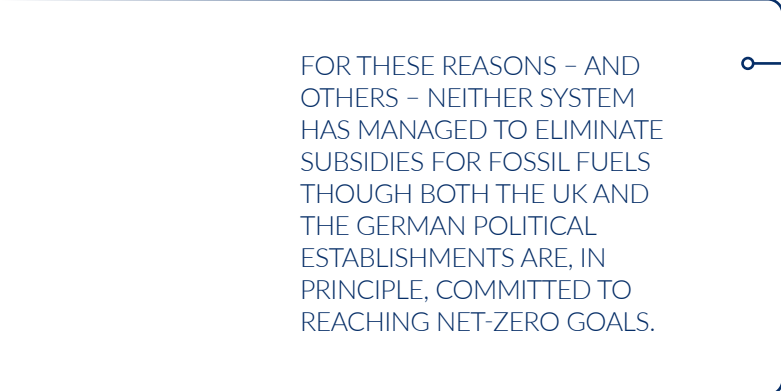
The German parliament will rubber stamp legislation, but only once ministers have made sure that both their department and their party is on board. The devolved nature of the German constitution also means that central government has limited power over the actions taken (or not taken) by the different Länder.

The UK, on the other hand, has none of the decentralisation of the German system with much power concentrated with the Prime Minister and the Treasury.



THE GERMAN AND UK  
INSTITUTIONAL SYSTEMS  
DIFFER SUBSTANTIALLY  
NECESSITATING  
DIFFERENT APPROACHES

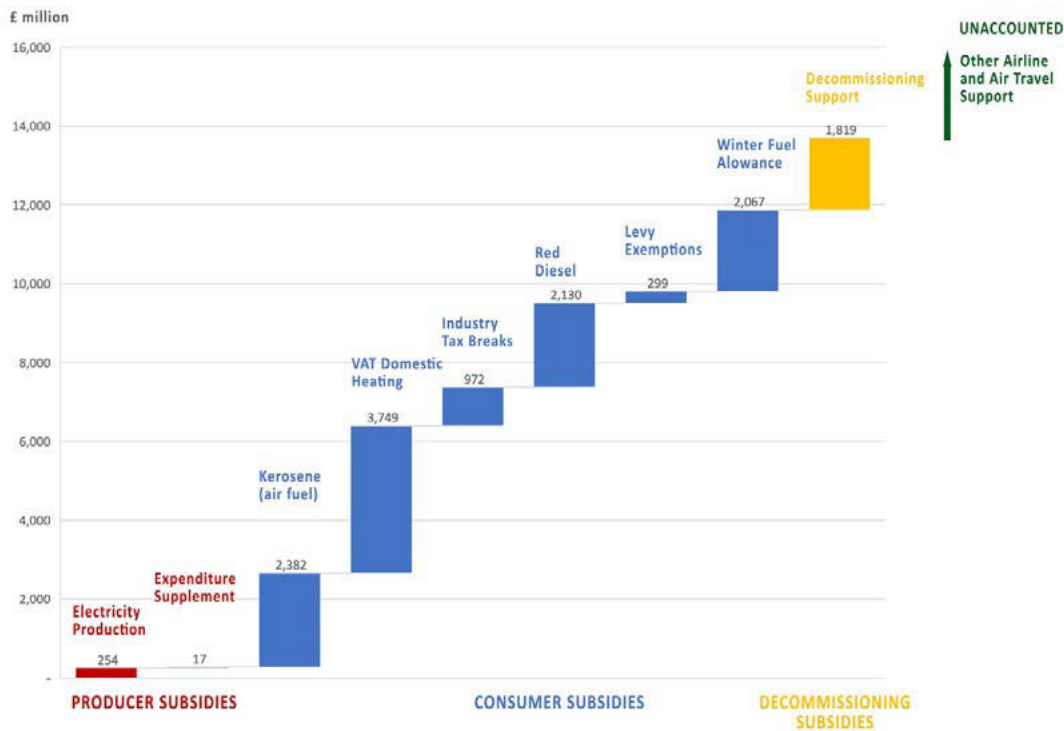
Nonetheless, in the UK system, the Treasury is still able to block most reforms if they don't accord with their traditional outlook. That is to say either expenditures are seen as a political imperative or the Treasury has calculated that, in net revenue terms, the income flowing back to the Treasury from these industrial activities exceeds the costs.



FOR THESE REASONS – AND  
OTHERS – NEITHER SYSTEM  
HAS MANAGED TO ELIMINATE  
SUBSIDIES FOR FOSSIL FUELS  
THOUGH BOTH THE UK AND  
THE GERMAN POLITICAL  
ESTABLISHMENTS ARE, IN  
PRINCIPLE, COMMITTED TO  
REACHING NET-ZERO GOALS.

## 2.2 BACKGROUND TO UK FOSSIL FUEL SUBSIDIES

### Fossil Fuel Subsidies in the UK total around £14bn



The outlook for fossil fuel subsidies in the UK is riddled with uncertainties.

The war in Ukraine, launched by an aggressive petrostate against a neighbour, has changed all previous assumptions and created an energy market that is currently indivisible from politics. Things are unlikely to return to any kind of stability in the short term. Yet – while there are obvious dangers – there are also potential benefits.

There is the opportunity to see an accelerated clean transition as vital to future energy security and assess renewables as delivering “faster than anyone expected.” Certainly, renewable electricity displaced about £6bn worth of gas in the UK alone last year, the centreright think-tank Onward estimates.<sup>4</sup> A major UK electricity company has announced that it is helping to deliver the first British home so well equipped with green-technology that it will never generate a fuel bill.<sup>5</sup>



<sup>4</sup> Financial Times August 23 2022: Gaslighting Finds a Whole New Meaning with this Energy Crisis by Pilita Clark <https://www.ft.com/content/232d2cc2-a489-4a8c-ace9-1edb86ba9de0>

<sup>5</sup> Financial Times June 3 2022: Octopus and Ilke launch clean energy scheme with no bills for householders by George Hammond. <https://www.ft.com/content/b81307f1-94cc-4b0f-9b64-1ac072dfe9dd>

Yet, in the short term, the uncertainty triggered a revived focus on fracking (now abandoned once again) and prompted the expansion of bulk LNG storage. At the same time officials with an overview of the transition are highlighting potential problems ahead for renewables. For example, the UK is currently the leader in offshore wind with 28.9 per cent of the world's offshore turbines but it is also running short of choice sites for wind power.<sup>6,7</sup> This problem is offset, at least in part, by the opportunity to upgrade existing wind power generation with newer turbines that can generate significantly more energy (when the wind blows).

It is also the case, we understand, that fan blades from wind turbines cannot, currently, be recycled. They have to be buried instead – something that carries its own environmental impact.

THE CURRENT VIEW IS THAT, IN THE CURRENT STATE OF DEVELOPMENT, RENEWABLES TECHNOLOGY CAN ALLOW MUCH PROGRESS TO BE MADE BUT FALLS SHORT OF BEING THE MAGIC BULLET THAT CAN SOLVE ALL ENERGY RELATED ISSUES.

### A Positive Framing

Even before these developments, the debate around fossil fuel subsidies had become muted. Politicians and their advisors appeared to accept they were an integral part of the UK financial landscape. A Department for Business, Energy and Industrial Strategy (BEIS) official described reform of FFS as “not even a conversation”. Several reasons were given for this.

**UKRAINE:  
SHORT-TERM  
CHALLENGES.  
LONG-TERM  
OPPORTUNITY**

**FOSSIL FUEL  
SUBSIDIES ARE  
NOT EVEN A  
CONVERSATION**

Further issues arise both in terms of the security of the supply chain associated with renewable technologies – much of it currently controlled by China – and around the uncertainty of new renewable technologies that seem to offer promise but are still far from being a reality. The current view is that, in the current state of development, renewables technology can allow much progress to be made but falls short of being the magic bullet that can solve all energy related issues. Nuclear power is seen as the other main viable source of low carbon energy – though it is not without its own issues.

It is as well to take such views on board when campaigning for a smooth energy transition.

In the UK most of the FFS “are almost all in the control of the Treasury,” said one former minister meaning that other departments don’t get much say in the subsidy discussion. As a result, government officials we spoke to could remember no occasions when FFS were discussed seriously.

Another issue relates to how FFS are defined and documented. Often designated as economic support for special interest groups such as farmers or the fishing industry, this blurring of lines leads to a policy position that there are no FFS in the UK.

<sup>6</sup> Sunday Times, August 28 2022: An Offshore Wind Revolution has Begun – can it Meet the UK’s Power Needs by Ben Spencer: <https://www.thetimes.co.uk/article/an-offshore-wind-revolution-has-begun-can-it-meet-theuks-power-needs-ph6w5bt09>

<sup>7</sup> The UK has focused primarily on offshore wind because of its geography and increasingly vocal local opposition to onshore wind installations

## A Positive Framing

Despite this, there is an acknowledgement that the UK has been doing relatively well in eliminating FFS compared with most other European countries. One of the major differences between the UK and Germany has been that the UK has moved from coal to gas in the electricity sector whereas Germany has moved from nuclear to coal, closing nuclear power stations on essentially ideological grounds before they came to the end of their working life.

THE UK IS DOING BETTER THAN OTHERS IN ELIMINATING FOSSIL FUEL SUBSIDIES

The exceptions to areas where the UK is making progress include.

- *Subsidies to encourage investment in North Sea drilling. Former Prime Minister Liz Truss planned to offer hundreds of new parts of the UK seabed for oil and gas drilling in the North Sea in a move the Scottish government described as 'alarming'.<sup>8</sup> At the time of going to press it was not clear whether the new Prime Minister Rishi Sunak will press ahead with these.*
- *Tax concessions for red diesel for farmers and the forestry (£2.1 billion)*
- *Motor transport, building and policing roads and motorways – and airlines and flights.*
- *Air fuel*
- *Winter fuel payments for older people, and other cold weather payments for those on some benefits at least (£2 billion)*
- *Subsidies to struggling parts of high-energy industries like iron and steel, aluminium or cement.*
- *Subsidised VAT payments on domestic energy (£3,479 million) [2021 figure]*
- *Subsidies to mitigate inflationary energy costs for consumers (approx. £100-150+ billion).<sup>9</sup>*

One of the most expensive items is the 5 per cent VAT rate concession on domestic energy, without which the £100-150 billion planned to subsidise people's energy would be 15 per cent higher.

