



Biodiversity in Environmental Fiscal Reform Workshop

Stewardship, Protected Areas and Fiscal Incentives

Elements of sound environmental fiscal policy -with a focus on biodiversity

Presentation by ETA unit, National Treasury, South Africa
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Presentation Outline

1. Introduction
2. Draft environmental fiscal reform policy paper
3. Environmental Fiscal Reform Agenda
4. Summary of key regulatory and tax reforms
5. Incentives for biodiversity management and protection
 - Income Tax Act Amendments 2008
6. Conclusions



Introduction 1

- Movement → more unregulated economies (or market economies)
- Interrelated and integrated world economy
- Rapid economic growth → more resource demands and greater challenges to Sustainable Development.
- Conflict between Economic Growth (rising GDP) and the State of the Environment.
- Result: uncertainty → insecurity, lack of trust, speculation, instability.
- Certainty brings stability
- Criteria: Fiscal policy bring certainty to the market.
- Certainty and equity (fairness)



Introduction

- Sustainable development is about enhancing human wellbeing over time and managing a broad portfolio of economic, social and environmental assets that society has at its disposal in order to sustain a flow of consumption.
- As the South African economy grows, it's important to ensure that it's not just the quantity of growth that matters but also its quality.
- It is estimated that almost 40 percent of the global economy is based on biological products and processes.
- Current population pressures and consumption trends has seen an increase in the rate of loss in biodiversity.



Introduction

- To conserve and maintain biodiversity, societies have identified priority areas which they deem valuable.
- Conservation measures largely regulatory in nature and include
 - setting aside land for national parks; and
 - imposing use restrictions on certain plants and animals.
- National Treasury embarked on a process to outline the role for market-based instruments to achieve environmental objectives in 2003.
- In 2006, the draft Environmental Fiscal Reform Policy paper was published for comment.



A View From Australia

In a recent address to: The Curtin Public Policy Forum the secretary of the Treasury in Australia, Ken Henry, listed eight medium-term challenges that economic policy advisers (in Australia) should be thinking about, these include inter alia:

- (a) “increasingly challenging issues in the inter-relationship between energy, climate change and water; and
- (b) some deeply entrenched failures in environmental management, including **loss of biodiversity**, partly due a history of exploitation of the ‘commons’ ”.

He also argues that:

“Market mechanisms will have to be used to do more, not less, of the allocation task, but with more attention paid to the role of government in defining property rights, pricing for externalities, and representing the interests of future generations”.



Fiscal Policy

- Fiscal Policy as one of the key instruments of the Economic Policy in the pursuit of
 - solid economic and productivity growth,
 - high employment and labour force participation,
 - low and stable inflation ,
 - and improved quality of life.



Policy Outcomes

To meet these policy outcomes (objectives) require:

- a sound ***macroeconomic environment***;
- effective taxation and government spending arrangements (fiscal sustainability- ***sustainable government finances***) and
- the managing of a broad portfolio of economic, social and environmental assets that society has at its disposal

This in order to sustain a flow of consumption to bring about improvements in wellbeing.



Macro Policy Framework

- It requires, a sound macroeconomic policy framework, consisting of monetary, fiscal and other instruments which supports sustainable economic growth and economic efficiency with consideration for environmental protections a major determinant of living standards in society and thereby the wellbeing of successive generations.



Dichotomy

- A dichotomy exists between strong economic growth (without appropriate environmental considerations) and the poor use of resources with its resultant production externalities leading to degradation of the environment and loss of productive capacity.
- Environmental (or ecological) Fiscal Reform (EFR) is about the wiser use of our natural resources and the wider use of our labour resources in our economy.



Environmental Fiscal Reform in South Africa

- Environmental fiscal reform refers to the interface between *environmental* and *fiscal* policy measures.
- An opportunity exists to undertake reforms to existing MBIs and develop new environmental tax instruments to achieve environmental goals.
- The draft Environmental Fiscal Reform Policy Paper provides the foundation to build on and support other environmentally related initiatives in South Africa.



