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To whom it may concern:

COMMENTS ON THE DRAFT CARBON TAX BILL FROM DECEMBER 2017

The comments below are from members of the Energy Governance South Africa (EGSA) network.

EGSA is a network of over 60 organisations and individuals promoting good governance in the energy sector¹.

General comments around a carbon tax

1. The carbon tax is intended as a tax on negative externalities in order to make the consumers and/ or producers pay the full social and environmental cost of goods in South Africa. Subsequently, we should see a reduction in consumption of goods and services with higher greenhouse gas emissions (GHG) and result in a more socially efficient outcome.
2. According to the documents on the carbon tax, the proposed carbon tax modelling results suggest that the carbon tax will lead to an estimated decrease in emissions of 13 to 14.5 per cent by 2025 and 26 to 33 per cent by 2035 compared with business-as-usual. While this is admirable, we believe that this is insufficient and is inconsistent with the global mitigation objective that we have signed on to, under the Paris Agreement and in order to avoid catastrophic climate change. Moreover, these estimates are based on a number of assumptions that are no longer true of the current bill, so it is doubtful that such large gains will be made.

¹ egi-sa.org.za

3. We agree that as the media statement notes, our efforts to reduce our GHG emissions and meet our commitments cannot be further delayed. For this reason we encourage the South African Government to implement this tax with immediate effect.
4. It is not clear whether the carbon tax related parts of SARS, the DEA and the DOE are sufficiently resourced to cope with the implementation and administration of the carbon tax and offsetting. The Carbon Tax Bill claims to be pro-poor, however no evidence offered by the National Treasury. The Socioeconomic Impact Assessment provided by the National Treasury offers some generalisations. However, how was the impact on the poorer sections of South Africa modelled and what were the results? In addition, no mention is made of the risk of a “utility death spiral” which may occur if there is not a concerted effort on government’s part to take advantage of the opportunity presented by renewable energy. The effects of such a process would be disparately borne by the poor, and therefore revenue recycling to address this is critical.
5. Who ultimately bears the burden of the tax? If a company has this tax imposed upon them, their choices are limited to: increasing their prices, decreasing their workforce (job losses), change their technology or reduce profits made. The imposition of carbon tax should ultimately deter carbon heavy practices or encourage a change in technology. If paying the tax is cheaper and easier than installing new technologies and practices, the desired outcome will not be achieved. Organised labour has previously expressed their concern that they are highly likely to bear the burden of this tax.
6. This then begs the question of clarity regarding revenue recycling. The current commitment to a vague increase in free basic energy allocation is admirable, but insufficient. Alton et al.²(2014) have indicated that increasing the social transfers is a good means of addressing the regressive impacts of the tax. Similarly, van Heerden et al. (2006)³ have demonstrated that the best “triple dividend” of reducing emissions and poverty whilst achieving growth are to be obtained from reducing food prices. Finally, van Heerden et al. (2016) have demonstrated that recycling revenue through investment in renewable energy will reduce impacts on the electricity intensive sectors as well as realising the maximum reductions in emissions. Whilst we understand that ringfencing is poor fiscal practice, a firm commitment to implement some or all of these strategies independently of the tax is critical to enable revenue neutrality and efficacy of the tax measures.
7. We believe the proposed headline carbon tax of R120 per ton of CO₂e for emissions above the tax-free thresholds is too low to change market behaviour - given the various tax-free allowances which would result in an initial effective carbon tax rate range as low as R6 to R48 per ton CO₂e. The headline carbon tax rate should be at least R230⁴, a firm commitment to increase to at least \$40 by 2025, and a limitation on the basic tax-free allowance should be imposed.

² Alton, T., Arndt, C., Davies, R., Hartley, F., Makrelov, K., Thurlow, J. & Ubogu, D. 2014. Introducing carbon taxes in South Africa. *Applied Energy*. 116:344–354. DOI: [10.1016/j.apenergy.2013.11.034](https://doi.org/10.1016/j.apenergy.2013.11.034).

³ van Heerden, J., Gerlagh, R., Blignaut, J., Horridge, M., Hess, S., Mabugu, R. & Mabugu, M. 2006. Searching for Triple Dividends in South Africa: Fighting CO₂ pollution and poverty while promoting growth. *The Energy Journal*. 27(2):113–141.

