GREEN economy Mauritius

Fiscal Policy Reforms

Background

While strong economic growth has propelled Mauritius to middle-income status, the country faces significant challenges, particularly in its energy and transport sectors. Fossil fuels make up 85 per cent of the country's primary energy requirements and have led to steadily rising carbon dioxide (CO_2) emissions per capita between 1995 and 2013. This high reliance on fossil fuels has also had other adverse impacts, for example worsening local air pollution, increasing traffic congestion, accidents, and road damage. There is an urgent need to reduce energy consumption and to increase electricity generation from renewable sources. Moreover, a shift to low-carbon transportation, improved solid waste management policies, and water sector tariff reforms are other green economy priorities.

Key Green Fiscal Policy Measures

- Fuel and motor vehicle taxes make up the majority of environmental tax revenues in Mauritius, accounting for 37 per cent and 30 per cent of the total respectively. Specific fiscal instruments include excise duties on gasoline and diesel and a tax on fossil fuels – the Maurice Ile Durable (MID) levy – introduced in 2008 and currently set at MUR 0.3 per litre (USD 0.008 per litre). Although the MID levy imposes a burden on CO_2 emissions, it is not related to the carbon content of fuels or to international valuations of the cost of carbon emissions. The MID levy is used to fund the Maurice Ile Durable Fund, which finances renewable energy projects. However, the revenues generated by the MID levy to date are insufficient to reach the government's objectives for renewable energies.
- The government has introduced a number of fiscal incentives for green investment in the energy sector, including a 15 year feed-in tariff introduced in 2011 for wind, hydro, and solar photovoltaic projects. The tariff is currently set between MUR 15 (USD 0.41) and MUR 25 (USD 0.69) per kWh, depending on installation size. A financing scheme for solar water heaters introduced in 2008 with a budget of MUR 600 million over three years (USD 16.61 million), has successfully equipped 20 per cent of households with solar water heaters. A VAT exemption on photovoltaic panels and a Power Service Subsidy aimed at financing renewable energy provision were introduced in 2014 and amounted to MUR 110 million (USD 3 million).
- There are a number of smaller environment related taxes and fees, including a road tax (15 per cent), a registration fee for imported vehicles (11 per cent), a fee on polyethylene terephthalate bottles and plastic products (3 per cent), an environmental protection fee applied on certain products and services (2 per cent), and other minor charges. Mauritius also has a CO_2-based feebate system which was introduced in 2011.

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Options for Expanding Fiscal Space for Green Investments

There is a need to better target existing fiscal instruments in order to reflect environmental impacts, induce a change in behaviour, and create additional fiscal space for green investments. Policy options in the medium- to long- term include the following:

- ***Turning the MID levy into a carbon tax*** by formulating it in direct relation to the carbon emissions of petroleum products. The carbon tax could be introduced gradually between 2016 and 2025 in three phases. In the first phase (2016-2018), the MID levy could be raised to MUR 0.60 per kg (USD 0.016 per kg), in the second phase (2019-2024), a fuel-specific carbon tax at a rate equal to 50 per cent of the level that would fully internalize externalities could be introduced, and in the third phase (2025 onwards), a fully corrective carbon tax could come into effect. This reform is expected to increase electricity prices by 2.09 per cent in the first phase, by 9.66 per cent in the second phase, and by 25.69 per cent in the third phase, while electricity consumption is expected to decrease by 0.3 per cent, 1.18 per cent, and 3.14 per cent respectively in the three phases. This reform would increase revenues from about MUR 97 million (USD 2.68 million) per year from 2016 to 2018, to MUR 361 million (USD 9.99 million) per year from 2019 to 2024, and to MUR 943 million (USD 26 million) per year from 2025 onwards.
- ***Reform the current system of transport fuel taxes into a fuel specific, environmentally efficient excise duty.*** The net effect of the reform (including the carbon tax and re-modulated excise duties) on final transport fuel prices would be a reduction of 3.9 per cent for gasoline and an increase of 8.1 per cent for diesel, resulting in a reduction in revenues of 7.3 per cent from gasoline and an increase in revenues of 21.8 per cent from diesel. The additional revenue would be about MUR 282 million (USD 7.8 million) per year, which represents a non-trivial increase in fiscal space. This reform is substantially neutral from the distributive point of view as it leaves the progressive pattern of expenditures for fuels unchanged.
- ***Use additional tax revenues for green investments.*** In the short term (2016-2018), the additional revenues that could be collected from the carbon tax would be MUR 96 million (USD 2.66 million) from electricity production and MUR 281.06 million (USD 7.78 million) from transportation fuels. These resources could be directed towards a renewed feed-in tariff scheme. With a feed-in tariff of MUR 13 (USD 0.36) per kWh, the scheme would induce 0.99 MW per year of new installed capacity in 2016-2018, 1.69 MW in 2019-2024, and 3.23 MW from 2025 onwards. The share of total installed capacity from renewable sources would increase to 4.89 per cent in 2030.
- ***Other fiscal options.*** In addition to the options proposed above, further incentives for clean energy could be considered, such as a partial tax deduction of investment costs in renewable technologies. Other options include adopting unit-based pricing for solid waste management based on the "pay as you throw" principle and raising domestic water tariffs to reflect the full cost of water use. Water tariffs could be based on household income and could result in a decrease in water consumption by 18.58 per cent, an increase in revenue of 12.38 per cent, and an increase in recovery of operation costs from 65 per cent to 74 per cent.

Way Forward

To be successful, the proposed fiscal policy reforms should be undertaken in a phased approach over a ten year period beginning in 2016. It is also important to periodically assess the effectiveness of the fiscal reforms and to make adjustments as needed. Finally, the proposed reforms need to be considered in a comprehensive policy context, taking into account other complementary policies and measures as well as wider economic, social, and environmental needs.