Fiscal Reform in SA

- The National Treasury has published a draft policy paper in the area of Environmental Fiscal Reform styled “A Framework for Considering Market-Based Instruments to Support Environmental Fiscal Reform in South Africa”.
- The paper outlines the role that market-based instruments, specifically environmentally related taxes and charges, could play in supporting sustainable development in South Africa, and to provide a framework for considering their possible application.
- As the South African economy grows and imposes increased demands on its environmental assets base, it is vital that it does so in a sustainable manner and that issues such as poverty, inequality and international competitiveness are effectively addressed.
- The paper focuses and elaborates on the options for environmental fiscal reform and the policies and measures that could be used to achieve both environmental and revenue-raising objectives.



Scope of the Policy Paper

- The policy paper focuses mainly on taxes and charges whilst giving due consideration to the importance of incentives where appropriate.
- It presents a guiding framework and criteria that should be used in developing and evaluating environmentally-related taxes and charges for South Africa.
- Expenditure reforms such as direct subsidies for environmentally beneficial activities are not considered in the paper.



Why the Need for a Policy Paper?

- Maintenance of a coherent tax policy framework;
- Development of a coherent process and framework to consider and evaluate environmental taxes; and
- Consider both environmental and revenue outcomes and the “double-dividend” hypothesis.



Environmental Challenges

- Air pollution and climate change;
- Biodiversity loss and damage to terrestrial ecosystems;
- Land degradation;
- Water pollution and water quality and resource management; and
- Waste generation
- Energy generation, usage and waste disposal



Intervention Options

- **Command-and-control measures (regulatory mechanisms):**
 - Use of legislative or administrative regulations that prescribe certain outcomes;
 - Usually target outputs or quantity, e.g. minimum ambient air quality standards, within which business must operate.
- **Market-based instruments:**
 - Policy instruments that attempt to internalise environmental externalities through the market by altering relative prices that consumers and firms face;
 - Utilise the price mechanism and complement command-and-control measures. Under certain circumstances MBIs are considered more efficient than command-and-control measures.

