

A BROAD OVERVIEW ON DOMESTIC OFFSETS POTENTIAL IN SA

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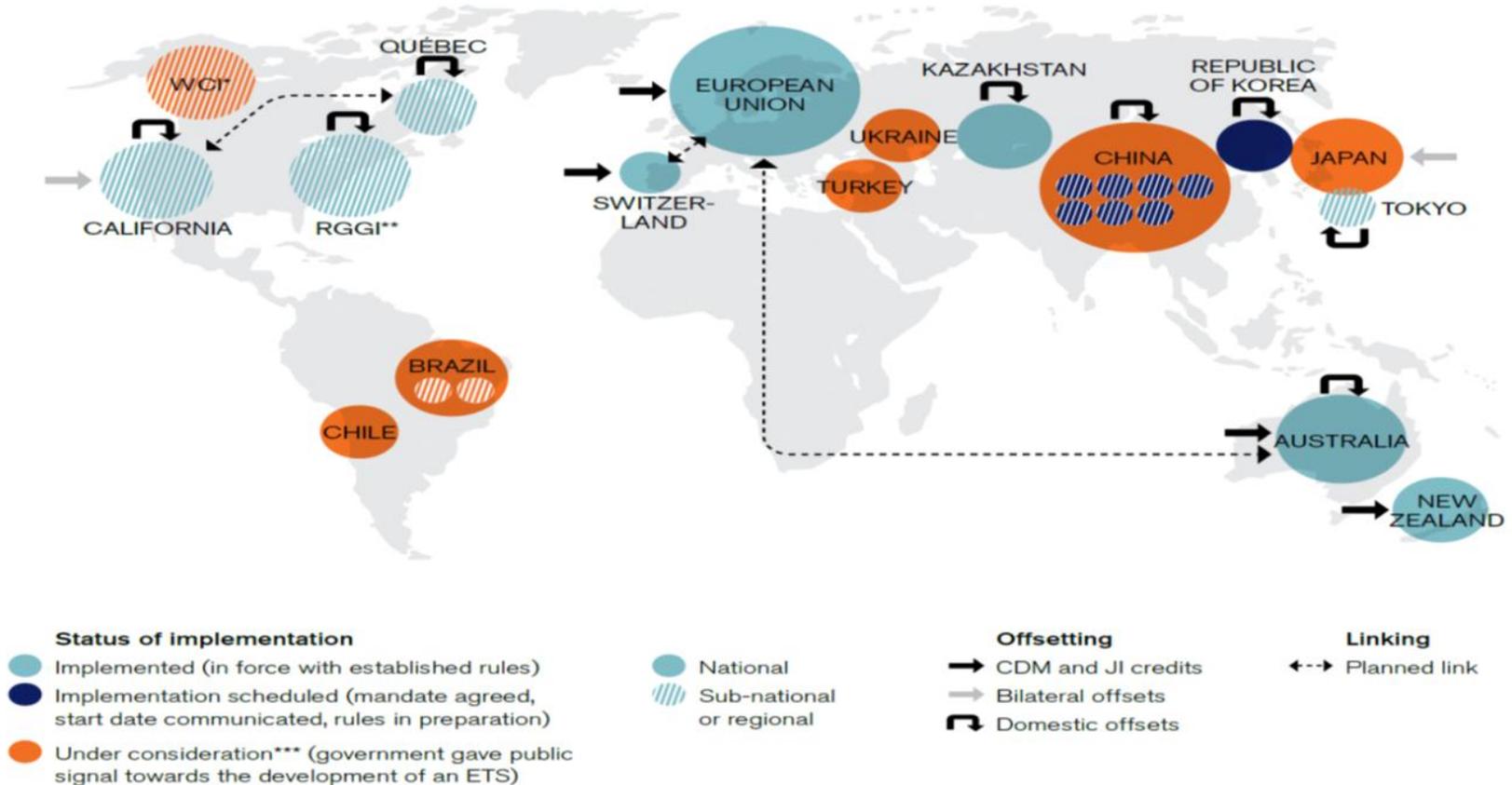
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Declaration

- South Africa seeks to establish the Carbon Tax policy, with carbon offsets to be used to offset tax liability of key economic sectors/ industries.
- Key message – South Africa is still at an exploratory stage on this matter and is weighing various aspects related to offsets.
 - Key lessons will be drawn from international experiences whilst domestic and regional circumstances will be taken into account.
 - The approach therefore in this presentation is to assess the international landscape as well as consideration of unique domestic circumstances.

