CPD 15 mins

CO^2 Tax: The Dirty Tax

Kerry Dimmer

It's been a year since the government announced its intention to introduce Carbon Tax, and six months since it was imposed on new car sales. Like most taxes, it's not being well received, but not for the usual reasons.

It is one of the major concerns of economists, policy-makers and environmentally aware citizens. It gravely threatens humankind and all living things, and will create a global recession unlike anything we can comprehend. Global Warming and climate change is not a fantasy - it is potentially the biggest catastrophe the earth has ever faced.

The blame lies with all of us, in particular the older and past generations, simply because we were unaware of the dire consequences of our need for power. When we burn fossil fuels like coal, oil and gas, carbon atoms are converted to carbon dioxide (CO^2), which rises into the atmosphere trapping heat radiated from the Earth's surface. Carbon emissions remain resident in the atmosphere for approximately 100 years, and it is that cloud that essentially threatens our existence.

All burnt fuels from residual oil to natural gas can be accurately measured for carbon content and the amount of CO^2 released into the environment. We know, therefore, that South Africa releases 1000 tonnes of CO^2 every 1.3 minutes making us the 13th highest emissions contributor, according to the United Nations Statistics Division.

Solving the problem is a global concern and why international Climate Change conferences are vital for the exchange of information while providing a platform for nations to pledge their commitment to finding solutions. Individually, countries are introducing measures to reduce emissions; one of those being Carbon Tax. Rationalising Carbon Tax is a no-brainer given the levels of CO^2 that are already in the atmosphere and being added to daily by the millions of vehicles on our roads and by relative industries such as fuel processing and electricity supply.

Taxing fuels according to carbon content should be pretty simple to administer - right? The easiest would be to collect tax at the point where fuels are extracted before entering commerce, with fuel suppliers and processors passing the cost of such tax on along the market stream. But it's not quite that easy, particularly in South Africa's vehicle market.

Last September South Africa introduced a Carbon Tax on all new vehicles that emit more than 178 grams of carbon dioxide per kilometre, and the industry is not happy at all. Not because of the tax, per se, but because there are a number of issues that it appears that The Treasury has not taken into account. One of those is the concern that the measurement threshold has been set too low.

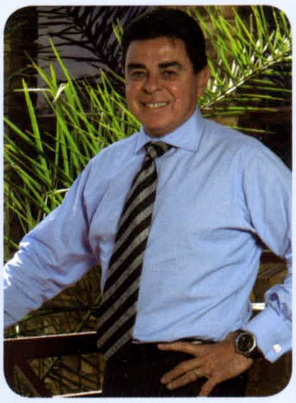
Gary Ronald of the AA explains: "There are approximately only 12 models available in South Africa that satisfy the measurement criteria, which means almost every new vehicle will attract the tax. If you are going to introduce a Green Tax, surely you should look at every vehicle in the car park rather than a select group?"

Compounding the issue is the poor quality of the fuel available in our country. Jeff Osborne of the Retail Motor Industry (RMI) Organisation points out that South Africa is essentially still supplying the Euro 2 level fuel as opposed to what is available in Europe – the cleaner-burning Euro 4 and Euro 5. "The irony of this is that vehicles manufactured here that are compliant with Euro 4 and Euro 5 specifications can't be sold in SA because of the poor quality of fuel so have to be exported to other markets. Likewise, importers cannot bring in the higher spec'd models."

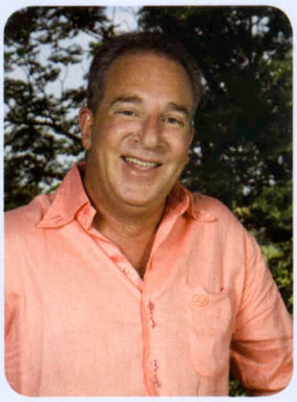
Over and above this there is no incentive for owners of older vehicle models to scrap their vehicles or install catalytic converters (think taxis), as was applied in America and Europe some years ago. "Here the buyers of new cars are being punished by having to pay a punitive tax on a new car. Surely the levels of CO^2 emissions are a lot lower by comparison to those older, smoke-belching, gas-guzzling vehicles. Why limit the tax to the activity of new car purchase?" asks Osborne.