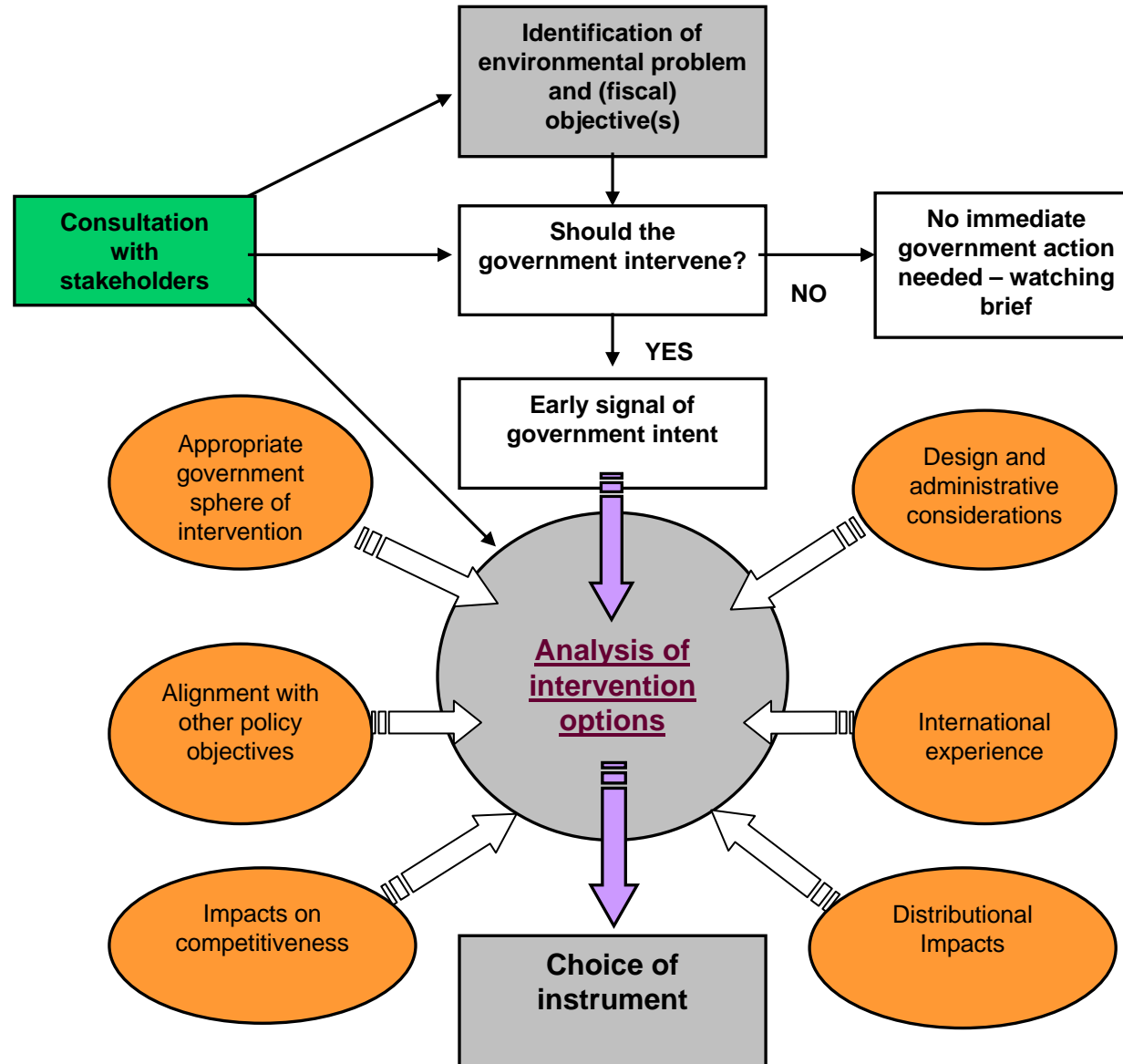


National Framework for Sustainable Development

- As a developing country, the key challenge for SA is to ensure an improvement in human development indicators and reduction in poverty levels.
- The draft National Framework for Sustainable Development analyses and identifies the most urgent trends related to energy, water, soil, and waste as a result of economic growth strategies:
 - Rising per capita electricity consumption reaching 3860 kWh per person per annum by 2003;
 - Excessive freshwater consumption per capita and inefficient water use by key industrial and agricultural sectors;
 - Rising CO₂ emissions per capita (more than 9 metric tons per person per annum compared to global average of ~6); and
 - Faster growth of municipal solid waste than the average economic growth rate, nearing average of 2kgs / person / day in some cities.



PROCESS TO EVALUATE OPTIONS





A Framework for Considering Environmental Taxes

- Market-based instruments have a number of advantages when used to supplement regulatory approaches.
- How should the relative merits of different environmentally-related tax proposals be assessed?
- What does a good environmentally-related tax look like?



Criteria / Design Considerations

- **Purpose** – scope, intent and reach
- Environmental effectiveness – **must be linked to the environmental externality and aim for best design possible (e.g. exemptions);**
- Tax revenue – **level of revenues and revenue use/revenue neutrality;**
- **Support for the tax** – public support and acceptance is important (e.g. tax payer morality);
- Legislative aspects – **implications need to be considered (also WTO, SADC);**
- Technical & administrative feasibility:
 - *Define taxable commodity;*
 - *Setting the tax rate;*
 - *Tax avoidance and evasion;*
 - *Collection costs; and*
 - *Compliance costs.*
- Competitiveness impacts – **tax incidence is critical. May require adoption of mitigating measures;**
- Distributional impacts – **mitigation and compensation measures may need to be considered; and**
- Adjoining policy areas – **is the instrument capable of contributing to other social and economic objectives?**



Internalisation Of Externalities – Competitiveness Issues

- Internalising negative externalities comes at a price.
- Aims to internalise externalities to a socially optimal level cannot be achieved overnight.
- There are “win-win” cases where more environmentally informed business practices could lead to corresponding improvements in competitiveness.
- Improved environmental performance may also improve access to certain markets – notably in the export sectors.
- However, these benefits are not immediately possible in all cases.
- A phased approach taking account of potential impacts on competitiveness must be adopted to give specific sectors time to adjust.



