

WWF LAUNCH OF CARBON TAX PAPER: REPORT

please note that this is a report and not the official views of WWF on the event.

FEBRUARY 2012.

Summary of Ismail Momoniat address and the question and answer session

Ismail Momoniat opened his address welcoming the paper by WWF, but with a tinge of regret that the paper by Treasury on carbon tax is still a work in progress. However, in spite thereof that the paper has not been released, Treasury made a decision to highlight in the budget that they intend to implement carbon tax in the future - at this stage projected for 2013/2014 – to alleviate fears that the tax will be levied at 100% and to indicate to the industry what they can expect in the future. Treasury was worried about the possible response by the industry, and indeed the business press has referred to it.

The budget highlights specific numbers, allows for trade exposure in some of the sectors, and initial allowance for emissions, i.e. 100% in the case of agriculture initially. The strategy is to start low and then to escalate the rate. During question time, he made it quite clear that they intend to escalate the rate quite dramatically in 2019.

With reference to the presentation of the previous speakers, he agreed that carbon tax is context specific, and in SA's context our dependence on cheap coal to generated energy serves to highlight the challenges. Compounding the challenge is the fact that the industry is also a large employer of workers with low skill levels.

He was very emphatic that the idea behind carbon tax it to effect behavioural change and not to generate extra revenue, a point that he returned to time and again. Having said that, he pointed out that Treasury do not know what will happen once the tax is implemented and will have to see wait and see what the effects will be.

Ismail Momoniat was adamant that there should be more debate on the issue of carbon tax, and that once the planned paper by Treasury is released in April further debate will be encouraged. However, the word 'tax' always invites resistance. Some of the opposition argue that there are other options, while others cannot understand why South Africa should lead on the issue of carbon tax, if India and Chine, for example, is not contemplating implementation thereof. His response to such critique is that South Africa should lead, and that there are many benefits attendant to doing so. In the process the country will attend to structural changes and will become more innovative and competitive. It will only become more difficult in the future; failing to make the right decisions now will lock in future emissions. There is no panacea and easy solutions; whatever option South Africa chooses, will be by sector. Any climate mitigation strategy will be a package of institutions and instruments.

With reference to debate in Denmark, he pointed that South Africa has also started to say that there is already examples of carbon tax in the system and that Treasury will need to unpack what is the

energy tax component and what is the carbon tax component. We need energy efficiency in our system as well.

In conclusions, and once again referencing the WWF paper, be complimented the authors for their very good summary of different approaches, revenue recycling, etc. However, Treasury has a problem with earmarking funds given the historical failures in South Africa in instances where it was done. Being transparent and getting the commitment to the project is important in the long run, and that is what revenue recycling is about. Treasury wants to make sure that wherever funding is allocated to, there is efficiency. He concluded by stressing that government must be accountable to all taxes it receives and carbon tax is no exception.

Saliem Fakir pointed out that carbon tax is now an acceptable principle to tax external costs. South Africa should not work in isolation, but must be aware of what is happening elsewhere – if the large economies will be subjecting their economies to carbon tax, they will want to make sure that the countries that they import from is doing the same. We should be aware of the areas that will be most affected. By instituting it sooner rather than later, we will reduce our dependency of fossil fuels and the accompanying exposure to price volatility and create opportunities for our economy.

Questions from the floor:

The first question referenced the importance of policy coherence that was highlighted by the first set of presenters. The speaker pointed out that not only is there a large amount of duplication of work done in this regard, but that the plethora of regulations and administrative tasks risks overburdening both government and the private sector, and adds to the costs of doing business.

Further questions dealt with the choice of carbon tax above carbon trading, querying the stated objective of the tax as an carbon reduction measure instead of just another tax; what complimentary packages to carbon tax would entail; and finally, how to manage downstream interventions to address the use of coal to generate energy.

First to respond was Ismail Momoniat. Although he pointed out that the question relating to coal and energy efficiency was more for the previous speakers, he reiterated that it is necessary to differentiate between the energy efficiency component and emissions. In South Africa there are particular challenges with SA mining sector, but he pointed out that even current pricing has been tough on industry.

With reference to carbon trading, he motivated Treasury's decision to choose carbon tax over carbon trading, with reference to Australian cap and trade and South Africa's large emitters. However, he pointed out that this does not preclude cap and trade, but that Treasury prefer for carbon tax for a number of reasons, as stated before.

Retuning to ring fencing he stated that it does not mean that government is not prioritizing. By insisting on a rule, you are indicating to government that you do not trust it to do the right thing. If this is the case, and government is not to be trusted, it can do a number of other things that the public will not even be aware of. However, it is important to have a measure of certainty; if we have recycling, we need to have a longer term of commitment and be clear on how industries will be awarded. Supporters of ear marking funds have not looked at how it is spent and attendant inefficiencies. It is also undemocratic to try and pre-empt debate on how money must be spent. The

key is that government should be accountable, and it is up to authorities and the public to ensure that government is spending money correctly. He concluded by asking the question that should Treasury be able to introduce carbon tax in a revenue neutral way, the industry suggest that we cap it and by doing so end up increasing the tax burden and impacting on democracy.