⁴ Literature estimates for maximum carbon tax efficacy imply a minimum tax price of R230 in 2019 according to the LTMS, rising to US\$40 by 2025. This is borne out by research from National Treasury, the University of Copenhagen, and the World Institute for Development Economics Research, who demonstrated that a price of US\$30 could achieve much of South Africa's mitigation ambition (Alton et al., 2014).

Comments on the Draft Carbon Tax Bill from December 2017⁵

General comments

1. The Carbon Tax Bill must align with the proposed Carbon Budget legislation, however the Carbon Budget is still a work in progress, so there is the risk that there will be inconsistencies between the two. This could lead to challenges from the affected parties, for instance double taxation claims, and cause further delays in implementation.
2. Section 19 states that the Minister must make regulations for many things (e.g. GHG emissions intensity, trade exposure, carbon offsets, etc.). These regulations need to be in place before the Carbon Tax can be implemented, and without these regulations, it is difficult to comment in detail on the Bill. What is the timeline and who is responsible for getting the regulations developed, consulted on, approved and implemented?
3. Section 19 and offsetting (Section 13). The Carbon Tax Bill, according to the supporting documents, was to have encompassed the offsetting details, and yet these details are missing. For instance, what are the criteria for approving carbon credit standards, how will the carbon credit verification, validation, registering, issuing, sale, retirement be handled, which carbon registries may be used. The carbon offsetting policies and rules need to be incorporated in the Carbon Tax Bill and not left to ministerial determination. We wish to put forward that South African Standards become acceptable under highly stringent and efficient criteria.

Suggested wording changes for clarity

1. Page 7. "greenhouse gas" means gaseous constituents of the atmosphere, both natural and anthropogenic, that **absorb and re-emit infrared radiation**, and...' the bold part should be changed to "absorb general radiation and re-emit infrared radiation"
2. Page 8. ' "person" **includes a partnership and a trust;**' the bold part should be changed to "means natural persons and all legal entities, including partnerships and trusts"
3. Page 9, 4.1 where is the reporting methodology referred to described and defined?
4. Page 10. "tonne" should be "tonnes".
5. Page 10 bottom. $X = \{(C \times 1) + (M \times 23) + (N \times 296)\} \times D$. It is not clear why X is shown here and where X is used. What is the X and where is it used? If X is actually B, then this should be stated.
6. Page 11 (bb). This appears to be incomplete: "C" represents the carbon dioxide of a fuel type ...'. Should it be: "C" represents the carbon dioxide **emissions resulting from combustion** of a fuel type ..."? This comment holds for (cc) and (dd) for the respective emissions of methane and nitrous oxide.
7. Page 12 (iii). Similar to point 5 above. The use of X instead of just saying Q is confusing.
8. Page 12/13 (c). The formula $P = (G \times H)$ should reflect the fact that G and H are being summed over all the components of the process, e.g. $P = \text{SUM}(G_q \times H_q)$, summed over all q (q being the number of different materials). This point has been raised previously and was neither addressed nor responded to in the Response Document (Annexure 3)

⁵ Using the document available here:

<http://www.treasury.gov.za/public%20comments/CarbonTaxBill2017/Draft%20Carbon%20Tax%20Bill%20December%202017.pdf>

9. Page 21, section 13. Rather than stating “utilising carbon offsets as prescribed by the Minister”, the processes and rules for carbon offsetting should be defined in the Carbon Tax Bill as offsetting is an intrinsic part of the intentions of the Bill.
10. Page 21, section 13. The use of “must” in this phrase is also problematic: “13. (1) Subject to subsection (2), a taxpayer **must** reduce the amount in respect of the carbon tax for which the taxpayer is liable in respect of a tax period by utilising carbon offsets as prescribed by the Minister.” It implies that offsetting is obligatory up to the limit, rather than optional. This must be corrected. A possible rephrasing is “...a taxpayer **may** reduce the amount in respect of the carbon tax for which the taxpayer is liable in respect of a tax period by utilising an **equivalent amount of carbon offsets as prescribed by the Minister.**”
11. Page 24, section 19. Regulations. These regulations are necessary for the interpretation and implementation of the Bill and need to go through the process of public consultation. This is especially true for the carbon credit eligibility criteria and management of the offsetting process. Whilst this should not hold back the promulgation of the law, a strict timeline for consultation and response must be established to ensure that the regulations are in place by the start date of 1 January 2019 as mooted in the Budget Speech of 2018.
12. Document consistently uses “terra joule” instead of “terajoule” as a unit of energy. This needs to be corrected throughout.

