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6 November 2009

Ms. Phumla Nyamza
Office of the Secretary
Parliament of the Republic of South Africa
P.O. Box 15
Cape Town
8000

RE: Public Hearings on the Political, Economic, Legal, Gender and Social Impacts of Climate Change

Dear Ms. Nyamza

We are pleased to participate and submit the following written submissions for consideration at the public hearings on the above topic.

1) Absent regulatory frameworks for carbon markets
2) Gaps in carbon and fiscal incentives for the carbon markets
3) Policy formation regarding national carbon emission reductions

We would also be willing to make verbal presentation on these submissions at the public hearings on 17th, 18th November 2009 if required.

Yours sincerely

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Submission to Parliamentary Committee

Political, Economic, Legal, Gender and Social Impacts of Climate Change

1.1. Absent Regulatory Frameworks for Carbon Markets

1.1.1. Why we need a regulatory framework for carbon markets in South Africa

The *mandatory carbon market* is regulated by the Clean Development Mechanism (CDM) of the Kyoto Protocol, where South African companies can earn carbon credits (Certified Emission Reductions or CERs) for carbon emission abatement projects under the registry of the CDM. This market is well regulated. The projects require approval so that they demonstrate additionality, an independently verified baseline calculation, an emissions monitoring system is in place, emission reductions are annually verified and claimed, and social and environmental impacts are assessed. This regulatory body ensures that there are quality projects with real, verifiable emission reductions.

However, there is also a *voluntary carbon market* where companies can invest in a carbon development projects that comply with one of several international standards of compliance, like the Voluntary Carbon Standard (VCS) or The Gold Standard. This market is not regulated and varying standards and prices are applied, which leaves this market open to abuse and even fraud.

Therefore, we require a regulatory framework to be developed in South Africa so that our country can benefit from the US$ billions that will be invested in carbon development projects in the coming years. We need to structure this regulatory framework for the following reasons:

a) The voluntary market already exists and unless it is brought under some regulatory framework it is going to discredit the carbon market in South Africa.

b) The global carbon market is set to trade some US$ 105 billion in carbon credits during 2009 and estimates predict that this market will reach US$ 1 trillion by 2020. South Africa needs to participate and be involved in this new revenue stream.

c) One of the aims at the COP15 meeting at Copenhagen in December 2009 is to set a framework to enable regional emissions trading schemes to link and create a global carbon market. We need to have a respectable and regulated market in South Africa in order to participate in this global network.

d) South African businesses already require a market to buy carbon credits for offsetting their own emissions. However, due to a lack of local carbon development projects and a regulatory framework they are being forced to buy carbon credit offsets from international markets. These carbon funds could be invested in local sustainable development carbon reducing projects in South Africa if we had a developed regulatory framework.

e) There are many companies and institutions in Europe that have funds for investment in Southern African carbon development projects, however, without many projects to invest in or without any regulatory framework in place, these funds are being diverted to other jurisdictions.

f) Carbon trading systems do not emerge spontaneously. Economic markets require strong underlying institutions to monitor behaviour and enforce compliance. When there is a lack of regulatory framework the bad money (bad carbon credits) always drive the good money (good carbon credits) from circulation.

1.1.2. What form should the regulatory framework take?

What is required is a regulatory framework that will have the following main functions:

a) A regulatory body that will oversee the compliance of any carbon exchange dealings or carbon brokerage services as well as to regulate the carbon retail market in South Africa.

b) An institution at which to register bone fide carbon development projects, which will issue verified carbon emission certificates from voluntary carbon development projects to the project developers.

c) An institution that will develop carbon development project regulations for qualification in terms of additionality, baseline verification requirements, monitoring requirements, social impact evaluation etc.

d) A body that will make recommendations to Government on the accounting and tax treatment of voluntary carbon credits, as well as recommendations on policy incentives to promote sustainable development and the reduction of carbon emissions.

e) A body that can link with the International Emissions Trading Association (IETA) and enable regional/global emissions trading to ensure that South Africa maximises the carbon market flow of funds.

1.2. Gaps in Carbon & Fiscal Incentives for the Carbon Markets

1.2.1. Income tax exemption on "regulated" voluntary carbon credits

Voluntary carbon credits should be afforded the same income tax treatment as the mandatory market's Certified Emission Reductions (CERs) earned on registered CDM projects, which are income tax exempt. This income tax exemption should be applied once we have a regulatory framework for carbon markets in place.

1.2.2. Individual tax allowance on domestic renewable energy installations

To engage and reward domestic uptake of renewable energy like solar thermal geyser and solar PV installations there should be an individual tax allowance equivalent to a 33% deduction for three years. This will encourage individual citizens to engage with climate change mitigation and reduce the demand on the power utilities electricity supply.

1.2.3. Capital expenditure tax allowance on clean technology resulting in reduced carbon emissions

Clean technology investments resulting in reduced carbon emissions should be eligible for a special deduction allowance of 150% of capital expenditure or a deduction over three years as a 50:50:50 wear and tear write-off. Presently, although there are incentives for energy efficiency achievements, there is no specific incentives for reduced carbon emissions.

1.2.4. A renewable energy feed-in-tariff for co-generation

Combined heat and power generation and power generation from waste streams like heat, gas flue, steam, spent biomass etc. should be subsidised with a special feed-in-tariff to encourage investment in these cogeneration technologies. These are highly efficient technologies reaching 80% to 90% efficiencies which also reduce waste streams from industry.

1.2.5. Support for co-generation under the Department of Trade and Industry's (DTI) Critical Infrastructure Programme (CIP)

Eskom's current proposed electricity tariff increases and the Power Conservation Program ("PCP") calling for a 10% reduction of electricity consumption from companies now makes it critical for private sector investors to find alternative sources of electricity supply such as co-generation and other alternative sources of energy.

Since the need for co-generation investment by companies is a new issue the DTI has not budgeted to support these kinds of projects under the CIP, even though co-generation projects meet with the objectives and in most instances.

However, the National Treasury has set aside an amount of R 2 billion over the next three years in the National Budget of February 2008 to support programmes aimed at encouraging or promoting more efficient use of electricity, generation from renewable sources, installation of electricity-saving devices and co-generation projects. It will make a lot of sense to channel some of these funds that have already been budgeted for, through the existing CIP because there is already a unit within the DTI incentivising infrastructure project that are critical to support economic development.

1.2.6. Amendment to section 12I of the Income Tax Act to include electricity generation

Section 12I of the Income Tax Act provides for an additional 55% tax allowance on industrial policy projects, however, this allowance does not include electricity generation. We believe that this allowance should include electricity generation from sources other than coal, which will provide an incentive for cleaner electricity generation in South Africa.

1.3. Policy Debate Regarding National Carbon Emission Reductions

There is a need for serious debate on whether South Africa adopts a carbon tax or a cap and trade system as a policy to reduce national greenhouse gas emissions. There are positive and negative issues surrounding both systems, however, we need to ensure that we adopt the right system and not the easiest system. The easy way has been cited by Government representatives as the reason to adopt the carbon tax system. The rationale is that our most efficient public department, SARS, will relatively easily be able to administer the system. However, there are far more important issues to consider in this process – not least to consider the most effective and efficient way of reducing carbon emissions.

The essential difference between the two systems is that a carbon tax system "fixes the price of carbon" and leaves the quantity of emission reductions up to the market. On the other hand, a cap and trade system "fixes the quantity of carbon emission reductions" and leaves the price of carbon up to the market. These critical differences require some serious debate because in a global financial market South African businesses need to remain competitive, and in terms of a global climate change agreement South Africa wants to guarantee the quantity of our carbon emission reductions.