In response to what the complimentary packages to carbon tax will entail, he raised a couple of possibilities, e.g. where would you provide support, do you allow for tax incentives, or do you provide other complimentary measures (e.g. Subsidies for public transport)? Very importantly, though, is education, education, but at the same time not scaring people too much because then they stop caring and do not take the measures that they need to take (e.g. Aids). No one measure will succeed, it is necessary to get pricing right and externalities, but do need additional measures.

Emily Tyler briefly responded and raised two points; firstly, she highlighted the complexity of any 'relief approaches' that have been implemented for specific industries internationally; secondly, and with reference to the first question, she emphasised the need for a response that will result in policy and institutional coherence and the need to build sensible institutions and the capacity to support that.

Brent Cloete pointed out that mitigation issues should be centralised to ensure efficiency and to build an understanding of the problem as a whole. Whether one chooses carbon tax or carbon cap and trade is all about context, but he agreed with Ismail Momoniat that carbon trading will not work well in the South African context. As far as benchmarking is concerned, the ideal would be to reduce emissions without any extra costs.

Next round of question:

Following on Brent Cloete's comments on benchmarking the question was asked how South Africa can do its benchmarking correctly, if it does not have the necessary data. An employee of Eskom highlighted the international nature of cap and trade and the opportunity to generate funding which carbon tax does not provide. Concerns were raised that the budget appears to be quite friendly to heavy emitters, and whether what is proposed, will be adequate to effect structural change. Another question queried the lack of detail in the budget to enable proper evaluation of how the tax proposals can be made more effective.

Once again Ismail Momoniat answered first, and in a playful mode he wondered why if Eskom is a state organ they are not falling into line. In response to the question on the choice between carbon tax and carbon capping, he reiterated his previous comments that Treasury is of the opinion that carbon tax is the more effective measure to change behaviour. He was also sceptical about the potential of carbon trading to generate a significant flow of income for South Africa, or as he put it 'the millions that are going to fly'. He also did not think that it is necessary to align with international practice, pointing out that if the big emitters are not going to act, it does not matter what we do. As far as Treasury is concerned, the debate is settled and the extent, to which we moderate it, will depend on the input we get on our paper.

He did not respond directly to a question on the possibility of aviation tax, pointing out that it is policy not to talk on new taxes between budgets. However Treasury is always looking at what other countries are doing and the need for alignment between countries.

Responding to the question that the current proposal is very lenient to heavy emitters, he said that Treasury decided on a balanced approach – they can be totally unfriendly to heavy emitters, but in so doing destroy jobs and the economy. They need to take into account all these considerations. Treasury tries to be friendly to everyone, but are firm about where they are going. Even amounts provided for are open for discussion. What would be the economic impact in the short term? Is it escalating too little too much? Whatever decision is made requires the wisdom of Solomon. In essence it is a judgment call and need consensus of society. In response to the question on the perceived lack of detail, he concurred, pointing out that Treasury was not ready with their paper, but wanted to put in their proposals for the reasons already stated in this address.

In response to the question on the lack of data and baseline information, Brent Cloete commented that there is information that the private sector has and which it does not want to divulge, but more interestingly, are the blockages and that which they do not know. His opinion was that a significant carbon price will quickly show you where the problems are, and where you can do what. But the fact that you do not have the information does not mean that you do not start the process.

Referring to a question about the integration of carbon cap and budget, he pointed out that the cap rate gets adjusted over time and their approach proposes that you reward emitters if they stick to cap. As far as carbon trading schemes are concerned, he highlighted the problem that most of our trading schemes are local; if we could connect to international scheme it could be more efficient. Once there are international schemes South Africa should link in, but should be mindful that we are not funding mitigation in Europe. With reference to aviation tax, he responded that if EU is forcing everyone to pay their local price, a trivial increase in the cost of airlines, is setting up a much larger debate than carbon emissions. Once you move into more global adjustments, it will become more of an issue.

Emily Tyler returned to the question about lack of data and baseline information, and pointed out that internationally they still make mistakes. In the UK they are now negotiating benchmarks that are lower than previous years. She argued that this is why one should not wait, but start early. Whether or not carbon budgeting is potentially a cap system, she opined that critical to answer the question would be to look at how carbon budgets are envisaged – guidelines or hard measure? Lastly she questioned whether the amounts contained in the budget as to the level of tax enough for structural change? At this stage unclear what the amount is that they are proposing, the budget states R120 but if there is a tax free element then it means a R43.