Wynter Murdoch, editor of Automobil says, ironically, that thanks to the introduction of the measure, new car prices can expect to rise by at least two per cent which will drive consumers to the dirty-engined, second-hand market. "It is likely to be two years before Green Fuel makes its appearance in South Africa," he says. "Until then

Kyle Mandy,
Head of National Tax Technical,
PricewaterhouseCoopers



Jeff Osborne,
CEO,
Retail Motor Industry Association
(RMI)



Gary Ronald,
Head of Public Affairs, AA

we'll continue to breathe dirty air – and pay in the region of R2,4-billion in CO^2 taxes for the privilege."

The issue of Carbon Tax is, however, more than just motor vehicles. In December The Treasury made available for public comment, a cabinet-approved draft policy discussion paper on taxing carbon emissions. PricewaterhouseCoopers is giving it a lot of thought, according to Kyle Mandy, PWC's head of National Tax Technical.

"Our thinking at this time is that The Treasury has not given enough consideration to how and whether the tax should be implemented in all sectors of the economy. As a starting point, it certainly shouldn't be implemented in the electricity sector at all, given the recent large price increases. However the two largest consumers of electricity – manufacturing and mining – do need some form of taxation to encourage the effective reduction of carbon."

From a taxation perspective, Mandy expects South Africa to follow the model that has been implemented in almost every other international jurisdiction, and that is to tax the fossil fuels at source. "For example, crude will be taxed at the point of extraction which will obviously add to the cost base of the user who will bear the economic effect of the tax."

Another niggling aspect presented in the discussion paper, feels Mandy, is the Long-Term Mitigation Scenarios report that presents models based on surveys conducted in 2006/7. "As we all know, a lot has happened in the world and South Africa's, economy since then, so those models are heavily outdated. For instance, back then it was estimated that the price of oil would peak at $155 in 2030, but in 2008 we already saw oil prices fairly close to that level.

"Consider, too, the massive electricity increases that could not have been contemplated when those models were created. So the rate and the sectors to which Carbon Tax would apply are based on outdated information."

While Ronald, Osborne and Mandy are in agreement that Carbon Tax is essentially a good thing, they are frustrated that there has been no indication by government of where the tax is to be used. "Government does, very loosely, allude to tax shifting," says Mandy, "so, taxing the 'bads', like carbon emissions versus reducing the tax on those things that have good implications.

"There is too, the allusion to revenue recycling, essentially where tax revenues are passed back into the economy through various means like subsidies or tax incentives to advance the environmental objectives, but the government has indicated that this will be done through the general budget. Consider, though, that the government's record in this regard is not really good if you remember what was promised with regard to the electricity tax incentives. The bottom line is nothing has happened and the government currently collects some R5-billion annually from electricity, none of it recycled into the economy."

So, no sweetener for the consumer, which translates, as always, in the poor being further burdened. Simon Gear, environmentalist and air quality consultant puts it succinctly: "Change only happens when it is economically driven. All the energy efficiency and alternative changes that are being encouraged now will be forced onto the consumer eventually by, for instance, rising fuel prices."

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There is general consensus that Carbon Tax should not be a stand-alone measure, it should ideally be one component of a package of measures that, together, serve to meet broader environmental objectives, such as enhancing and introducing regulations, education programmes and incentive packages.

The government would do well to ring-fence the revenue raised through the levy into the development and subsidy of low-carbon technologies - something that industry cannot independently cope with financially.

Carbon Tax won't stop climate change on its own, but "it will provide a signal to producers and consumers to change their behaviour over the medium to long term," says The Treasury's discussion paper. And if that doesn't sway you, then a visit to www.breathingearth.net may just prove more convincing. It will show that in the time it has taken you to read this article, South Africans have emitted some 7 000 tonnes of CO^2. Your individual contribution is, therefore, in the region of 8.44 tonnes per year and, dirty tax or not, you're going to pay for that!