THE CHANCES OF EQUALISING THE VAT ON DOMESTIC ENERGY, THAT IS TO SAY, RETURNING VAT ON ENERGY TO THE STANDARD RATE OF 20 PER CENT, IS NOW POLITICALLY TOXIC.

It has been since at least 1993 when Norman Lamont, Chancellor under the then Prime Minister Margaret Thatcher, announced on Budget Day that the eight per cent VAT charge on domestic fuel would more than double to match the full rate of 17.5 per cent the following year. The announcement led directly to the loss of the Christchurch by-election and Lamont's ministerial career came to an end shortly afterwards.<sup>10</sup>

The German government also now has a 7 per cent VAT rate on fuel, down from 19 per cent. The package is so generous that it has created tensions within the EU. Poorer nations in the block say it unfairly advantages German businesses.<sup>11</sup>

It might be possible to imagine this subsidy differently, to privilege domestic energy from greener sources of power, for example. The difficulty is that, if that were done at cost, there are bound to be some losers under the new dispensation – and they would probably be among the poorest section of society.

REMOVAL OF SUBSIDIES HITS THE POOREST IN SOCIETY

<sup>8</sup> <https://www.thetimes.co.uk/article/anger-over-new-spots-for-drilling-7cgtwvmv6>

<sup>9</sup> <https://www.theguardian.com/politics/2022/sep/08/liz-truss-to-freeze-energy-bills-price-at-2500-a-yearfunded-by-borrowing>

<sup>10</sup> : <https://www.heraldscotland.com/news/12614542.lamont-in-new-storm-over-vat-on-fuel-bills/>

<sup>11</sup> <https://www.telegraph.co.uk/business/2022/10/23/anger-germanys-industrial-heartlands-putin-cuts-gas/>



For decommissioning and North Sea exploration, the argument was about “*getting the balance right between taxation and support for investment given current level of oil prices... keeping it profitable for the sake of Scottish industry,*” according to one former minister.

Removing farm subsidies and weaning fishing communities off their dependence on subsidised red diesel was considered “very hard”, largely because these communities are already suffering economically, and there are, currently, no viable alternatives (few practical sized electric tractors or fishing boats, for example).

### The political landscape and the practicalities

PREVIOUS GOVERNMENTS ACCEPTED FOUR CLEAR ENERGY POLICY OBJECTIVES – ENERGY SECURITY (‘KEEPING THE LIGHTS ON’, AS POLITICIANS SAY IN THE UK), AFFORDABILITY FOR LOW-INCOME GROUPS, ENVIRONMENTAL BENEFIT, AND SELF-SUFFICIENCY. ALL TO BE DONE WHILE KEEPING THE VOTING PUBLIC ON BOARD.

After the 2008 financial crisis, things became more complicated. And again, after the Brexit vote in 2016.

Prime Minister Boris Johnson, allegedly influenced by his wife, Carrie, regularly expressed enthusiasm for the green agenda, but – as one of our interviewees told us – he “has been unbelievably ineffective – nothing has happened”.

First indications suggested that the recent, now defunct, administration under Liz Truss may have viewed green policies as ‘anti-growth’. Only a few weeks into her brief government, she deemed a £15 million energy-saving advice campaign proposed by the government’s Climate Change Committee this winter as unnecessary.

Labour claims an awareness campaign could save households up to £8.4bn – a saving of £300 per household.<sup>12</sup> However, it is likely true that an ‘advice campaign’ on its own will have very limited effect. Further subsidies for energy-saving schemes would likely be needed – a challenging proposition in the current constrained fiscal environment (see below).

IN THE RUN-UP TO THE 2024 ELECTION, BOTH MAJOR PARTIES EXPRESS A COMMITMENT TO THE CLIMATE AGENDA.

The Labour party has, positively, re-framed the green transition as a job creating, economic growth agenda. The still young Sunak administration is nominally committed to the previously agreed net-zero goals but has to manage tensions within its own party – hence the flip-flopping over the Prime Minister’s attendance at COP27. It will also need to look over its shoulder to potential votes it could lose to the green-sceptic Reform Party (the successor party to UKIP) to which the Conservative Party has already lost over 4,000 members in the last few weeks.

BROAD INTERNATIONAL COMMITMENTS STILL FACE LOCAL POLITICAL AND PRACTICAL OBSTACLES

The figure for total subsidies (as defined by the Organisation for Economic Co-operation and Development) given by the UK government is around £14 billion according to the most recent figures available (not including some critical exceptions).

The part they play in actively harming the climate has not been quantified but other uses have been assessed.

<sup>12</sup> The Guardian, Sunday October 9, by Michael Savage, Shanti Das and Rebecca Brahde: Anger as Truss ignores her climate advisers’ call for energy-saving drive. <https://www.theguardian.com/society/2022/oct/09/anger-as-truss-ignores-her-climate-advisers-call-for-energy-saving-drive>

For example, in May of this year the green thinktank E3G calculated that billions of pounds given away in a tax break for UK oil and gas exploitation could have cut the energy bills of 2m homes by £342 a year if invested in insulation measures.<sup>13</sup> Yet it doesn't happen. Why?

There are practical reasons of sequencing in that home insulation on a national scale is a multi-year process during which there will still be higher levels of energy use.

IN TERMS OF TIMING, IT IS THEREFORE NOT QUITE AS SIMPLE AS SHIFTING OIL AND GAS SUBSIDIES TO HOME INSULATION SUBSIDIES.

This is an example of what our climate campaigner meant when referring to 'lazy thinking.' It damages campaigners' credibility among policy makers.

<sup>13</sup> The Guardian, May 1 2022: Sunak's UK oil subsidy could have insulated 2m homes, says thinktank by Damian Carrington. <https://www.theguardian.com/environment/2022/may/31/sunak-uk-oil-subsidy-could-have-insulated-2m-homes-says-thinktank>.

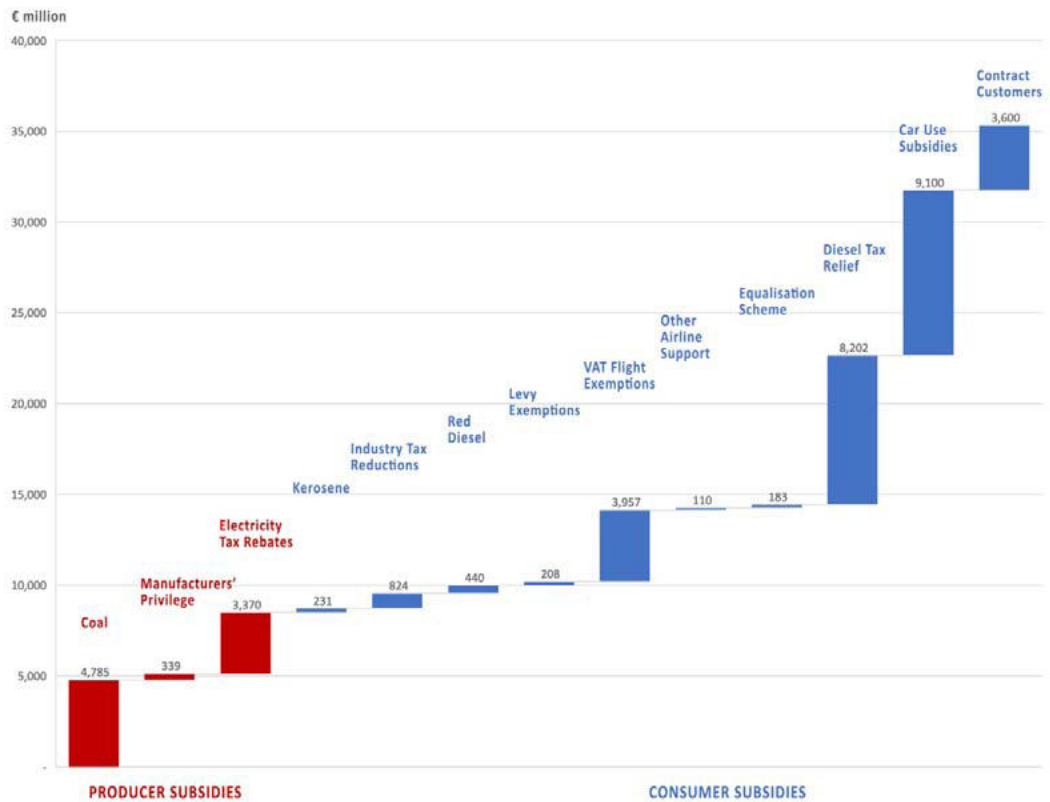
A second reality is that UK households have shown themselves to be unwilling to put up with the disruption associated with 'greening' their homes even if subsidized to do so. While this attitude might shift with soaring energy prices, there will also be limited fiscal space for such initiatives for a while as much of it is taken up with short term support for energy bills.

Nevertheless, in the November 2022 Autumn Statement the chancellor promised that £6.6bn would be spent during this parliament on energy efficiency and announced a further £6bn of funding from 2025, "doubling annual investment". The go-ahead was also given for the Sizewell C nuclear power plant.

THE CHANCELLOR PROMISED THAT £6.6BN WOULD BE SPENT DURING THIS PARLIAMENT ON ENERGY EFFICIENCY AND ANNOUNCED A FURTHER £6BN OF FUNDING FROM 2025, "DOUBLING ANNUAL INVESTMENT".

## 2.3 BACKGROUND TO GERMAN FOSSIL FUEL SUBSIDIES

### Fossil Fuel Subsidies in Germany total around €35bn



Source: OECD

IN GERMANY, SUBSIDIES ON FOSSIL FUEL USE AND CONSUMPTION PLAY A MAJOR ROLE IN INDUSTRIAL, ENERGY, AND SOCIAL POLICIES. AT THE SAME TIME, FOSSIL FUEL SUBSIDIES HAVE BEEN IDENTIFIED BY EXPERTS AND IN PUBLIC DEBATES AS KEY OBSTACLES IN MEETING THE COUNTRY'S DECARBONISATION GOALS.<sup>14</sup>

(Umweltbundesamt) estimates that various subsidies and tax expenditures worth €60.6 billion harm the climate directly.<sup>15</sup>

Germany has an effective and modern democratic and federal constitution. It is both more responsive and more democratic, and yet the German institutions seem to have found it even harder to get rid of FFS than in Britain.

