



Small Carrot, Smaller Stick: The South African Carbon Emissions Tax

The South African Carbon Tax Act (Act No. 15 of 2019) was signed into law by the President in May 2019 and came into effect from the 1st of June 2019. The carbon tax is part of Government's package of policy measures to mitigate climate change as outlined in the National Climate Change Response Policy, this "stick approach" enforces a taxation for every tonne of carbon dioxide emitted by corporate entities, in the hope that it will motivate them to curb their emissions allowing for government to meet their national GHG budget commitments. The South African carbon tax does not have an associated regulatory market, so carbon offset regulations were developed in such a way that they leverage off of the certification apparatus of voluntary carbon markets.

South Africa has therefore set the scene for a traditional carrot and stick relationship between carbon offsets and carbon tax, converting carbon emissions into a resource which could potentially be traded as any other commodity. Local carbon price discovery will therefore always be linked to the carbon tax rate, making an essential driver of this nascent market. So just how effective is the South African Carbon Tax Act as a market catalyst for the financialization of carbon emissions towards the greater goal of reducing greenhouse gas emissions (GHG)?

Learning from the rest of the world:

The international experience from the implementation of carbon "taxes and trading" have seen varying degrees of success with the European Union providing the most successful and advanced solution to date, through their robust policy which is supported by a well calculated and continually developed emissions trading scheme. The Emissions Trading System (EU ETS) was first launched in 2005 and has since been through numerous reforms and iterative processes throughout its various planned phases. The scheme commenced with lenient targets that are increasingly tightening, which should serve as a warning to complacency around the current South African Tax Act, in terms of the policy direction.

The EU ETS mechanisms commence with the establishment of national emissions caps by each EU member state - from this, cap allowances are set for major industrial operators. The emissions of these operators are stringently monitored through approved methodologies which are governed by strict regulations. Within this framework, participants are allowed to re-assign or trade their allowances and to generate a limited number of offset projects, including projects outside of the EU. Most importantly the system is given teeth and impetus by the imposition of significant penalties for excess emissions (up to 100 euros / tCO₂e).

The South African Carbon Tax is an altogether different instrument in that it automatically sets a reference price for carbon emissions, however if conceptualized correctly it could result in similar levels of success as the EU ETS.

The first conceptual issue to resolve is the establishment of a suitable tax rate, one that encourages meaningful behavioural change and indicates government's political will to address climate change. The South African carbon tax rate is currently at R144 / tCO₂e (an increase of 12 % from the 2021 rate), however once the various and sizeable industry specific emissions allowances are included the effective tax could be as low as R14 / tCO₂e. The global range is between R15 and R2 100 / tCO₂e, the global median is R192/ tCO₂e and the global average is R351 / tCO₂e.

Therefore, the current South African tax rate is not sufficient enough to deter carbon emissions nor allow for the development of a robust local carbon offset market.

The second issue is the conundrum between such a tax and any corresponding carbon offset market that is established around it, considering that such markets eventually reduce the revenue potential of the government setting the tax.

The third issue is around the oligopolistic and even monopolistic nature of key sectors in South Africa which make it unsuitable for a carbon trading system.

The stark reality is that a carbon tax and emissions trading system requires an appropriately sized stick and carrot, in this case a bigger stick and bigger carrot in order to achieve the desired outcomes of absolute emissions reduction. Offsetting and carbon markets should however only be viewed as a transition tool towards a decarbonized economy and whether we implement a carbon price or not there will always be a price for emitting carbon.

**Descriptive statistics for global carbon taxes taken from 2018*

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