Comment on Annexure 1⁶

1. The carbon tax recycling proposals are still too vague to be credible. For instance, the statement “Efforts will also be made to prioritise and enhance allocations for free basic electricity (or alternative energy) and funding for public transport and initiatives to move some freight from road to rail.”, fails to provide any certainty with regards to the revenue neutrality of the carbon tax and the pro-poor impact that is claimed.
2. What is the emissions database, what is in it, how can it be accessed and by whom, who updates it and how often? (Top of page 5).
3. Page 24. Tax payable in respect of electricity generation. The calculation of the Renewable Energy Premium is not explained. This should be part of the public consultation process as the REP will directly affect the tax to be paid.
4. Page 24/25. Similar to point 3 above, the Environment levy (ELR), should be defined and subject to public comment.
5. Page 24/25. The initial tax rate and the generous allowances are too low to have the desired effect on emission reductions. There have been several studies showing that the effective carbon tax rate needs to be much higher than the proposed effective rate of R6 to R48/tCO₂ (e.g. The Long Term Mitigation Study, on which South Africa based its Peak, Plateau, Decline commitment, used R100/t in 2003 Rands, which is equivalent to R231/t in 2019). Moreover, the delay in implementation means that projected gains will not be achieved in the same timelines, implying the necessity for either increasing the rate at which the price is incremented, or incrementing to a higher final price.
6. Page 26, Section 7. “energy combustion emissions.” should be “fuel combustion emissions”, because one can’t combust energy.
7. Page 25, Allowance in respect of fugitive emissions: Section 9. It is not true in all cases that it is difficult to reduce fugitive emissions in the short term as argued, for instance fixing leaking

⁶ using the document available here:

<http://www.treasury.gov.za/public%20comments/CarbonTaxBill2017/Annexure%201%20Explanatory%20Memorandum%20Draft%20Carbon%20Tax%20Bill%20December%202017.pdf>

gas pipes can be easily done. Rather have thresholds for allowed fugitive emission rates per process/activity.

8. Page 28. Offset allowance: Section 13. The Carbon Offset Regulation consultation and approval needs to be done before the Carbon Tax Bill is implemented so that the affected parties can be prepared. Please provide timelines for the stakeholder consultations and promulgation of the carbon offset regulations.
9. Document consistently refers to “terra joule” instead of “terajoule (TJ)” which is a measure of energy.

Comment on Annexure 2⁷

1. Page 2. “assessment of the ultimately policy/legislative/ regulations/ other proposal.” should be something like this: “assessment of the impact of policy/legislative/ regulations/other proposals”
2. Page 3. “Because of the tax-free thresholds” rather say “Because of the tax-free thresholds and carbon tax recycling measures”.
3. Page 4. The implementation date for the carbon tax was set in the 2018 budget for 1 Jan 2019, so the wording in the Bill should reflect this.
4. Page 4. “in-migration” should be “immigration”.
5. Page 6.. “conditioned to” should be “conditional on”.
6. Page 6. “the nations mentioned above committed to ...” should be “the nations mentioned above, apart from the United States, committed to ...”
7. Page 7. Additional nuclear generation is “off the table” according to the SA 2018 Budget, so references to nuclear should be removed.
8. Page 9. There is a contradiction in the argument about energy efficiency: “ These price increases, especially for instance in the electricity sector, ” however, it was stated on page 7 that “the introduction of the tax will have no impact on the price of electricity.”
9. Page 10. “also requires that ” should be “it is also required that”.
10. Page 11. The establishment of the Independent System and Market Operator (ISMO) has been delayed since it was approved by Cabinet in 2011 - nothing has happened since then. The DOE must be forced to get the ISMO process going again.
11. Page 13. Typo occurs twice: “The carbon tac will aim to incentivise behaviour change” should be “The carbon tax will aim to incentivise behaviour change”.
12. Page 13. At present, electricity consumers are not able to choose different electricity suppliers. Consumers should also be given the choice the electricity source, so that they can buy renewable energy from IPPs via the grid - as is done in several other countries, through allowing wheeling and implementing appropriate billing systems. This would greatly accelerate the move to low-carbon electricity.
13. Page 27. “National Treasury agreed to review the eligibility criteria for carbon offsets in consultation with the Department of Energy, IPP office and the Department of Environmental Affairs (DEA).” This review and the setting of the eligibility criteria need to be done urgently in view of the proposed 2019 implementation of the carbon tax. Otherwise small, local projects will not be able to benefit from being offset producers because of the high transaction costs of the international standards (CDM, VCS and Gold Standard).