**FOSSIL FUEL SUBSIDIES  
HAVE RECEIVED  
SIGNIFICANT ATTENTION**

#### The issues are well recognised

The most recent OECD figures used in this report suggest FFS in Germany total around €35 billion. A previous influential report on environmentally harmful subsidies by the German Environmental Agency

<sup>14</sup> After a ruling by Germany's constitutional court, the government has committed in law to reduce greenhouse gas emissions by 55 per cent by 2030; the country aims to be "net zero" by 2045.

<sup>15</sup> Andreas Burger & Wolfgang Bredschneider, Umweltschädliche Subventionen in Deutschland, aktualisierte Ausgabe 2021, Umweltbundesamt, Dessau-Roßlau 2021.

The major share is in fossil fuel-based mobility (€30.8 billion, with more than €12 billion for aviation), energy generation (eg. electricity) and industrial consumption (€24 billion), and another €5.7 worth of subsidies for agriculture.

Major subsidies also exist in the building sector significantly, though less directly, impacting greenhouse gas emissions. Using a broad lens definition of subsidies, the think tank Forum Ökologisch-Soziale Marktwirtschaft suggests that the equivalent of 100 million tons of carbon dioxide could be saved if fossil fuel subsidies were scrapped.<sup>16</sup> Whether such direct cause-and-effect relationships ever exist in complex social systems is, of course, debatable.

### But policy action is lacking

Despite public declarations and a high material and symbolic significance attributed to FFS in the context of climate change mitigation, little has happened on the policy front. The only real area of change has been in coal and lignite, where subsidies have been eliminated as part of an agreed plan to phase out these extremely carbon-intensive sources for electricity generation by 2038 – in reaction to an ever more apparent failure to meet Germany's decarbonisation targets.

Moreover, the Ministry of Economic Affairs and Climate Action under the leadership of Robert Habeck has started to reshuffle funds for construction from new buildings to refurbishments and retrofitting of existing housing stock. In other areas, hardly any progress is evident, as official bodies like the European Commission observe.

ON BALANCE, LITTLE  
POLICY ACTION HAS  
EMERGED

On top of that, the new social democratic-green-liberal coalition has reacted to the current energy crisis with several significant fiscal measures that directly support fossil fuel consumption.

<sup>16</sup> Forum Ökologisch-Soziale Marktwirtschaft, Zehn klimaschädliche Subventionen im Fokus, November 2020.

Long-distance commuter tax rebates that privilege car use have been hiked; a three-month cut in fuel taxes was introduced from June to August 2022 (worth €3.15 billion) and a planned increase in CO2 charges for domestic heating and vehicle fuel use has been suspended. A reduction in electricity and energy taxes for energy-intensive industries worth €1.7 billion has also been extended until the end of 2023.

This is despite a long-standing discussion in Germany on the need to switch from consumption-focused subsidies that incentivise fossil fuel use to direct fiscal support for firms and households that encourages and underpins energy transitions, like electrification and savings.

It is important to note that fossil fuel subsidies are clearly identified and discussed as distinct subsidies in Germany. People are generally aware of the role they play in industry and in their everyday lives.

Nonetheless, and most worryingly, the government does not seem to have a plan of how to move to a longer-term climate policy agenda that involves the redesign of subsidies for energy consumption, mobility, and agriculture.

THE GOVERNMENT DOES NOT SEEM TO HAVE A PLAN OF HOW TO MOVE TO A LONGER-TERM CLIMATE POLICY AGENDA THAT INVOLVES THE REDESIGN OF SUBSIDIES FOR ENERGY CONSUMPTION, MOBILITY, AND AGRICULTURE.

After sixteen years of Angela Merkel's 'muddling through', and in times of heightened uncertainties, kneejerk politics and policies drawn up as a series of 'instant responses' prevail.

Interest group and electoral politics combined with entrenched policy processes make FFS very 'sticky' and explain a persistent gap between intentions and action. Energy-intensive industries and those selling carbon-goods (primarily cars) traditionally have a strong footing in the Christian democratic

(CDU) party (through the Mittelstandsunion consortium, for example) and social democratic (SPD) party (through industrial workers). They enjoy privileged access to the highest echelons of government – big industry has the ‘Chancellor’s ear’, as one interviewee put it.

FEDERAL MINISTRIES AND MINISTERS HAVE SIGNIFICANT INDEPENDENCE AND POLICY LEVERAGE IN THEIR AREAS OF RESPONSIBILITY, AND THESE MINISTRIES REGULARLY RESIST REFORMS THAT GO AGAINST THE INTERESTS OF DOMINANT INTEREST GROUPS IN THEIR SECTORS.

Just as important is the fact that federal ministries and ministers have significant independence and policy leverage in their areas of responsibility, and these ministries regularly resist reforms that go against the interests of dominant interest groups in their sectors. This is particularly the case for transport (with strong ties to the automotive industry) and agriculture ministries.

FOSSIL FUEL SUBSIDIES ARE PART OF GERMAN INDUSTRIAL POLICY

Unfortunately, this situation can worsen if the Chancellor does not take up a strong leadership role to guide the way. Ministers and ministries can then act in their – or their peers’ – own interests, leaving the entire economy and population with no long-term perspective, which makes planning and investment a difficult task.

Last but not least, the two mainstream parties hesitate to cut subsidies that benefit the citizens who make up significant parts of their electorate or whose political support can be crucial in maintaining ever more fragile electoral coalitions. Among these are workers in subsidised industries; residents in rural areas, who rely on combustion engine cars; and poorer groups, who

benefit from fuel subsidies (commuter tax expenditures and reduced diesel fuel taxes, for example). In the current environment of very high energy prices, all parties agree that scrapping subsidies would be ‘political suicide’ and would lead to accusations of being responsible for a deliberate process of de-industrialisation and job losses.

THE TWO MAINSTREAM PARTIES HESITATE TO CUT SUBSIDIES THAT BENEFIT THE CITIZENS WHO MAKE UP SIGNIFICANT PARTS OF THEIR ELECTORATE OR WHOSE POLITICAL SUPPORT CAN BE CRUCIAL IN MAINTAINING EVER MORE FRAGILE ELECTORAL COALITIONS.

REMOVAL OF SUBSIDIES IS SEEN AS POLITICALLY TOO RISKY

Moreover, even climate policy advocates have been content to stand back and comply with the idea that higher energy prices will perform the work of disincentivising fossil fuel consumption and help the government achieve its net zero targets, without the need for deliberate reform.

There is also an emerging perception that, should the government press too hard with measures that have cost-implications (like raising or expanding carbon dioxide charges), conservative forces could latch onto that by openly questioning climate change mitigation policies. They could frame such policies as harmful for employment and growth (as increasingly happens elsewhere, including the UK). In cases where the government or reform leader fails to argue clearly or convincingly enough to win people over, this could lead to social and economic unrest.

### 3. WHY SO STICKY?

*“The great enemy of the truth is very often not the lie, deliberate, contrived and dishonest, but the myth, persistent, persuasive and unrealistic.”*

**John F. Kennedy**

The reality on the ground is that FFS have proven very sticky.

It is also true that many of the issues associated with the stickiness of FFS are issues that affect climate and environmental policy more broadly. There are therefore broader environmental policy lessons to be learned than just application to FFS.

#### 3.1 THE POLITICAL CYCLE

Politics operates to a four-to-five-year political cycle. Enacting policies that are unpopular in the short term while any benefits will only materialize in the long-term are hard to implement. As one former Secretary of State put it to us, we know what works but what works may be highly unpopular. Subsidies are popular, removing them is not.

Episodes like the gilet jaunes protests in France further add to the skittishness around unpopular measures and often force political U-turns. As former President of the European Commission Jean Claude Juncker once put it: ***“We know what we need to do. What just don’t know how to get re-elected if we do it.”***

It is tempting to adopt an air of superiority and sneer at the political classes for these reasons. But that is the reality of life in a democracy and scoffing is both pointless and counterproductive. It simply allows a self-satisfied shifting of blame onto others while diluting or killing efforts to look for ways to achieve change given the world as it is.

However, while governments have relatively short parliamentary terms, politicians, political parties and regulators are there for the longer term and do act to balance short-term imperatives with longer-term plans in as far as is possible.



WE NEED TO WORK  
WITH THE WORLD AS IT  
IS RATHER THAN HOW  
WE MIGHT LIKE IT TO BE

IT IS MORE PRODUCTIVE TO LOOK FOR WAYS IN WHICH DESIRED POLICY ACTION CAN BE FRAMED AND IMPLEMENTED TO PROVIDE POLITICAL BENEFIT WITHIN THE POLITICAL CYCLE.

There is also the issue of financing. Shifting subsidy monies towards home insulation would, for instance, provide a positive long-term solution for many and allow the withdrawal (or the much-reduced cost) of some fossil fuel subsidies. However, this requires up-front financing since subsidies will only be reduced after an insulation drive is complete nationwide.

That said, and despite the limited fiscal space available, in the latest Autumn Statement the UK government has announced the setting up of an energy efficiency task force backed by £6 billion in new funding. It is part of the government’s new target of reducing energy consumption from buildings and industry by 15 per cent by 2030.

Crises such as the current energy crisis do, however, have to be dealt with immediately, which may blunt long-term strategies.

#### 3.2 INSUFFICIENT POLITICAL APPEAL

One former UK minister described his astonishment, on being elected, at discovering that ‘really motivated’ colleagues, committed to fighting climate change, numbered only around 25 out of a 650-strong House of Commons.

Though it has taken decades to get there, the environmental movement has been successful in pushing climate issues to the top of the discussions in the political agenda.

THERE REMAINS, HOWEVER, A GAP BETWEEN THE TOP-LEVEL POLITICAL RHETORIC AND THE NUMBER OF POLITICIANS WILLING TO TAKE ON ENVIRONMENTAL ISSUES AS THEIR PERSONAL AREA OF INTEREST AND ACTIVITY.

This reflects two main issues:

- *In real life, most voters have more immediate concerns that trump environmental ones – despite voters being willing to declare climate concerns (without any real personal commitment) when answering survey questions that are all too often too superficial and/or carried out by groups wishing to get a particular outcome*
- *environmental policies are too often seen (and maybe too often presented) as coercive actions that interfere with people's lives, reduce life options and increase short-term costs – both for industry and for individuals*

WHILE CLIMATE CHANGE HAS BEEN EMBRACED AS AN IMPORTANT POLICY AREA IN MOST COUNTRIES, THE PRACTICAL IMPLEMENTATION OF CLIMATE-FRIENDLY POLICY REMAINS A DIFFICULT SUBJECT POLITICALLY

As one former UK minister put it to us: “You need to think about the politics - the fact that losers scream more than winners applaud.” While environmental policy continues to be perceived as creating losers today for potential winners tomorrow, progress will remain halting.

