Session 1: Financial Incentives for Climate Change Mitigation and Adaptation

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Introduction

• Financial Incentives to farmers for climate change mitigation likely to become more prevalent after Copenhagen
• Appropriate time to look at coherence with farm policies
• Which instruments are likely to be the most effective?
• What might be the distribution of costs and benefits?
• Are these likely to be consistent with WTO obligations?
Policy Approaches

• Reduction of GHG emission from crop and livestock production
• Absorption through carbon storage (sequestration)
• Encouragement of alternative crops, including biomass for alternative fuels
• Use of alternative fuels in farm (and processing) operations – co-generation
Instruments available

- Performance standards
- “Best Practices”
- Taxes on emissions (carbon tax)
- Cap-and-trade
- Subsidies
  - for sequestration
  - for alternative crops
  - cross-compliance with standards
  - for research and extension
Effectiveness

• Performance standards are difficult to apply to farming: monitoring performance likely to be too expensive (though one can use proxies)
• Best Practices more feasible: feeding practices, minimum tillage, land reserves, tree planting (build on current conservation policies)
• Carbon tax: only addresses the energy use issue
• Cap-and-trade: difficult to administer for small-scale agriculture
Subsidies

• Simpler to administer: self-identification
• Effective if correctly targeted
• But may be challenged by competitors
• May fall afoul of trade rules
  – Agreement on Subsidies and Countervailing Measures (SCM)
  – Agreement on Agriculture (AoA)
Constraints on Subsidies

• SCM
• Defines subsidy
  – it must entail a financial contribution;
  – it must be made by a government or any public body within the territory of a Member; and
  – it must confer a benefit.
• Defines Specific Subsidies
• Some Specific Subsidies Prohibited
  – Contingent on exports
  – Local content conditions
• All others Actionable – including climate change subsidies that are specific
Constraints on Subsidies

• AoA
• Constrains “all of [a member’s] domestic support measures in favour of agricultural producers.”
• Distinction depending on putative degree of trade distortion
  – Green box – non or minimally trade distorting
  – Blue Box – tied to supply control
  – Amber Box – reduction required (except de minimis)
Subsidies in Green Box?

• No, or minimal, effect on production, trade distorting effects
• Publically funded, not from consumer, and not a price support
• For environmental payments:
  – Clearly defined environmental program
  – Limited to extra costs/loss of income from complying

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Sequestration Subsidies in Green Box?

- Sequestration subsidies not related to price, not financed by consumer, and part of a defined program
- But are they related to the additional costs?
  - What does it cost to decide not to plough up a pasture?
- Costs are “opportunity costs” not easily counted
- Farmers may need incentives to join scheme
Subsidies with Cross-Compliance in Green Box?

• Subsidies with Cross-compliance conditions
  – will usually have no (positive) output effects,
  – not consumer financed

• But they do not reflect additional costs
  – Cross compliance usually comes as an additional condition to encourage those programs
Cross-Compliance Subsidies in Green Box?

• Cross-compliance subsidies may be notified as Direct Payments
  – with cross-compliance as a convenient link to provide justification for direct payment

• Compatible with green box if not linked to current output or prices – and no production required
Biofuels Tax-credits as Green Box subsidies

• Is ethanol an agricultural product? If so, tax credits would be included under AoA

• Are they green box compatible?
  – Presumably qualify as environmental payments
  – But no relation to additional costs of participating in environmental scheme
  – Conservation (resource retirement) payments can not produce “marketable agricultural output”

• Most likely should be notified as PS-AMS
Summary

• If agriculture is to be included in GHG emission mitigation programs, likely to involve subsidies to encourage certain practices:
  • Subsidies could fall under green box if tied to extra cost of conforming with environmental program
  • Cross-compliance for direct payments faces hurdle that payments should not be dependent on production
  • Biofuel subsidies (or tax credits) are likely to be amber box, as there will be an incentive above additional costs, and will in any case be related to production