The international context

Figure 1: Map of existing, emerging, and potential emissions trading schemes

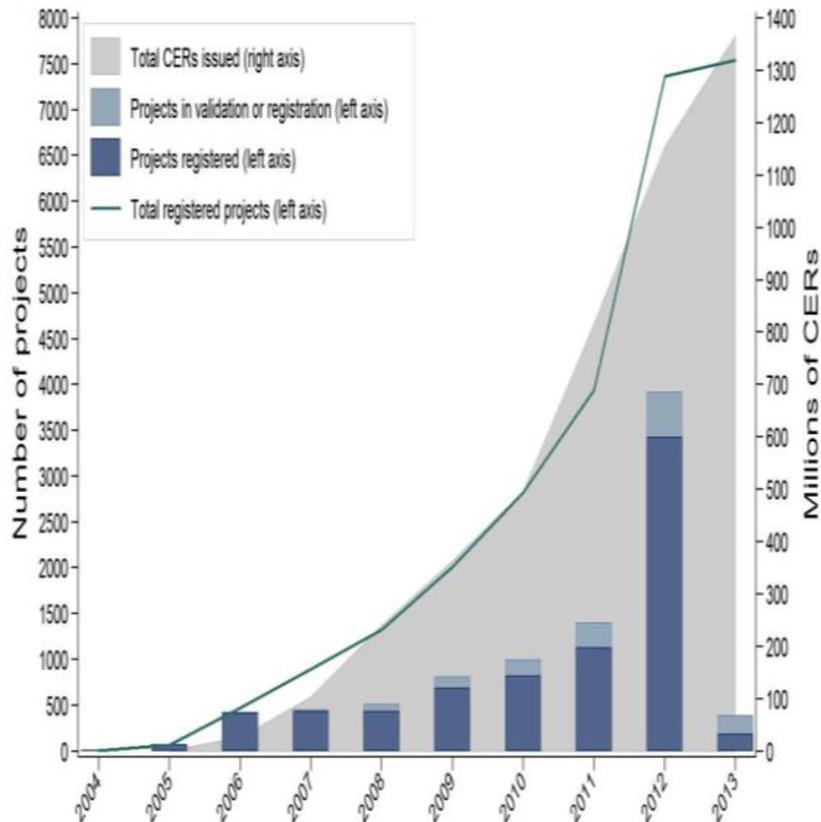


* WCI – Western Climate Initiative. Participating jurisdictions are British Columbia, California, Manitoba, Ontario and Québec
 ** RGGI – Regional Greenhouse Gas Initiative
 *** Schemes under consideration are at different stages in the process. See Section 3 for more details.

Note 1: The size of the circles is not representative of the size of the schemes.
 Note 2: Mexico's Congress passed a General Law on Climate Change, which provides the federal government with the authority to create programs, policies, and actions to mitigate emissions, including an ETS.
 Note 3: Costa Rica is working on the design of a domestic carbon market that would contribute to meeting the country's carbon neutrality goal

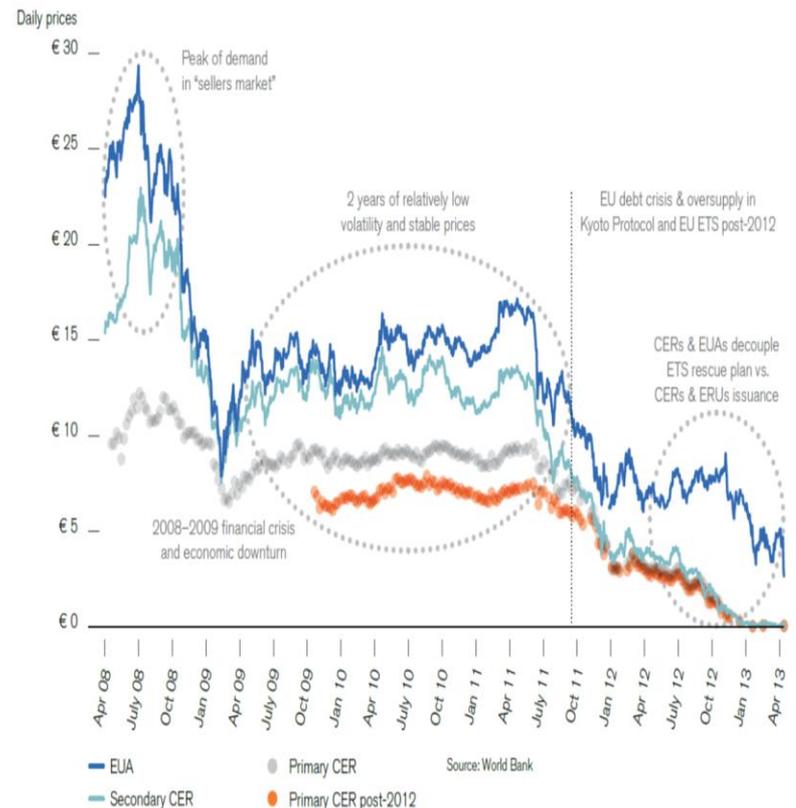
Too much CERs in the market only undermine the price