Things have moved on, however. In both the UK and Germany, all the major political parties have defined environmental policies – though none tend to include the removal of subsidies. In the UK, the Conservative Environment Network has signed up around 150 parliamentarians though it is not clear how many of them are truly committed to campaign actively for environmental causes rather than just being happy to have their name appended to the group while doing little. Some also form part of the Net-Zero Scrutiny Group that is sceptical about the speed of transition.

IN BOTH THE UK AND GERMANY, ALL THE MAJOR POLITICAL PARTIES HAVE DEFINED ENVIRONMENTAL POLICIES – THOUGH NONE TEND TO INCLUDE THE REMOVAL OF SUBSIDIES.

### 3.3 ALL POLITICS IS LOCAL

Given the global nature of climate change and other environmental challenges, there has been considerable effort devoted to influencing trans-national initiatives such as the COP series and the efforts of the IPCC.

YET OUR POLITICAL SYSTEMS REMAIN NATIONAL (OR SUBNATIONAL) AND GEOGRAPHICALLY BOUNDED.

This is, first of all, reflected in the challenges we have seen in reaching global agreements. But it is also reflected in the fact that any global agreement has to be implemented locally, country by country taking into account local conditions and national political realities.

ASPIRATIONAL GLOBAL AGREEMENTS STILL HAVE TO TACKLE THE CHALLENGES OF LOCAL IMPLEMENTATION

As we hope we have managed to make clear in this report, there are significant differences between countries – both technically and, especially, politically. This requires more effort than has maybe been the case to define implementation pathways that have a chance of success in each country.

There are also opportunities at regional and city levels in those situations where local government has enough powers to effect change locally.

### 3.4 MINISTRIES AND SPECIAL INTERESTS CAN AND DO VETO PROGRESS

This applies mainly to the German system where each ministry is semi-independent and dominated by sectoral interests like the motor industry. The Chancellor rarely imposes his or her will, rather acting as an orchestrator in reaching compromise. The net result is a corporatist approach designed to accommodate everyone's interests and making progress inevitably slow.

The decentralized German system also gives significant power to the Länder further complicating the implementation of policies at a national level.

**DIFFERENT SYSTEMS, DIFFERENT CHALLENGES**

The highly centralised UK system is different. There is little or no power in the regions (except for the devolved nations) and each department of state is subordinated to the collective decisions of the cabinet – as interpreted by the Prime Minister – but where everything involving money is subject to the decisions by a UK Treasury that acts as a hard brake on much investment.

### 3.5 THE SHEER INTERCONNECTEDNESS OF SUBSIDIES WITH PEOPLE'S LIVES

FFS do not stand alone as climate or environmental policy. They are part of a complex interaction between environmental policy, energy policy, social policy, industrial and economic policy.

**APPROACHING FFS IN ISOLATION FRAMED EXCLUSIVELY AS PART OF CLIMATE POLICY CANNOT, THEREFORE, BE SUCCESSFUL.**

Some are purely about looking after disadvantaged communities, sectors or industries.

In a complex system, small changes can also have widespread network effects. For instance, failure to subsidise gas will not only impact the price of home heating but will also impact the cost of nitrate fertilisers which, in turn, affects the price of food, which, in turn, hits the poorest hardest.

**REMOVAL OF SUBSIDIES HAS A REAL IMPACT ON PEOPLE'S LIVES WITH THE POOREST MOST AFFECTED**

This interconnectedness – the sheer complexity of the impacts of the subsidies – makes it a fiendishly difficult subject for public policy in practice. Yet much work done around FFS and the use of fossil fuels in general tends to focus narrowly on potential climate impacts without working through the ramifications on many aspects of people's lives.

An important question is 'what, exactly, is being subsidized?' Is it people's problems with high bills or particular forms of consumption? There are good reasons why we will need to subsidise some aspects of a transitional period in the economy before we reach net zero.



GETTING PAST THE SILOS: POLICY ANALYSES NEED TO ADDRESS MORE EXPLICITLY THE IMPACT OF CLIMATE ACTION ON OTHER AREAS OF POLICY

### 3.6 FOCUSING ON THE TRANSITION PROCESS

We need to bear in mind that what we are trying to achieve is a smooth transition towards a cleaner energy future while keeping citizens on side throughout the process. In that regard,

IT IS MORE PRODUCTIVE TO FOCUS ON HOW TO ENABLE SUCH A SMOOTH TRANSITION RATHER THAN FOCUS SPECIFICALLY ON SUBSIDIES.

The transition period towards Net Zero will have to involve some subsidies – if only to ‘keep the lights on’. This will involve the continued production and use of fossil fuels through the transition period. In some cases, one can even envisage more subsidies being needed.

For example, when half the population is driving electric vehicles, garages dispensing petrol and diesel (which currently already operate to low margins) may well need to be subsidised to allow them to cater for the remaining, if dwindling, number of fossil fuel powered vehicles. Such subsidies may become an essential social benefit and it would be unproductive to condemn them as unnecessary FFS.

APPROPRIATE SEQUENCING OF POLICY INTERVENTIONS IS VITAL.

For instance, diesel subsidies for farmers, fishermen, high energy industries, etc. cannot be removed until there are viable ways for such industries credibly to shift to alternative forms of energy.

All this points to the fact that a focus on FFS (or, indeed, on fossil fuel use in general) may not be the optimal way to approach public policy campaigning. It is more productive to focus on viable pathways to energy transition – and, if one is to maintain credibility at the policy level, not to underestimate or underplay the very real challenges associated with such a transition.

SWITCH THE CAMPAIGNING FOCUS FROM FOSSIL FUELS TO THE ENERGY TRANSITION WHILE RECOGNISING THE CHALLENGES

In Germany, much of the burden for this still falls on the Green Party. A group of ‘planning optimists’ is driven not just by an expertise-based understanding of how fiscal reforms could contribute to CO2 reductions but also by promoting ideas of how to manage the economic and redistributive repercussions of decarbonisation. For instance, they are optimistic that renewable energy generation is competitive and provides a viable solution for German industry, together with hydrogen, energy saving measures, and systems integration.

THE EXTENT TO WHICH SUCH LEADERSHIP ON ‘ECOLOGICAL MODERNISATION’ CAN EFFECTIVELY BRING ALONG OTHER POLITICAL PARTIES AS WELL AS INDUSTRY AND CITIZENS REMAINS TO BE SEEN.

In this particular electoral cycle, this is further hampered by the fact that Green-led ministries and the parliamentary faction find themselves buried under more urgent tasks and crisis management imperatives.

In the UK, neither the Green Party nor the Liberal Democrats, the two parties most committed to environmental policies, currently have any significant political power at national level. Both main political parties, Conservatives and Labour, have 'green' policies as part of their platform and there is some evidence that the narrative is starting to shift to one that presents the green transition as an economic opportunity (see below). For instance, the Labour Party's recently announced a 'green prosperity plan', aimed at *'tackling the climate head on, and using it to create the jobs, the industries and the opportunities of the future.'*<sup>17</sup>

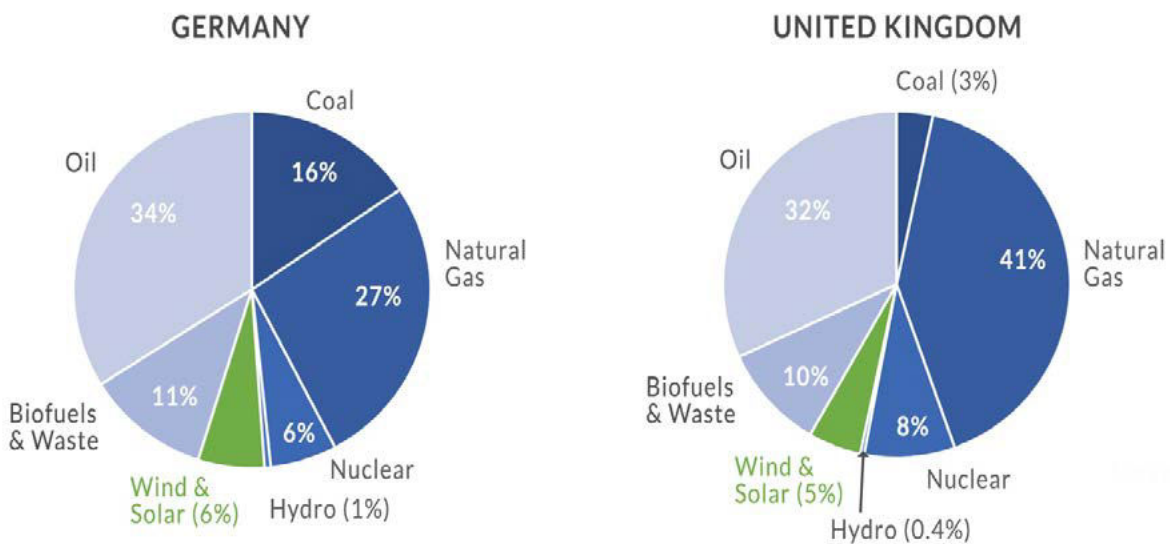
### Challenge and Opportunity

We are still in a fossil fuel dominated world (see figure below) making a smooth and equitable energy transition a challenge as well as an opportunity. All underlining the relative ineffectiveness of the 'stop fossil fuels' line of campaigning and the huge potential still to be had through an effective transition.

THE NARRATIVE IS STARTING TO SHIFT TO ONE THAT PRESENTS THE GREEN TRANSITION AS AN ECONOMIC OPPORTUNITY

## CONTINUED DEPENDENCE ON FOSSIL FUELS: CHALLENGE AND OPPORTUNITY

### Sources of Energy Generation



Source: International Energy Agency, 2020 figures

<sup>17</sup> <https://www.theguardian.com/politics/2022/sep/28/youth-climate-activists-influenced-labour-policies-says-campaign-group>

### 3.7 THE GLOBAL COMPETITIVENESS DILEMMA

COUNTRIES SUCH AS GERMANY REMAIN DEPENDENT ON A GLOBALLY COMPETITIVE, ENERGY INTENSIVE MANUFACTURING INDUSTRY

There has been considerable effort devoted to maintaining German industrial competitiveness. This is one example of how national interests end up obstructing wider agreements. Blocking of the UK's support for creating a level playing field on emissions and tax equalization in the aviation sector by the EU, USA and China is another example.