Distributional Issues - Impacts On The Poor

- The poor and low-income groups are often hardest hit by negative environmental externalities.
- Important for environmentally-related fiscal policy to ensure that environmental instruments are pro-poor where possible, or at least do not place a disproportionate burden on low-income groups.
- A sustainable growth path should provide protection and support to the poor.
- That is development that meets the needs of the present without compromising the ability of future generations to meet their own needs.
- Tradeoffs to be well managed.



Environmental Fiscal Reform Agenda

- Climate change:
 - Electricity levy
 - Consideration of tax treatment of CERs related to Clean Development Mechanism.
 - Engaging with DEAT on Long Term Mitigation Scenarios Project and aligning with the work of Treasury..

- Other:
 - Motor vehicles: reforms to ad valorem excise duties for environment purposes. Incorporate environmental criteria:
 - Fuel economy
 - Carbon dioxide emissions
 - Engine size
 - Incentives for cleaner production:
 - Energy efficiency
 - Water use efficiency



Environmentally-related taxes in SA

- **Transport Fuels**
 - GFL
 - RAF
 - Equalisation Fund levy (0)
 - Customs & Excise levy
- **Vehicle taxation**
 - Ad valorem Customs & Excise
 - Road licencing Fees
 - Environment Excise?
- **Aviation Taxation**
 - Aviation Fuel levy
 - Air Passenger Departure Tax
 - Airport Charges
- **Product taxes**
 - Plastic shopping bag levy
- **Electricity levies**
 - NER levy
 - Local Govt surcharge
 - Electricity levy
- **Water Supply**
 - Water Resource Mgt charge
 - Water resource development works charge
 - Water Research Fund levy
 - Muncipal surcharge
- **Waste water**
- **Waste disposal (including radioactive waste)**



New Environmentally-related Tax Instruments (NEPI)

- Electricity
 - Electricity consumption tax; and/or
 - Fossil fuel input tax.
- Water supply and use – tax instruments probably less appropriate than alternative allocative instruments such as tradable permits;
- Waste water – DWAf has already taken the initiative in this area and is in the process of developing the Waste Water Discharge Charge System (WDCS).



Active Legislation

(A) Air Quality Act

- The Air Quality Management Act aims to address air pollution holistically and covers atmospheric pollutants including:
 - Smoke or particulate emissions (coal and fuel burning)
 - Vehicle emissions
 - Dust from mining activities
 - Sources of greenhouse gases
 - Transboundary pollution
- Existing minimum ambient air quality standards apply to ozone, oxides of nitrogen, nitrogen dioxide, sulphur dioxide, lead particulate matter, and total suspended solids.
- The act allows for the use of emissions trading schemes and incentives to reduce air pollution.
- The role of charges / taxes to complement regulatory measures to achieve air quality objectives to be explored further.



(B) Waste Bill & Radioactive Waste Bill

- SA implements the Waste Management Hierarchy as the guiding principle for waste management practices.
- It encourages waste avoidance, minimisation, recycling and reuse, waste treatment and final disposal (when all options exhausted).
- The Waste Bill seeks to apply a range of new waste management related concepts; and replace and / or clarify existing waste management legislation.
- The bill empowers the Minister of Environmental Affairs and Tourism to:
 - Establish regulations related to waste minimisation targets for specific goods / products; and
 - Implement financial incentives / disincentives to encourage behaviour towards waste management and generation.
- The use of MBIs as part of a strategy to manage waste will be explored.