Offsets within the EU-ETS market – CDM EB report 2013



Price signal

Figure 4: EUA and CER prices (2008–2013)



Some lessons from the EU-ETS

- Do not overwork the principle of “grandfathering”.
- Back-loading only serves to delay the pain – encourages timing the market
- Target sectors where there are greatest sources of emissions but in a developing country balance this with sustainable development requirements.
- Know what sectors and gasses to target – your GHG profile and energy mix are an important factor.
- Tie your vision/ target to the international obligation and strive towards it
- Should the point of checking emissions be at industry installation point or point of entry/ energy source.
- Consider price floors and reserve margins to cushion free fall.
- Set the reserve margin – which is partly a shock absorber and discourages market dumping and reckless speculation.
- An upfront commitment on abatement costs commitments by the industries/ companies/ sectors as a motivation for free allocation should be introduced upfront.

Position on Markets within UNFCCC

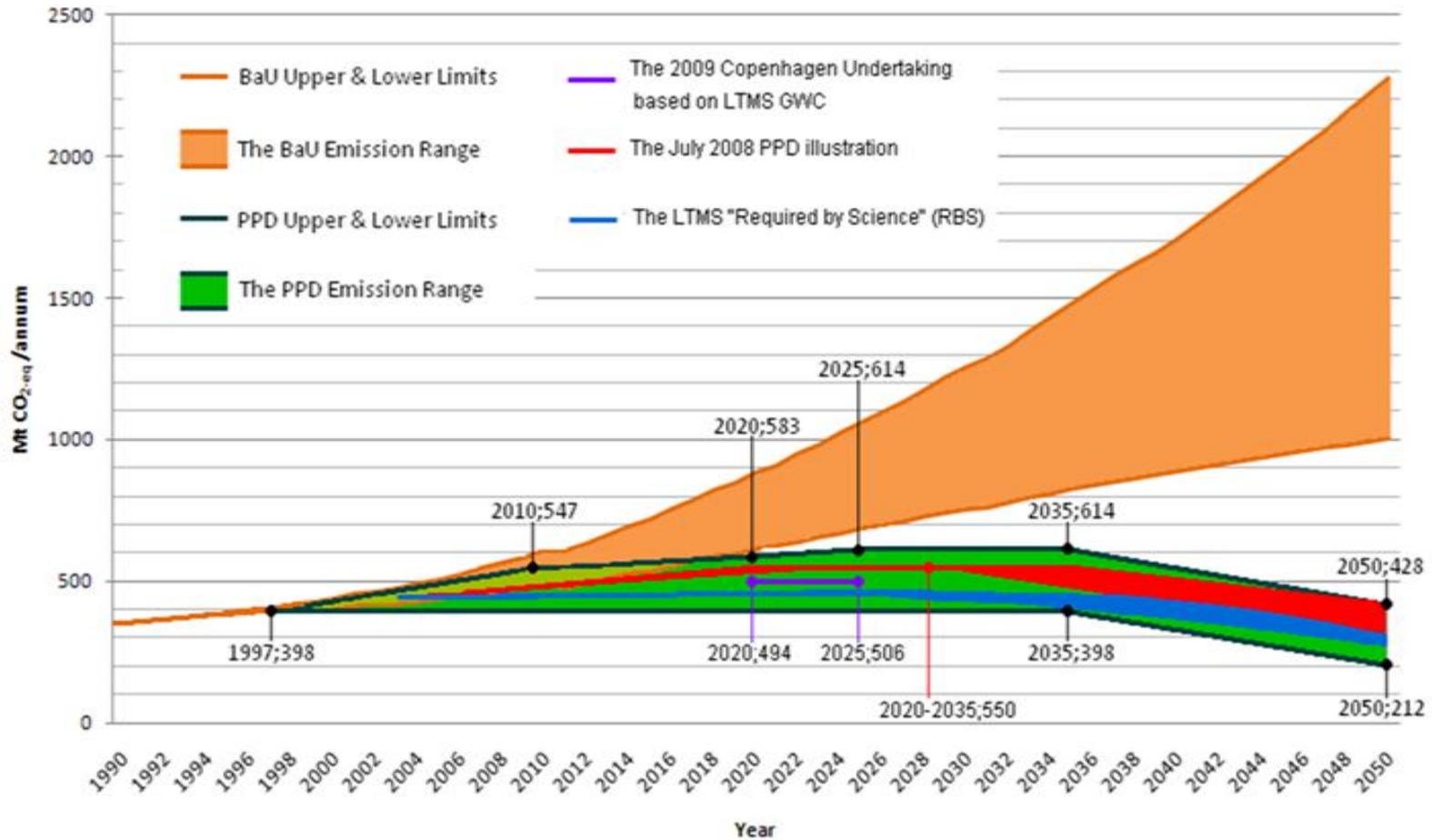
- The NMM design must encompass the following elements:
 - Result in real emissions reductions
 - Be *supplemental* to domestic action, therefore the appropriate ratio between the Party's level of mitigation and use of NMM should be properly determined.
 - Be subject to the *common standards* developed under the FVA:
 - Deliver *real, permanent, additional and verified emissions reductions and/or avoidance*.
 - *Disallow double counting*.
 - Participation in the various mechanisms should be voluntary but to attract participation there must be adequate demand, there may have to be a consideration for exploration of price floors, introduction of reserve margins for tradable units, regulation of the market to intervene when the market takes too long to clear.