One former energy minister spoke at length about the effect of the carbon price war on international trade. Acting independently can have devastating effects on industries such as fishing. Yet he believed maritime and airline subsidies to be among the most damaging.

### 3.8 IMPROVING THE QUALITY OF CAMPAIGNING

There is an increasingly strong case for improving the quality of campaigning around the energy transition and supplementing the focus on climate with other narratives that have a chance of gaining more political traction.

ONE HIGH-LEVEL GLOBAL CLIMATE NEGOTIATOR URGES A MOVE AWAY FROM 'GENERIC ABSTRACTS' AS THESE ARE 'NOT HELPFUL' FOR POLICY. HE PUTS THIS DOWN TO 'LAZY CAMPAIGNING' AND 'NOT DOING HOMEWORK'.

Other interviewees agreed that campaigners had failed to convince, being inclined towards performative approaches such as the recent attacks on famous artworks rather than seeking to persuade by making a politically viable case for a green transition.

SOME CAMPAIGNING IS, AT BEST, INEFFECTIVE, AT WORST COUNTER-PRODUCTIVE

Such actions, as well as the road and rail disruptions that interfere with people's everyday lives, may well be counter-productive in that they put off individual politicians from tying themselves too closely with the environmental movement.

Some have also argued that a sole focus on climate will remain insufficient to drive a transition. One community organiser described how 'climate change' remains too abstract a concept to act as a sufficient motivator for people in his community to take action. He did, however, point to significant success in achieving climate-friendly community action when such action was framed as addressing people's everyday concerns.

ITS TIME TO CHANGE THE NARRATIVE AND GO BEYOND CLIMATE AS THE SOLE FOCUS

Some have been even more outspoken. In a recent interview in The Telegraph<sup>18</sup> titled “*The Eden Project’s Sir Tim Smith: ‘Shut the f\*\*\* up about climate’*”, well-known environmental campaigner Sir Tim Smit argues that it is time to move beyond the apocalyptic climate narrative to focus on the practicalities of defining the economic and social opportunities offered by the green transition. He argues for an ‘upbeat, enthusiastic, can-do attitude’ to replace the sense of hopelessness and the fact that the campaigning platform over the past decades has not been sufficiently effective.

HE ARGUES FOR AN ‘UPBEAT, ENTHUSIASTIC, CAN-DO ATTITUDE’ TO REPLACE THE SENSE OF HOPELESSNESS

The positive economic story has been part of environmental campaigning for some years but suffers from two drawbacks:

- *It is dwarfed by the apocalyptic narrative*
- *It has, to date, been put forward in broad generic terms rather than being well defined in its detailed practicalities and political viability*

While all this is being contested, fossil fuel interest groups on both sides of the Atlantic have formed themselves into a sophisticated lobby. ‘Britain’s Global Warming Policy Foundation is a very politically skilled organisation,’ we were told. Another commented on the onshore fracking lobby.

The other big risk today is that climate policy is being transformed into a question of political identity associated with left wing politics and shunned by those on the political right. While most marked in the US, a new Anti-Net Zero cultural war import from America is gaining traction in parts of Europe.

ONCE CLIMATE BECOMES EMBEDDED AS A CULTURE WAR ISSUE, IT WILL BECOME MUCH MORE DIFFICULT TO SHIFT POLITICALLY.

CLIMATE RISKS BECOMING AN IDENTITY ISSUE IN THE CULTURE WAR

<sup>18</sup> The Telegraph, 6 November 2022

## 4. CONCLUSIONS

This project was intended to be focused on how and why fossil fuel subsidies remain sticky despite much campaigning to get rid of them over many years.

Our main conclusions can be summarised as follows:

- *FFS do not stand alone. They are intertwined with many aspects of people's lives which makes their elimination politically challenging and, to date, of limited success*
- *A corollary of that conclusion is that environmental policy does not stand alone either. It is interconnected with economic, industrial, and social policy and needs to be addressed as such if it is to gain more traction more rapidly than it has so far*
- *Policy is primarily a political process not a technical one. Campaigning therefore needs to evolve from technical (or performative) approaches to exploring methods that are politically viable in each individual country where political structures and circumstances are different*
- *Smokers do not continue to smoke because they have never heard of the fact that smoking damages one's health. Similarly, policy action that can benefit the climate (including FFS reduction) is not held up because there is insufficient science around climate change. Rather it is held up because it is highly challenging and the need to keep citizens on side with any of the specific initiatives proposed – many of which are opposed*
- *For policy initiatives to move forward they may need to be re-framed in the context of economic and social policy rather than as pure 'environmental policy'. There is some evidence of this starting to happen*
- *The narrative focused on climate risk and damage may need to be overtaken by a more positive narrative of how an energy transformation can improve economic and social policy as well as being one route towards greater energy sovereignty – an issue brought to the fore by the war in Ukraine*

- *Energy policy is highly complex and politically charged. While there is no shortage of high-quality technical work, campaigning and policy influence need to be based on approaches that are politically sophisticated*
- *There is a significant risk that climate politics are set to become matters of political identity and part of the evolving culture wars. If allowed to happen, they will become ever more difficult to shift*
- *All the above conclusions apply to other environmental issues such as biodiversity restoration – an issue that, in most voters' minds, is even more abstracted from their everyday lives than climate change.*

### The Opportunity

There is little doubt that the world is going through major change economically, politically, socially. Change at both the geopolitical and local political levels. Old 'truths' are increasingly contested.

While such change may, at times, seem chaotic, all change presents opportunities for those who can harness it to their advantage.

The war in Ukraine and its consequences have highlighted the imperative for a major reconfiguration of energy policy. In the medium and longer term this offers a golden opportunity for a shift towards cleaner forms of energy where such exist and to the extent that they represent a viable alternative to existing arrangements.

THERE IS A GOLDEN OPPORTUNITY FOR A SHIFT IN ENERGY POLICY OVER THE MEDIUM & LONG TERM

These opportunities can be harnessed through politically skilled initiatives that go beyond broad abstractions to drive change that is based on both a positive, energising vision of the future as well as well worked out approaches that are technically and politically practicable, while being honest about the limitations and the necessity for the careful sequencing necessary to maintain voter support.

## APPENDIX 1

### GERMAN CASE STUDY

#### SUMMARY

In contrast to the United Kingdom, fossil fuel subsidies are recognized and discussed as an obstacle to climate mitigation policies and green transition in Germany. To our surprise, this view is widely shared amongst economic experts and political elites from left to right.

However, the problem is that hardly anything happens in practice.

While subsidies for coal production and use have been phased out, other fossil fuel subsidies for industry, for car users, for air traffic, and agriculture remain untouched. Parties are concerned about potential reactions from important if minor electoral groups, while key federal ministries, the chancellor, and powerful groups within the respective major parties (CDU and SPD) act as protectors of industries that rely on subsidized energy or the sale of products that are rendered more attractive by subsidies (i.e. cars).

Impetus for reform would need to come from the Green party with support from environmental expert and lobby groups; these are the “change-agents”, who can count on strong popular support for climate mitigation policies, who could enlist pro-climate mitigation advocates from other parties in the project, and who have by now developed sophisticated proposals for how to manage transition problems and distributive effects associated with cutting subsidies.

There exists a high risk, though, that current crisis management and its effects on political dynamics will render the implementation of a consistent reform package inopportune during this electoral cycle.

There also looms a larger risk as a significant share of Germans is less optimistic about the benign economic consequences of green transition than the European Commission or other European populations, while Germans are equally concerned than many other populations about higher energy costs.

#### ANALYSIS

In Germany, subsidies on fossil fuel use and consumption play a major role in industrial and social policies. At the same time, fossil fuel subsidies (FFS) have been identified as obstacles in meeting the country’s decarbonization goals.<sup>19</sup>

The OECD places German FFS at around €35 billion while the German Environmental Agency (Umweltbundesamt) reckons that various subsidies and tax expenditures worth €60.6 billion harm the climate directly.<sup>20</sup> The major share is in fossil fuel-based mobility, energy generation (e.g. electricity) industrial consumption, and agriculture. There also exist major subsidies in the building and construction sector whose impact on greenhouse gas emissions is significant but less direct. Based on a wider conception of subsidies, the think tank Forum Ökologisch-Soziale Marktwirtschaft calculates that 100 million tons of CO<sub>2</sub>eq could be saved if fossil fuel subsidies were scrapped.<sup>21</sup>

Germany has made various pledges to reduce FFS, e.g. by signing the G7 treaty of May 2016 and again the declaration at the COP26 meeting in Glasgow, in which participants declared the intention to phase out “inefficient” subsidies for oil, gas, and coal until 2025; the general aim to reduce such subsidies was also expressed in the government’s 2016 “climate action plan 2050”.

<sup>19</sup> After a ruling by Germany’s constitutional court, the government has committed in law to reduce greenhouse gas emissions by 55 per cent by 2030; the country aims to be “net zero” by 2045.

<sup>20</sup> Andreas Burger & Wolfgang Bredschneider, *Umweltschädliche Subventionen in Deutschland, aktualisierte Ausgabe 2021*, Umweltbundesamt, Dessau-Roßlau 2021.

<sup>21</sup> Forum Ökologisch-Soziale Marktwirtschaft, *Zehn klimaschädliche Subventionen im Fokus*, November 2020.

Since 2015, the Finance Ministry produces regular reports to assess subsidies in terms of sustainability criteria. The new Coalition Agreement between Greens, Liberals, and Social Democrats from November 2021 states that *“we want to gain additional fiscal room of maneuver by cutting unnecessary, ineffective, and environmentally harmful subsidies that damage the climate.”*<sup>22</sup>

Particularly the Green party, environmental/climate policy think tanks and NGOs, and the German Environmental Agency, have been pushing for such reductions over years, with ever more detailed calculations (of fiscal and environmental impacts) and proposals for reform.

Yet, despite public declarations and a high material and symbolic significance attributed to FFS in the context of climate change mitigation, little has happened at the policy front. The only real area of change has been in coal and lignite, where subsidies have been reduced as part of an agreed plan to phase out these extremely carbon-intensive sources for electricity generation until 2038 (in reaction to an ever more apparent failure to meet Germany's decarbonization targets that became clear around 2015-6).