(C) Environmental Tax Reforms

- Accelerated depreciation allowances for plant and machinery used for the production of biofuels and electricity generation from renewables.
 - 50:30:20 per cent write-off over three years.
- For income tax purposes, companies are allowed deductions for expenditures incurred in the production of income. Special depreciation rules apply to expenditures of a capital nature.
 - Amendments to the Income Tax Act to ensure that business expenses, operating or capital, incurred for the purpose of environmental protection is treated similar to other business expenses.
- Amendments to the income tax act to support biodiversity conservation and management by private landowners.



Mine Rehabilitation

- In terms of the Mineral and Petroleum Resources Development Act:
 - all mining companies must complete Environmental Management Programme Report and make financial provision for mine rehabilitation on closure.
- Mines can set aside funds using the following financial provision method/s:
 - Contributions to a dedicated trust fund; and / or
 - Financial guarantees.
- For contributions made towards an approved mining rehabilitation trust fund, the income tax act allows:
 - Deductions for income tax purposes; and
 - Tax free build-up of such reserves.
- The terms of the fund must be approved by the Minister of Minerals and Energy and the sole purpose must be environmental rehabilitation.



Promotion of Biodiversity

- The DEAT has established a regulatory framework to encourage the **conservation** and **protection** of **biodiversity** and priority areas by private landowners to support sustainable economic development.
- **The key pieces of legislation** that enables this process are:
National Environmental Management
 - Biodiversity Management Act (No 10 of 2004)
 - Protected Areas Act (No 57 of 2003) (National Parks and Reserves)
- Private landowners may enter into agreements and management plans in terms of above legislation:
 - Private owners surrender some level of use in the land (and improvements thereon)
 - Private owners are often required to make operating and capital expenditure to maintain the land



Existing Income Tax Provisions

- Even though operating expenses may be required under these agreements, these expenses do not qualify for tax relief unless part and parcel of a trade
- Capital expenditures under these agreements cannot be depreciated (nor can the cost of land be deducted)
- However,
 - Landowners incur conservation and maintenance expenses that generate benefits for society.
 - Landowner restricted from using the land for other purposes except as stipulated in the agreement.



Amendments

- *Biodiversity Management Agreements*
 - Conservation maintenance and rehabilitation expenses incurred by landowners will be allowed as deduction against trading or farming income
- *National Parks and Reserves* (outside the vicinity of a trade/farm):
 - Conservation maintenance and rehabilitation expenses incurred by landowners subject to **30 year declaration** will qualify for a tax deductible section 18A donation
 - Amount of cost to landowner to acquire land plus capital expenditure incurred by landowner in respect of the land declared as a **national park or nature reserve** subject to a **99 year period of declaration** will qualify for a tax deductible section 18A donation



Summary of Provisions:

- **Conservation and Maintenance Expenses:**
 - Provisions implemented in terms of **Section 37C** of the Income Tax.
- Biodiversity Management Agreement (S44 of NEMBA) of at least 5 years.
 - Allowed **income tax deductibility** i.t.o **S 11(a)**
 - Where deductions exceed income – deemed to be expenditure incurred in following year of assessment.
 - Businesses can claim this deduction.
- S 20, 23 & 28 of the National Protected Areas Act
 - Deemed to be a donation for purposes of **S 18A** of the Income Tax Act where declaration of at least **30 years**.
 - Where declaration is for **99 years**, S37C provides for section **18A deduction** and **exemption from Capital Gains Tax**.
 - Available to all landowners.



Conclusion

- Biodiversity conservation generates benefits for current and future generations.
- Economic growth? Yes
- However, the maintenance of an adequate natural resource base is essential for economic growth and poverty alleviation objectives.
- The role for market-based instruments such as **taxes and user charges** and **incentives** should not be underestimated.
- Price signals present a way to achieve environmentally preferable outcomes and complement the current regulatory framework.
- Finally, the need to conserve and manage biodiversity should be considered in the broader context of climate change.



Thank you.