South African context: Key Policies

- Constitution
- National Climate Change Response Policy (NCCRP)
- PPD
- National Development Plan (NDP)
- New Growth Path (NGP)
- Carbon Tax
- Industrial Policy Action Plan (IPAP)
- Integrated Resource Plan (IRP)
- National Sustainable Development Strategy

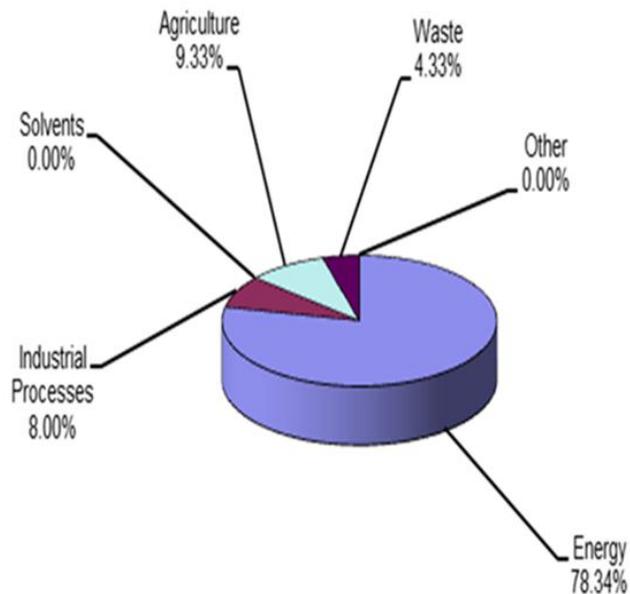
SA's international commitments

The desired South African climate change mitigation outcome - the "Peak, Plateau and Decline" (PPD) greenhouse gas emission trajectory – comparison with other popularised conceptions of PPD

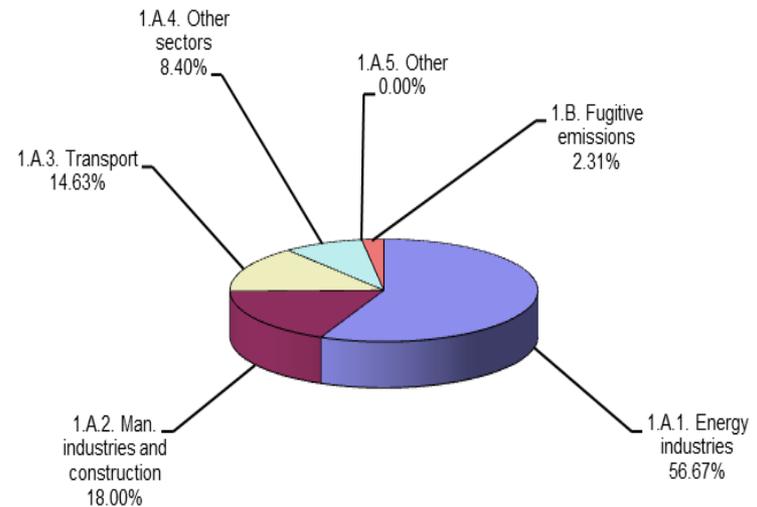


Energy sector contributes more to emissions and industry is more energy intensive

SA's GHG profile (UNFCCC)