Moreover, the Ministry of the Economy and Climate under new minister Robert Habeck has started to reshuffle funds for construction from new buildings to refurbishments and retrofitting of existing housing stock to reduce CO2 emissions in that sector.

In other areas, hardly any progress is evident, as even official bodies like the European Commission observe. On top of that, the new social democratic-green-liberal coalition has reacted to the current energy crisis with several significant fiscal measures that directly support fossil fuel consumption.

Long-distance commuter tax rebates that privilege car use have been hiked; a three-month cut in fuel taxes was introduced from June to August 2022 (worth 3.15 billion); a planned increase in CO2 charges for domestic heating and vehicle fuel use has been suspended; and a reduction in electricity and energy taxes for energy-intensive industries worth 1.7 billion was prolonged until the end of 2023.

This is despite a long-standing discussion in Germany on the need to switch from consumption-focused subsidies that incentivize fossil fuel use to direct fiscal support for firms and households that encourage (and aid in) energy transition (e.g. electrification) and savings (through efficiency-enhancement measures).

Most worryingly, the government does not seem to have a plan of how to redesign of subsidies for energy consumption, mobility, and agriculture, apart from a pledge to introduce a still undefined “Klimageld” (climate dividend). In times of extremely alleviated uncertainties, and as a matter of path dependency, reactive politics and responsive policy making reign.

Interest group and electoral politics combined with entrenched policy processes make FFS very sticky and explain a persistent gap between intentions and action. Energy-intensive industries and those selling carbon-goods (primarily cars) traditionally have a strong footing in the Christian-democratic (CDU) (e.g. through Mittelstandsunion) and social democratic (SPD) party (through industrial workers), and they enjoy privileged access to the highest echelons of government – big industry has the “chancellor's ear”, as one interviewee put it.

Just as important is the fact that federal ministries and ministers have significant independence and policy leverage in their areas of responsibility, and these ministries regularly resist reforms that contradict the interests of dominant interest groups in their sectors; this is particularly the case for the Transport (with strong ties to the automotive industry) and Agriculture Ministries.

Unfortunately, this situation is worsening, if the chancellor is not assuming his leadership role and guiding the way; ministers and ministries are acting in their (or their peer's) own interest, while the entire economy and population have no long-term perspective, which makes planning and investment a tedious task.

<sup>22</sup> “Mehr Fortschritt wagen. Bündnis für Freiheit, Gerechtigkeit und Nachhaltigkeit”. Koalitionsvertrag 2021 – 2025 zwischen der Sozialdemokratischen Partei Deutschlands (SPD), BÜNDNIS 90 / DIE GRÜNEN und den Freien Demokraten (FDP), 24 November.

Last but not least, the two mainstream parties hesitate to cut subsidies that benefit consumers, who make up significant parts of their electorate and/or whose political support is crucial in maintaining ever more fragile electoral coalitions. Among these are workers in subsidized industries; residents in rural areas, who rely on combustion engine cars; and poorer groups, who benefit from fuel subsidies (e.g. commuter tax expenditures and reduced diesel fuel taxes). In the current environment of extremely alleviated energy prices, all parties agree that scrapping subsidies would be “*political suicide*” and bears the risk of assuming responsibility for a deliberate process of deindustrialization and job losses.

Moreover, even climate policy advocates acquiesced to the idea that higher energy prices will perform the work of disincentivizing fossil consumption and help the government achieve its net zero targets, without need of deliberate reform.

There is also an emergent perception that, should the government press too hard with measures that have cost-implications (e.g. raising/expanding CO2 charges), the conservative party could latch onto that by openly questioning climate change mitigation policies that it could frame as harmful for employment and growth (as increasingly happens elsewhere, e.g. the UK). In case the government or reform leader is not clear and strong enough in their argument, this might lead to social and economic unrest.

In this constellation, much depends on the Greens to assume leadership in the project of reducing FFS. This is the party, who has most explicitly committed to such reforms and whose electorate most clearly supports (if not expects, and would benefit from) them.

Green leadership could sway those parts of social democrats and liberals (and sometimes even conservatives), who quietly support the idea of reducing FFS but do not want to, or cannot, invest political capital in this project; in general, public support for (even costly) climate policies is (still) high in Germany, offering a window of opportunity for green leadership.

Finally, with their linkages to think tanks like Agora Energiewende and Forum Ökologisch- Soziale Marktwirtschaft, officials in green-led ministries and members of the green parliamentary fraction make up a unique group of “*planning optimists*”. This optimism not just entails an expertise-based understanding of how fiscal reforms could contribute to CO2 reductions, which is much more prevalent amongst green party members than elsewhere; Greens also promote ideas of how to manage the economic and redistributive repercussions of decarbonization.

For instance, the Greens are optimistic that renewable energy generation is competitive and provides a viable solution for German industry, accompanied by hydrogen, energy saving measures, and systems integration. The idea is to guide industry with regulations (e.g. a ban on combustion engines), de-risking, and fiscal incentives combined with alternative forms of support (e.g. “*Contracts for Difference*”) while moving away from Germany’s passive industrial policy strategies; for instance, one member of parliament was clear that industry requires direction to invest long-term, rather than political “neutrality” for technological choices.<sup>23</sup>

The Greens have also pushed for plans to introduce a “*climate dividend*” (lump sum payments to households) that could cushion persistently higher energy costs and eliminate the regressive distributional effects of increased consumption charges.

The only real hope for scrapping fossil fuel subsidies in Germany thus lies with a broader, longer-term “*ecological modernization*” coalition with the Green party at the centre, significant expert/lobby support, and resonance in significant shares of the electorate.

In this particular electoral cycle, there are several risks for these ecological modernists, though. For instance, the critical implementers (in green-led ministries and the parliamentary fraction) might remain buried under more urgent tasks and crisis management imperatives and/or unable to reach their primary government sponsors (above all, Robert Habeck).

<sup>23</sup> By contrast, the current FDP transport minister Volker Wissing states that government should remain “neutral” on technological choices by industry.



Moreover, the respective ministers might be too weak politically to withstand opposition from other cabinet members, who then kill reforms. Moreover, to strengthen their cause and render reforms sticky, the ecological modernization advocates will need to introduce strategic changes that could tilt the policy process in favor of decarbonization – e.g. by advocating elements of green budgeting and stronger procedures for subsidies monitoring.

The problem here is that the structure of German federal bureaucracy is biased against consistent and coordinated planning due to the entrenched power and orientations of ministries as well as the imperatives of coalition governments. Moreover, the crucial finance ministry is under leadership of the FDP, and Christian Lindner might simply block reform initiatives despite the coalition's commitment to policy progress and administrative reform.

Beyond the electoral cycle itself, huge questions about the economic and political viability of ecological modernization remain for an industrial, export-oriented economy like Germany. Will German energy-intensive industry become competitive with reliance on (currently more expensive) green solutions, like green steel? Or will falling fossil prices render traditional production methods much cheaper (in the absence of consistent carbon pricing and/or tariffs that depend on EU reforms), giving producer countries in other world regions (that are also geopolitical rivals) a competitive edge?<sup>24</sup>

Moreover, reducing fossil fuel subsidies for, and increasing carbon charges on, consumers ultimately only makes sense from a climate policy angle if these consumers gradually reduce their general consumption levels or at least significantly alter what they spend money on (e.g. meat; long-distance travel; detached houses etc.). Otherwise, it is hard to see how ecological footprints could be made smaller.

This means that the promise of ecological modernization might be too optimistic, and that at some point a discussion on bans, down-scaling and welfare losses (as understood under current consumption society criteria) will need to be had. If people (voters) in Germany realize that first steps to reach ecological sustainability ultimately hold implications that they reject, the still rather strong support for green policies could falter; this is already indicated by surveys, which show that while large majorities in European populations support climate mitigation policies, they are unwilling to pay more for energy consumption.<sup>25</sup>

For now, the best hope thus is to bet on a rather benign narrative that has support in critical parts of industry and broad swathes of the electorate, but may require to be rewritten in the years to come.

<sup>24</sup> Germans are already more skeptical about the idea that a green transition will make companies more competitive than other Europeans and are in the group showing least support for climate-related corporate regulations; see Special Report 513, "Climate Change", Eurobarometer 2021, and Special Report 527 "Fairness Perceptions of the Green Transition", Eurobarometer 2022.

<sup>25</sup> Special Report 527 "Fairness Perceptions of the Green Transition", Eurobarometer 2022.

## APPENDIX 2 UK CASE STUDY

### A NARRATIVE HISTORY OF FFS IN THE UK

The outlook for fossil fuel subsidies in the UK is riddled with uncertainties. The war in Ukraine, launched by an aggressive petro-state against a neighbour, has changed all previous assumptions and created an energy market that is currently indivisible from politics. Things are unlikely to return to any kind of stability in the short term; yet while there are obvious dangers there are also potential benefits.

Politicians now see an accelerated green transition as vital to future energy security, and assess renewables as delivering “faster than anyone expected.” Certainly, renewable electricity displaced about £6bn worth of gas in the UK alone last year, the centre-right think-tank Onward estimates.<sup>26</sup>

A major UK electricity company has announced that it is helping to deliver the first British home so well equipped with green technology that it will never generate a fuel bill.<sup>27</sup> Yet the uncertainty has triggered a revived focus on fracking, and called for the expansion of bulk LNG storage.

Officials with an overview of the transition also point to potential problems ahead for renewables with choice sites for wind power running short, despite the UK being the leader in offshore wind, with 28.9 per cent of the world’s offshore turbines.<sup>28</sup>

Even before these developments, the debate around fossil fuel subsidies had become muted. Politicians and their advisors appeared to accept they were an integral part of the UK financial landscape. A Department for Business, Energy and Industrial Strategy (BEIS) official described reform of FFS as “not even a conversation”. Several reasons were given for this.

In the UK, the main difficulty is that that most of the FFS “are almost all in the control of the Treasury,” said one former minister. They are not a DECC (Department of Energy and Climate Change) responsibility and they and other departments are constantly going into battle with the Treasury – mainly about budgets – and there hasn’t been any opportunity to take them on over their entrenched positions on their own responsibilities. Government officials we spoke to could remember no occasions when FFS was discussed seriously.

Another EIS official put it simply: ‘As long as revenue exceeds tax breaks, they will continue to exist’.

