

# Energy transition in extractive industries

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# Scope of paper

- Considers the working mandate to
  - Extend scope of extractive industries taxation to cover energy production
  - Limit focus to tax issues related to transition in energy production
- Shaping the paper
  - Uses International Renewable Energy Agency's (IRENA) 1.5°C pathway as a roadmap for energy transition to zero-carbon sources by 2050
  - Accordingly, paper focuses on decarbonisation of energy production - transition to renewables, hydrogen, CCS and sustainable biomass
  - Considers challenges in both developed and developing countries
- Limitation in scope
  - Interaction with carbon taxation/pricing and fossil fuel subsidies
  - Avoid wider issues of climate change
  - Avoid other market based or regulatory measures to achieve energy transition
  - Avoid discussion of local/subnational taxation while acknowledging importance

# Framing the discussion

- Narrowing down to tax issues (Section 2, paras 21-47)
  - Considers challenges in both developed and developing countries
  - The role of energy transition in broader climate goals
  - Pace of energy transitions – balancing progress across regions and countries
  - Alignment of energy transition policy instruments and the role of tax policy
- Examination of issues for developing countries (Section 2)
  - Transition impacts for resource-rich developing countries
  - Transition impacts for other developing countries
- Transition issues for current energy sector (Section 3, 48-60)
  - Wider view of energy sector beyond extractive industries
  - Energy types – intermediate transition natural gas, alternative fuels, hydrogen
- The comparative landscape (Section 4, 61-65)
  - Transition from current fossil fuel-based power generation
  - Inventory of types of measures, including both incentives and measures to disincentivise

# Direct tax measures (Section 5)

- Policy context
  - Balancing energy access and energy transition considering SDG 7
  - Need for developing countries to work within limited fiscal headroom and attract investment into the RE sector
  - Consistency with other policy measures
  
- Taxation of resource rights in renewables
  - As RE costs come down, valuation of RE endowment and taxation thereof
  - Hydropower resources – Norwegian example
  - Cross border tax issues – para 74 – Art. 6 UNMC and reference to treaty subcommittee
  
- Use of tax incentives
  - Incentive types – credits, exemptions; choice between investment incentives and income exemptions
  - Consistency with other measures
  - Consideration of other constraints and trade measures (para 78)

# Direct tax measures (Section 5)

- Encouraging internal measures and new technologies
  - Adoption of new technology – accelerated depreciation, credits
  - Need to keep level playing field and avoid picking winners and losers
  - Use of waste or flared byproduct to generate energy
  - New forms of energy such as hydrogen
  - Ownership of IP in energy transition measures
- Tax issues in repurposing of infrastructure
  - Repurposing for qualified energy transition functions such as CCUS
  - Interaction with decommissioning of infrastructure
  - Consideration of possibility of abuse, and of ringfencing tax measures
  - Possibility of relaxing rules in targeted areas for energy transition
  - Issues to consider in relaxing rules
- Ancillary matters
  - Treatment of contractors and subcontractors in energy transition
  - Decommissioning of fossil fuel plants and interaction with regulatory mandates

# Indirect tax measures (Section 6)

- VAT or GST measures
  - Typical use of VAT exemptions
  - Consideration of use of VAT as a policy lever
  - Need to preserve the VAT chain and VAT neutrality
  - Technical issues in the application of VAT in energy transition projects
  - Guidance at country level to outline VAT treatment of investments in energy transition
  
- Excises and environment related levies
  - Largely a consumption side issue, but an important factor to consider in ensuring a level playing field
  - Use of excise in energy source
  - Appropriate capture of externalities in shipping and aviation
  
- Customs duties
  - Relaxation of duties for renewables and preferential tariffs for RE
  - Need for administrative controls to prevent abuse

# Transition in the extractive industry (Section 7)

- Decarbonization of the extractive sector
  - Use of emissions reductions targets and tax measures that incentivize measures
  - Need for transparency and setting of standards for reporting
- New technology in the extractive sector
  - Use of tax measures to encourage development
  - Use of tax system to disincentivise carbon emitting technologies?
- Repurposing and decommissioning
  - Use of measures discussed in the tax section above
  - Consultative processes suggested in a country context to design an approach that fits country and investor needs

# Policy design (Section 8)

- Principles of tax policy design to promote energy transition
  - Need for fossil fuels will continue and transition should try and avoid shocks
  - Broad principles in design of policy suggested (para 123)
- Need to attract financing for the transition and tax measures
  - Significant capital needed to finance energy transition consistent with SDG 7
  - Need to consider innovative ways to attract capital, and preserve tax benefits
  - Consider measures to de-risk energy transition investments and preserving such tax benefits for investors
  - Transferable tax credits and deferral models discussed
- Design of tax incentives
  - Types of measures and design principles
  - Technology incentives and application of R&D measures
- Interaction with windfall taxes



# Ancillary matters and tax administration (Secs 9 & 10)

- Associated issues covered
  - Mining of critical minerals
  - Introduction of Carbon Border Adjustments by major trading partners
  - Deep sea mining
  - Environmental, Social, and Governance standards (ESG) and taxation
  - Energy transition, taxation and impact on human rights
  
- Tax administration
  - Need to consider administrative aspects of rules
  - Key challenges and risks of abuse of provisions
  - Organization and staffing for administering tax rules for energy transition
  - Monitoring frameworks for energy transition rules
  
- Appendices
  - Inventory of measures identified during research
  - List of climate commitments made through NDCs
  - Further reference materials
  - Alternative measures