Energy sector breakdown

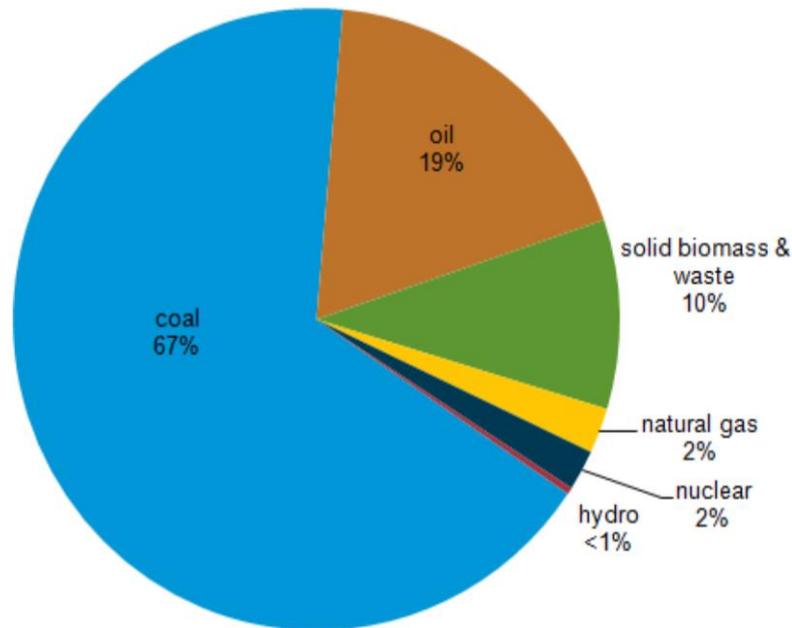


South Africa is largely dependent on coal but seeks to transform to a low carbon economy

IEP

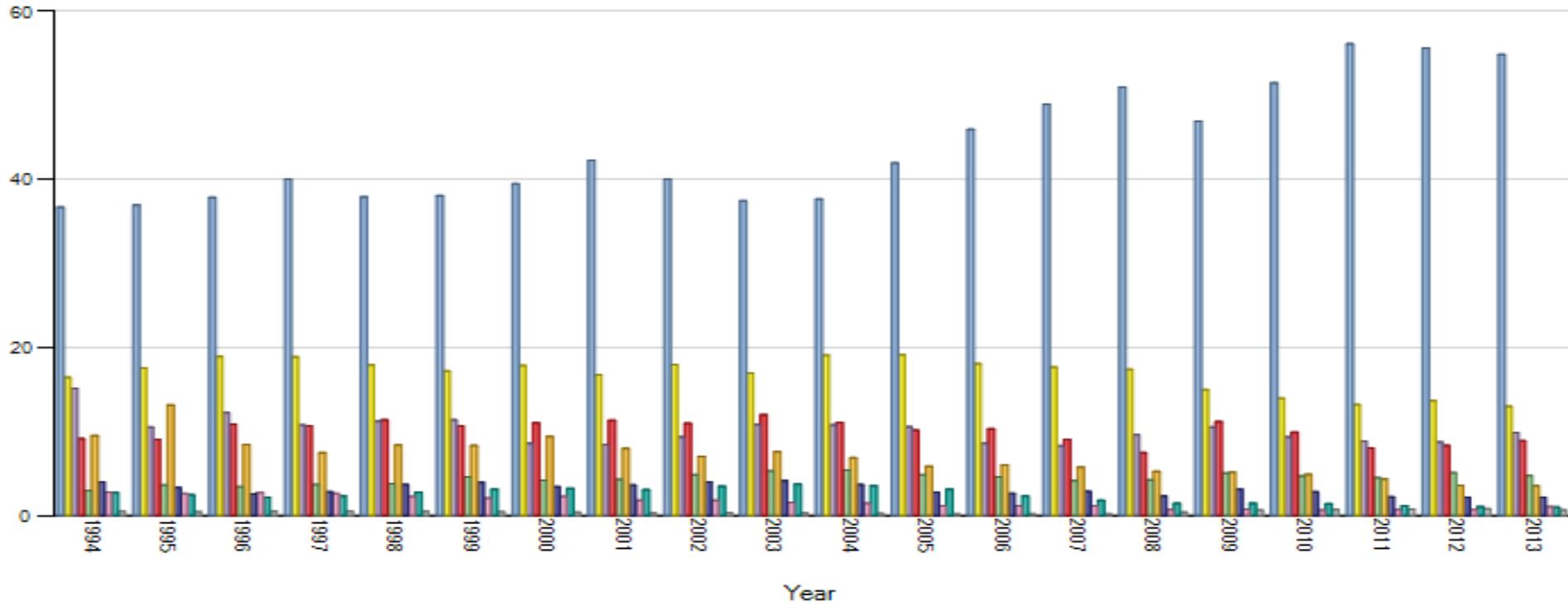
“Primary Energy supply in South Africa is dominated by coal (~67%), followed by crude oil (~20%). Nuclear, natural gas and renewable energy (including hydro and biomass) have historically played a less significant role in the total energy mix, collectively contributing the remaining ~13%.”