Despite this, there is an acknowledgement that the UK has been doing relatively well in eliminating FFS – compared with most other European countries. The exceptions are:

- ***Subsidies to encourage investment, in North Sea drilling, and decommissioning.***
- ***Tax concessions for red diesel for farmers and the fishing industry.***
- ***Motor transport, building and policing roads and motorways – and airlines and flights.***
- ***Air fuel.***
- ***Cold winter payments for older people.***
- ***Subsidies to struggling parts of high-energy industries like iron and steel, aluminium or cement.***
- ***Subsidies to mitigate inflationary energy costs for consumers.***

For decommissioning and North Sea exploration the argument was about: “getting the balance right between taxation and support for investment given current level of oil prices... keeping it profitable for the sake of Scottish industry,” according to one former minister.

<sup>26</sup> Financial Times August 23 2022: Gaslighting Finds a Whole New Meaning with this Energy Crisis by Pilita Clark <https://www.ft.com/content/232d2cc2-a489-4a8c-ace9-1edb86ba9de0>

<sup>27</sup> Financial Times June 3 2022: Octopus and Ilke launch clean energy scheme with no bills for householders by George Hammond. <https://www.ft.com/content/b81307f1-94cc-4b0f-9b64-1ac072dfe9dd>

<sup>28</sup> The Sunday Times, August 28 2022: An Offshore Wind Revolution has Begun – can it Meet the UK’s Power Needs by Ben Spencer: <https://www.thetimes.co.uk/article/an-offshore-wind-revolution-has-begun-can-it-meet-the-uks-power-needs-ph6w5bt09>

Removing farm subsidies and weaning fishing communities off their dependence on red diesel was considered “very hard”, largely because these communities are already suffering economically, and there are few alternatives (few practical-sized electric tractors or fishing boats, for example).

Previous governments accepted four clear energy policy objectives – keeping the lights on, affordability for low-income groups, environmental benefit and self-sufficiency. After the 2008 financial crisis, things became more complicated.

Prime Minister Boris Johnson, allegedly influenced by his wife, Carrie, regularly expressed enthusiasm for the green agenda, but – as one of our interviewees told us – he “has been unbelievably ineffective – nothing has happened”. First indications are that the new administration under Liz Truss may view green policies as ‘anti-growth’. Only a few weeks in government, she deemed a £15 million energy-saving advice campaign proposed by the government’s Climate Change Committee this winter unnecessary. Labour claims an awareness campaign could save households up to £8.4bn – a saving of £300 per household.<sup>29</sup>

At last year’s COP 26 in Glasgow, the final communique included a commitment to phase out FFS - a similar commitment is in the draft wording of the COP 15 on the biodiversity targets, which should be agreed at the UN Conference on Biological Diversity (CBD) in Canada in December.

The most recent available figure for total subsidies (as defined by the Organisation for Economic Co-operation and Development) provided by the UK government is around £14 billion.

The part they play in actively harming the climate has not been quantified but other uses have been assessed. For example, in May of this year the green think tank E3G calculated that billions of pounds given away in a tax break for UK oil and gas exploitation could have permanently cut the energy bills of 2m homes by £342 a year if invested in insulation measures.<sup>30</sup>

The analysis did not, however, address the issues related to sequencing and timing.

## WHY WE STILL HAVE FOSSIL FUEL SUBSIDIES.

We have been offered a number of different reasons:

*The sheer interconnectedness of subsidies with people’s lives:*

Most UK households are currently reliant on gas boilers for heating and gas-fired power stations generate 44 per cent of electricity.<sup>31</sup> The government has pledged to install 600,000 heat pumps a year by 2028 by investing £60 million in innovation to help to make them cheaper (they currently cost an average of £10,000), smaller and easier to install. But these long-term targets are of no help immediately and the government has opted to pay an estimated £150 billion to cover the cost of a two-year price freeze to cut families’ energy bills. It will mean that for every pound a household spends on gas and electricity the government will pay about 75p in subsidy.<sup>32</sup>

One UK politician told us: “People don’t realise the complications. Making nitrate fertiliser, for example, requires natural gas so if the gas price goes up so does the price of fertiliser, and if fertiliser goes up, food prices will go up and, basically half the world, is dependent effectively on nitrate fertiliser and we don’t yet have a solution.”

29 The Guardian, Sunday October 9, by Michael Savage, Shanti Das and Rebecca Brahde: Anger as Truss ignores her climate advisers’ call for energy-saving drive. <https://www.theguardian.com/society/2022/oct/09/anger-as-trussignores-her-climate-advisers-call-for-energy-saving-drive>

30 The Guardian, May 1 2022: Sunak’s UK oil subsidy could have insulated 2m homes, says thinktank by Damian Carrington. <https://www.theguardian.com/environment/2022/may/31/sunak-uk-oil-subsidy-couldhave-insulated-2m-homes-says-thinktank>

31 The Times Saturday September 10 2022: Why are our Energy Prices So Complex? by Tom Calver and Ben Spencer. <https://www.thetimes.co.uk/article/why-are-our-energy-prices-so-complex-nmxkhj0gv>

32 The Times October 16 2021: Pledge to Slash Cost of Green Heat Pump by Oliver Wright. <https://www.thetimes.co.uk/article/pledge-to-slash-cost-of-green-heat-pump-5khnhm8> and The Times September 9 2022: Two-year price freeze to cut energy bills by £1,000 by Oliver Wright. <https://www.thetimes.co.uk/article/two-year-price-freeze-to-cut-energy-bills-by-1-000-3gwwbcbp6>

Another said: *'Subsidies are incredibly difficult to withdraw. It is just politically difficult to make people's lives harder. We live in a democracy and politicians will know that if they make it more costly to live or get to work or to do work without the alternatives being there, there will be public anger, and they might be voted out of office. It's basic human nature.'*

*Lack of interest among politicians, key office holders and officials.*

One former minister described his astonishment, on being elected, at discovering that 'really motivated' colleagues, committed to fighting climate change, numbered only around 25 out of a 650-strong House of Commons.

High-level climate negotiators spoke of discussions that revealed politicians' unwillingness to take unpopular decisions. In a reference to the 2018 French yellow vests protest movement that was initially prompted by rising crude oil and fuel prices, one said: *"Politicians are very frightened of doing something in a four-year-period of office...you could end up with a gilets jaunes situation."* Already more than 100,000 people have signed up to the online Don't Pay UK campaign. The group plans mass non-payment of energy bills if 1 million sign up and government fails to address crisis.<sup>33</sup>

A leading economist explained the difficulty of 'selling' green energy:

*"People fundamentally don't seem to believe that renewables are now the cheapest source of power and therefore this whole scramble to try to find new sources of oil and gas doesn't make any sense.... I don't think we have an energy crisis – we have a climate crisis. Renewables are becoming ever cheaper and why people don't turn around to build the cheap thing and just worry about subsidising the expensive thing I don't know. People have to hear arguments lots of times to believe them... if we kept saying 'renewables are getting ever cheaper' instead of saying 'fossil fuels are getting ever more expensive'...perhaps they would start to believe it."*

*Single countries are rarely able to shift things by themselves.*

It is too easy for narrow national interests to obstruct wider agreements. The UK, for example, supported a plan by the International Civil Aviation Organisation (ICAO) to create a level playing field on emissions and tax equalisation, but the EU has been hesitant, and the key initiatives blocked by the USA and China.

One former energy minister spoke at length about the effect of the carbon price war on international trade. Acting independently can have devastating effects on industries such as fishing. *"People will say, 'Well, they do that over there for their fishing industry and we have to compete with them. On regulation they say 'If you do that to us, you don't get any benefit, because they can then get the fish.'"*

He believed maritime and airline subsidies to be among the most damaging:

*"Both have cheap fuel and that creates an incentive to send goods distances that they probably ought not to if the market was sending true signals and in the end you get more pollution and environmentally damaging economic activity."*

Lazy thinking by campaigners.

One high-level global climate negotiator urges a move away from 'generic abstracts' as these are 'not helpful' for policy. *"You hear less about campaigning against fossil fuels today than you did in the previous decade."* He puts this down to 'lazy campaigning' and 'not doing homework'...

At the same time, fossil fuel interest groups etc., have formed themselves into a sophisticated lobby. *'The Global Warming Policy Foundation'* is a very politically skilled organisation,' one interviewer told us. Another, commenting on the onshore fracking lobby and calls to end a 2019 moratorium on shale gas fracking in England, said: They are very good, very effective at convincing newspaper editors that fracking is a silver bullet.' He also pointed to a new Anti-Net Zero cultural war import from America' gaining traction among young British followers.

<sup>33</sup> The Guardian, August 11 2022: More than 100,000 people join Don't Pay UK in protest against energy price rises by Jane Clinton. <https://www.theguardian.com/business/2022/aug/11/more-than-100000-people-join-dont-pay-uk-to-protest-against-price-rises>

Some consider Russian leader Vladimir Putin to be effectively managing the green transition for us. Others are more sceptical. An oil specialist told us:

*"I sit in a lot of seminars about the effects of the Ukraine war and they often conclude 'Oh, it's speeding up the transition' but I think that's wishful thinking. Inflation and the rise of the cost of basic goods, stress on households... when it comes to those kind of dilemmas the bottom line is what really matters to most households. People will just expect governments to do whatever they have to do to lower energy prices.... We could say, if we end up with a global recession, that it will reduce energy consumption but it will also restrain the amounts of money governments have to invest in transition so it's complicated."*

## CONCLUSIONS

Our conversations lead us to conclude that:

### **Not all subsidies are bad**

It isn't as if governments should not use their resources to change the political and economic landscape. They should. Nor is it that FFS are bad because they are subsidies. Some are purely about looking after disadvantaged communities or sectors – they don't all require competitor nations to follow suit.

There may even be reasons why we will need to subsidise some aspects of a transitional period in the economy before we reach net zero.

### **We need to make sure there is capacity in the system**

The transition period towards Net Zero will have to involve some subsidies – if only to keep the lights on. This may well involve continuing to produce some oil and gas, and perhaps even coal, for the interim period. One former minister put it like this to us:

*"What happens when 50 per cent of the population of the UK is driving electric vehicles? How is anyone going to be able to afford to keep open a petrol or diesel garage?"*

*They operate on low margins as it is – which means they suddenly all have to close. I can see a moment where we're going to have to subsidise keeping fossil fuels because we want petrol stations open as a social benefit during the transition."*

### **We also need to distinguish between different kinds of subsidy**

A great deal of confusion swirls around the word 'subsidies'. One financial expert told us it can mean four different things:

- **money handed directly to the consumer**
- **some form of special taxation**
- **money given to preserve energy security**
- **financial support where there is a 'learning curve' or research and development to sustain a business until it reaches the point of financial viability**

All these are lumped together as 'subsidies' yet they are very different things. In the view of one financial expert, they all have one effect in common, which is to distort the market. The problem around how we define FFS is because some subsidies may be useful, even to bring net zero closer. We might, for example, find ourselves attempting to reduce demand by subsidising home insulation or electric vehicles.