⁷ Using the document available

here:<http://www.treasury.gov.za/public%20comments/CarbonTaxBill2017/Annexure%202%20Socioeconomic%20Impact%20Assessment%20-%20Carbon%20Tax%20Bill%202017.pdf>

14. Page 34. "administration of the carbon offsets scheme by the Designated National Authority within the Department of Energy. " The Designated National Authority needs to be sufficiently resourced to carry out this work.
15. Page 35. "the implementation of the offset mechanism will require additional funding and this will be supported initially through the World Bank Partnership for Market Readiness project. " Need more detail on the offset processes and resourcing and timing, otherwise the local offsetting stakeholders will be adversely affected.

Comment on Annexure 3⁸

1. Offsets are defined in the Draft Regulations on the Carbon Offset which has been published for public comment. However elsewhere it is stated that the Carbon Tax Bill incorporates the offset rules.
2. Page 6, 2.2.1. Comment: the proposal that benchmarking be used "*the company's performance against the benchmark will determine the quantum of the carbon tax that could potentially be allowed as a pass through*" provides a double reward for those companies with process emissions well below the benchmark (reduced tax burden per litre, and increased margin because of pass-through). At the same time, it will mean that their fuel price is higher than that of the competitors (adding a pass through on top of the standard price), providing a negative sales response. It seems unnecessary and possibly perverse to provide selective pass through on this basis.
3. Page 12. "The Draft Regulation on the Carbon Offset has been revised to allow for certain types of renewable energy projects including some projects under REIPPPP, and small and medium scale renewable energy projects." Where are these revised regulations? The inclusion of REIPPPP projects is problematic, because it largely violates the concept of additionality which is key for offsets: since these projects were contracted at a specific bid price (at which they were financially viable) the provision of offsets is therefore a financial windfall, not a necessary financing for operations. As such, they would likely fail to meet basic additionality criteria for carbon offsets.
4. Page 12. "The carbon offset scheme will rely primarily on existing international carbon offset standards namely, the Clean Development Mechanism (CDM), Verified Carbon Standard (VCS) and the Gold Standard (GS) and their associated institutional and market infrastructure. However, scope is also provided for the use of local standards/ methodologies where appropriate and independently verifiable." The use of local standards/methodologies is not expended on in the Bill. What then is being referred to here?
5. Page 17, 2.10.2. Comment: We agree that an ETS is not an optimal solution for South Africa. We would also caution against linking with carbon pricing mechanisms in other jurisdictions. This would likely have the effect of undermining the local market, as historical evidence points to such market linkages increasing price volatility.
6. Page 17, 2.10.3. Comment: The SA energy policy is not driven by market forces, so the carbon tax won't force change. Treasury response: "*This line of argument does not take into account the polluter pays principle that is, the need for all polluters to be held accountable for the damaged cause as a result of the negative externalities they are responsible for.*"

⁸ Using the document available here:

<http://www.treasury.gov.za/public%20comments/CarbonTaxBill2017/Annexure%203%20Response%20Document%20to%202015%20Draft%20Carbon%20Tax%20Bill.pdf>

This is a problem at present because of the lack of transparency in the IRP process and the associated modelling. It is apparent that the current modelling has constrained renewable energy generation (See the recent CSIR studies on the current IRP). In addition, the National climate Change Response White Paper articulates the polluter pays principle as “those responsible for harming the environment paying the costs of remedying pollution and environmental degradation and supporting any consequent adaptive response that may be required.” Since the proposed tax rate is well below most estimates of the social cost of carbon (typically between US\$40 and US\$200 per tonne of CO₂e), it is clear that this implementation of the principle falls short of the required level of stringency.

This submission is from the following members of EGSA:

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