Total primary energy supply in South Africa, 2010



Source: U.S. Energy Information Administration

Key export sectors and sectoral breakdown – value terms (Top – 10) -



HS

- C05: Mineral products (25-27)
- C06: Products of the chemical or allied industries (28-38)
- C02: Vegetable products (6-14)
- C04: Prepared foodstuffs; beverages, spirits & vinegar; tobacco & manufactured tobacco substitutes (16-24)
- C07: Plastics & articles thereof; rubber & articles thereof (39-40)
- C10: Pulp of wood or of other fibrous cellulosic material; waste & scrap of paper or paperboard; paper & paperbo...
- C01: Live animals, animal products (1-5)
- C08: Raw hides & skins, leather, furskins & articles thereof; saddlery & harness; travel goods, handbags & simila...
- C09: Wood & articles of wood; wood charcoal; cork & articles of cork; manufactures of straw, of esparto or of oth...
- C03: Animal or vegetable fats & oils & their cleavage products; prepared edible fats; animal & vegetable waxes (...)

Proposed carbon tax design features

- A carbon tax at R120 per ton of CO₂e above the suggested thresholds with annual increases of 10 per cent until 2019/20 is proposed as from 1 January 2015.
- A basic tax-free threshold of 60 per cent is proposed.
- Additional tax-free allowance for process emissions (10%)
- Additional relief for trade-exposed sectors (max 10%)
- Carbon offsetting allowed to reduce carbon tax liability (max 5% or 10%)
- The overall tax-free allowance for an entity will be capped at 90 per cent of actual verified emissions.
- Tax-free thresholds will be reduced during the second phase (2020 to 2025) and may be replaced with absolute emission thresholds thereafter.

Carbon Tax policy sectoral classification (this list is to be refined and expanded along IPCC classification)

Sector	Basic tax-free threshold*	Maximum additional allowance for trade exposure	Additional allowance for process emissions	Total	Maximum offset
Electricity	60	–	–	60	10
Petroleum (coal/gas to liquid)	60	10	–	70	10
Petroleum – oil refinery	60	10	–	70	10
Iron and steel	60	10	10	80	5
Cement	60	10	10	80	5
Glass and ceramics	60	10	10	80	5
Chemicals	60	10	10	80	5
Pulp and paper	60	10	–	70	10
Sugar	60	10	–	70	10
Agriculture, forestry, land use	60	–	40	100	0
Waste	60	–	40	100	0
Fugitive emissions – coal mining	60	10	10	80	5
Other	60	10	–	70	10