Most subsidies are traditional tax breaks, although since the invasion of Ukraine and fuel inflation around the world, billions in government cash is now flowing directly into the energy companies in compensation for the price cap introduced in October.

Some involve payments to vital or disadvantaged groups, like older people or small farmers – which would have to be replaced by other payments – although they are ostensibly for fossil fuels.

### **Define FFS more usefully**

For example, we find ourselves attempting to reduce demand by subsidising home insulation or electric vehicles – though the Treasury is generally opposed to this. There are also massive revenue implications – and you could be mainly supporting those who are better off.

The problems emerge if goods or services are not taxed to the full value of the carbon tax. In other words – when we know the carbon price necessary to drive the economy towards transition by 2030/2050, then anything which is not taxing fossil fuels by that amount is a subsidy.

One former minister told us: *"Now that is probably not quite the definition that either the Treasury or the OECD use, but I think it's a defensible economic definition because it is basically saying that the subsidy is what we pay for it, once we have internalised all the externalities from fossil fuel emissions."*

*"That means to internalise the emissions costs by using the carbon price in exactly the same way as, traditionally, the public sector has assessed investment projects and so forth on the basis of a reasonable rate of return and some sort of social rate of return, cost benefit analysis."*

There are difficulties about cost-benefit analysis, of course. But we don't need to go into that here...

**'Politically correct' reforms are less important than the sequencing of vital changes**

*"You need to think about the politics - the fact that losers scream more than winners applaud," said one former minister. "When you do the rest of it, having done the sequencing, you also need to do it in a big bang and make sure that you have lined up lots of people applauding because there is a rather marvellous phrase from the former American president Woodrow Wilson which says: 'If you want to make enemies, try to change something.'"*

He described how potentially good schemes risk failure if not carried through or communicated clearly to the voter. The Green Deal, for example, promoted by Lib Dem politicians during the Coalition was scrapped by the Tories and many voters never properly understood that the scheme was going to be paid for out of savings on people's energy bills:

## WHY THE GREEN DEAL FAILED

The Green Deal was a short-lived 'pay-as-you-save' energy efficiency scheme, introduced in the UK by the coalition government in 2013 at the instigation of the Liberal Democrats. Government funding support was withdrawn in July 2015 after embarrassingly low take-up. A National Audit Office review later concluded that the £240m cost did not generate any additional energy savings.

The scheme provided loans for homeowners to undertake efficiency measures, recouped through regular energy bills, in theory funded through the savings generated. No grant or subsidy was offered and interest rates were set higher than 'high street' rates. The high cost meant few measures were financially viable and the complexity of linking a loan to a particular property for up to 25 years deterred take-up. Initial hype claimed some 14 million homes would benefit; in the event only 14,000 were retro-fitted using Green Deal finance.

The UK scheme has been compared unfavourably with the German EnEv programme which ran until 2010. That was offered to landlords and public bodies rather than individual homeowners and provided both grants and subsidised interest rates. Some 200,000 homes a year benefited, with substantial CO<sub>2</sub> emission savings."

"The only way to make green taxes saleable is to ensure that people believe that the revenue raised from it will be handed back in other ways. It is key to show that money taken in green taxes will be handed back."

In the same way, cancelling subsidies for red diesel will need to wait until affordable alternatives are available.

### **What then should we do?**

The world is not short of opinions as to what 'should' be done. Yet most such opinions come to nothing in the messy realities of the real world.

One former energy minister advocated swift action coupled with clear communication of the rewards:

*"If I had been chancellor, I think I would have done a major rejig. I was very keen on green taxation and on sin taxes and tax reductions. I would have done it all in one go – bang! The reason chancellors don't do things is because they fear that the losers will scream louder than the winners so you have to get to a position where the winners can clearly see the benefits, because you're bound to have some losers."*

An environmentalist politician said the answer lay in long term planning, fearing the government is stuck in 'time-warp thinking':

*"It is very disappointing to see, in their Energy Security Bill, which has had its second reading in the Lords, that there was nothing in there around increasing more renewables and there was nothing in there about home insulation – so I think at the moment the government is stuck in a sort of a time warp of thinking 'we've got an energy security crisis...we need to find new sources of energy... What do we know that works quickly?' Whereas actually, they need to be thinking about cutting demand and what can we do that, in the long term, will mean that we are resilient when this happens again?"*

Integrating green energy into grids designed for fossil fuels requires investment. One interviewee urged politicians to work with specialists to seek ways to overcome the obstructions to peoples' lives during the transition such as re-utilising the gas pipes underneath our cities and towns with non-fossil fuel heating.

*"The really big issue is between electric heating and gas heating," he said. Moving to electric and having to rip out your gas boiler and put an electric powered heat pump in is too disruptive. "The thing about heat pumps is that the barrier for their deployment in most homes is quite high...not that we shouldn't try. I'm into heat networks I think they are less disruptive...that's why I would love there to be a possibility for hydrogen."*

Yet other interviewees dismissed the potential of hydrogen. One described it as 'a craze' and 'largely a bail-out package for the fossil fuel industry', adding:

*"It's inherently more efficient to electrify than to use hydrogen...that's basic physics. If you have no choice, that's the last resort so there is absolutely a niche for hydrogen but that's very different from 'Creating the hydrogen economy' not least of which because hydrogen is a gas that escapes easily and is a very heavy greenhouse gas...very heavy so it's really nasty if it gets away."*

One oil industry specialist, speaking about the green transition, said:

*"Globally it is being discussed - that is incredibly significant. Things take a long time. To get from when we had the Paris agreement in 2015 and where we are now... It was only in 2015 that global leaders started talking seriously about climate change. It was only at COP 26 that they made this commitment to phase out 'inefficient' fossil fuel subsidies. So, yes, I think there has been progress made but we are at the foothills of a very steep mountain and we haven't got much time..."*

In short, it is unproductive to gather all this spending together under one heading - fossil fuel subsidies - because most governments regard them as a variety of payments to support specific groups or specific industries facing unaffordable energy costs.

It may be, in those circumstances, that campaigns to 'eliminate FFS' is not a productive approach - and may actually be counter-productive. We need instead to define FFS as anything that frustrates a just and low-hardship transition to a different energy mix, while taking into account the state of the different technologies, the challenges faced by different industries and different consumer groups, and the mammoth difficulties of transforming our whole energy system.

	UNITED KINGDOM Sources: OECD report on support for data or estimates. <sup>34</sup>	GERMANY Sources: OECD report on support for data or estimates.. <sup>35</sup>
	£ millions	€ millions
<b>PRODUCTION SUBSIDIES</b>		
Capital allowance on exploration and equipment costs for oil and gas drilling	0 (down from over £1bn in 2020)	0
Support for coal production	N/A	4,785 (not including miners' bonuses)
Ring-fenced expenditure supplement (2020 figure)	17 (Designed to support shale gas exploration)	N/A
Manufacturer's privilege	0	339 (for energy used to generate energy – since 1930). 2020 figure...
Tax rebates & exemptions for electricity production	120 (for CHP using fuel to produce things other than electricity, like heat) 134 (on energy destined to be used abroad)	1,527 This came into effect in 2018 316 (2020 figure) Reduced CHP fees for manufacturers and energy-intensive industries
<b>CONSUMPTION SUBSIDIES</b>		
Kerosene (mainly air fuel)	2,382 (2020 figure)	231
VAT concession for domestic heating	3,749	Not listed by OECD
Reduced taxes for high energy manufacturing industry	972	331 73 (other manufacturing categories not using high energy) 420 (energy tax relief)
Reduced taxes on red diesel	2,130	440
	(incl forestry)	
Exemptions from climate levy/energy tax for some forms of transport	45	71 137 (inland waterways)
VAT exemption for international flights	'Missing' from OECD table	3,957
Other airline support	Not clear how much, but it isn't zero	40 regional airport grants 70 VAT reductions on gas Reduction of air traffic control fees through state subsidies (not quantifiable).
Equalisation scheme	N/A	183 When they introduced the German energy tax, they reduced pension contributions to compensate. This pays out to companies that need more relief.
Winter fuel allowance	1,968 (2021/2 figure) <sup>36</sup> 99 (cold weather payments to claimants)	Not listed by OECD
Shipping	??	25 (2020 figure) Low cost loans for financing building of cruise ships through the state-owned credit institute for reconstruction (KfW-IPEX Bank)
Energy tax relief for diesel fuel	N/A	8,202
Car subsidies	Mostly hidden because road tax fails to cover the costs	6,000 commuting allowance plus other hidden subsidies (2020 figure)
Allowance for use of private car for business	??	3,100 (2020 figure)
Tax privileges for special contract customers when paying electricity concession fees	N/A	3,600



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	£ millions	€ millions
<b>CONSUMPTION SUBSIDIES - CONTINUED</b>		
Reductions in climate levy for businesses with energy agreements in place	254	N/A
<b>DECOMMISSIONING SUPPORT</b>		
Tax relief on decommissioning	219 Against petrol tax (PRT) paid in previous years	N/A
Ring fencing tax relief on oil and gas, for decommissioning	1,600	N/A
Transfers of tax history	-5 This allows companies to sell oilfields they want to decommission, along with their tax histories.	N/A

34 [https://stats.oecd.org/Index.aspx?DataSetCode=FFS\\_INDICATOR\\_DETAILED%20](https://stats.oecd.org/Index.aspx?DataSetCode=FFS_INDICATOR_DETAILED%20)

35 [https://stats.oecd.org/Index.aspx?DataSetCode=FFS\\_DEU](https://stats.oecd.org/Index.aspx?DataSetCode=FFS_DEU)

36 Outturn and Forecast tables: Spring Statement 2022 (XLS). Second Outturn and forecast table (1b), Spring statement 2022 real terms, 2022/23 price.







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[www.radixcbps.org](http://www.radixcbps.org)

[ron.soonieus@radixcbps.org](mailto:ron.soonieus@radixcbps.org)

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