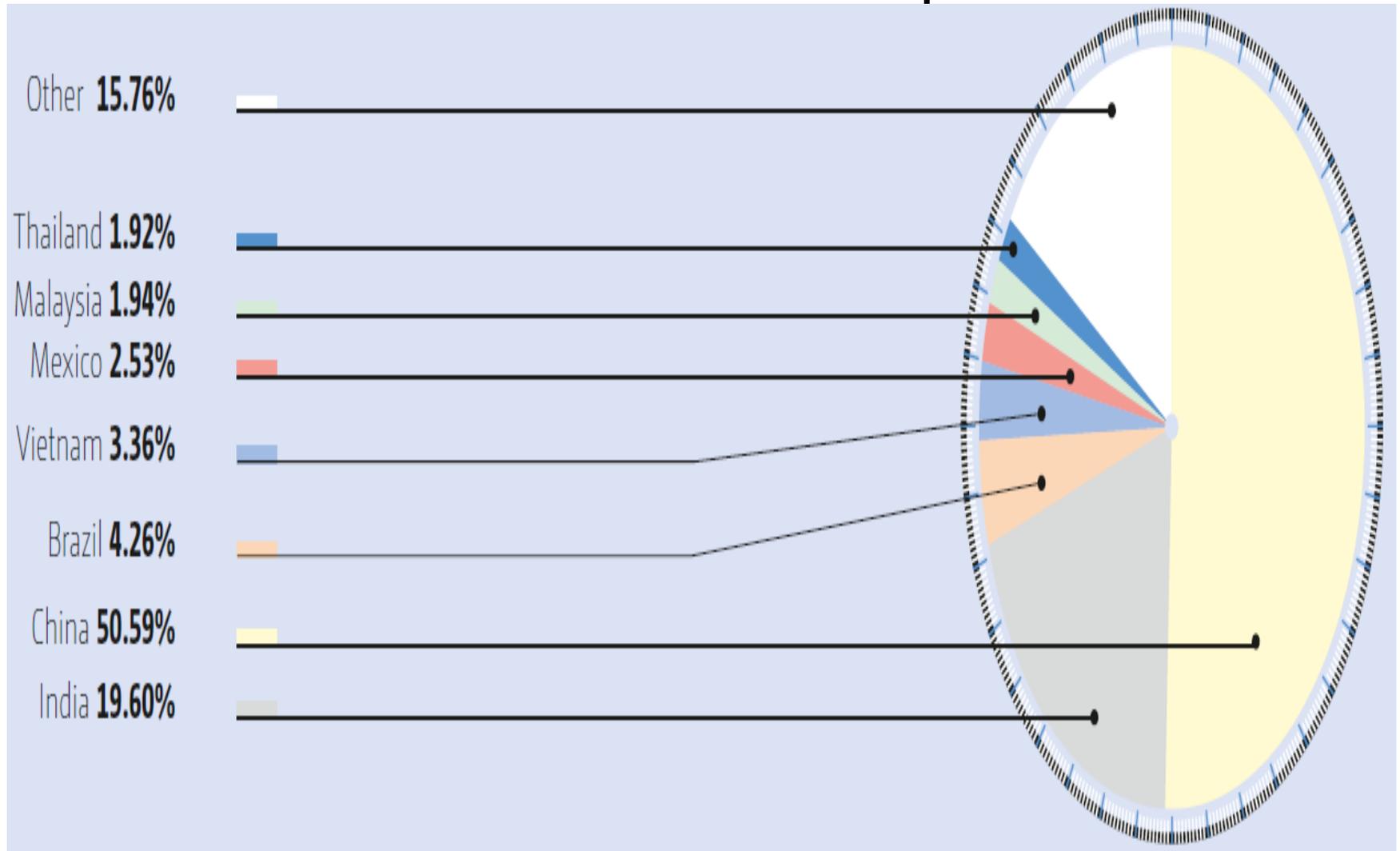
INSTITUTIONAL INFRASTRUCTURE – SOME OF THE CONSIDERATIONS

CDM

CDM Purpose

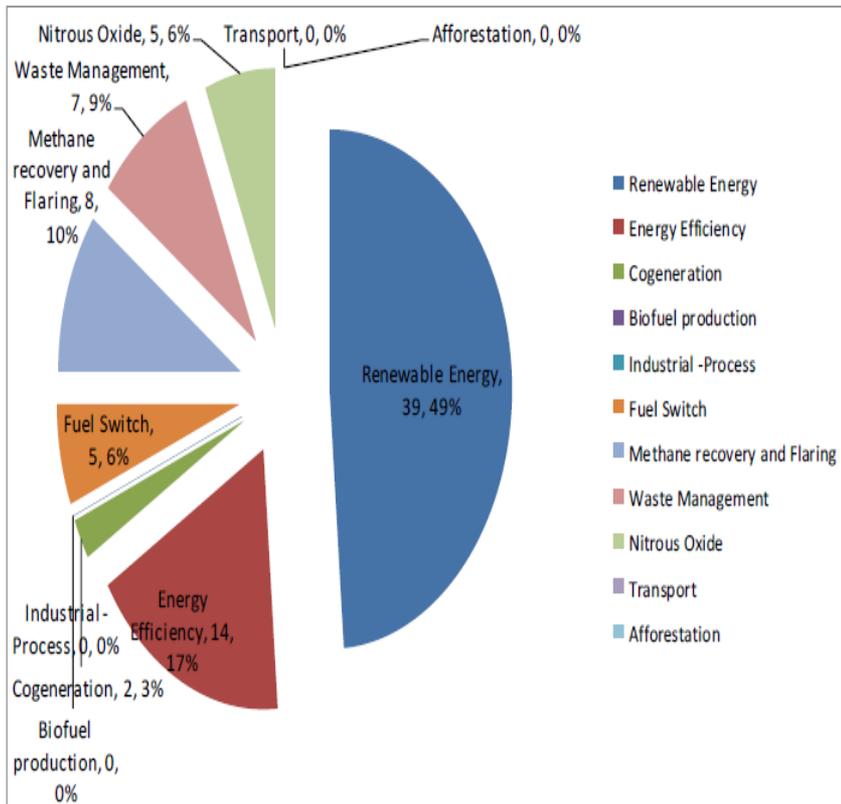
- The purpose of the CDM is twofold:
 - To assist an Annex I Party, the Industrialised Country, in complying with its Kyoto targets,
 - To contribute to technology transfer and sustainable development in the host Party, the Developing Country.

The global spread of CDM projects is unevenly distributed – CDM EB Annual report 2013



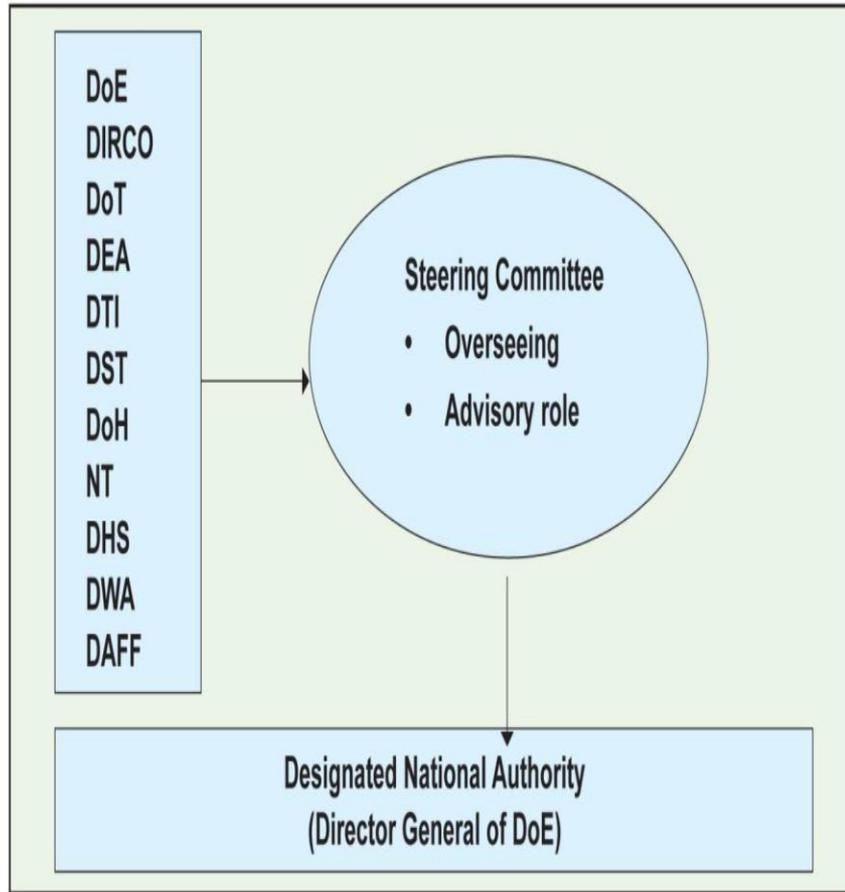
Further considerations

CDM project distribution in SA: registered projects



- Priority project categories
- Auction/ free allocation/ hybrid approach for allowances
- Quantitative restrictions
- Tracking and registry – MRV considerations.
- Real reductions in emissions should be MRV'd
- Compliance vs voluntary participation.
- Cost containment reserves and price stabilization/ price floor/ price ceilings etc.

Institutional arrangement for CDM



- DNA works hand in hand with a technical advisory steering committee. The committee is comprised of members from thirteen National Departments.
- In the public domain there is:
 - South African CDM Project Approval Procedure;
 - Sustainable Development Criteria;
 - Guideline for CDM Applicants in South Africa.
 - Reach out stakeholders interested in developing CDM projects through workshops,
 - one on one meetings and seminars.

Key challenges related to CDM projects

- Lack of Project Finance
 - Many projects are stuck at an idea note
 - Financial institutions conduct risk assessment before providing loans to CDM project proposals.
 - Scale vs cost issues.
- Complexity of the CDM
 - The process is lengthy and costly
 - Continuous development of the CDM procedures
- High Transaction costs incurred upfront – hit hard especially to small scale projects.
- EU's directive on restrictions to use of CERs from projects registered after Dec- 2012 may affect the appetite for CDM investments.

Potential for domestic offsets

- The expected demand for offsets generated by the carbon tax could be between 25 and 30 million tonnes of CO₂e per annum,
- A potential supply of over 50 million tonnes of CO₂e per annum has been estimated.
- Main sectors – agriculture, manufacturing industries, energy demand, metal production, chemical industries etc.
 - Industrial sectors
 - Land sector

Expectations

- To learn how other countries whose share of CDM projects – they have a strong infrastructure to introduce domestic offsets.
- What critical design elements are in place that enable investment attraction?
- What considerations inform the choice of standard to be used domestically?

Conclusion

- Be advised that this is an overview presentation of broad considerations as the policy linked to offsets programme is still under development.