

Carbon pricing for our future

Seven years ago, in April 2016, Malaysia officially signed on to the Paris Agreement to pledge its commitment to achieve carbon neutrality by 2050. But since then, there has been no sight of a definitive road map to achieve this national goal, leading to questions on whether this remains only an ambition.

The latest report from the Intergovernmental Panel on Climate Change (IPCC) warned that global emissions will need to be halved by 2030, if warming is to be limited to 1.5°C. The solution, according to scientists, lies in climate-resilient development, which involves integrating measures with actions to reduce or avoid greenhouse gas (GHG) emissions.

Malaysia's GHG emissions per capita is among the highest among the Asean nations, recorded at 12.77 tonnes in 2021 compared with our closest neighbours, Singapore (6.7 tonnes) and Thailand (6.31 tonnes).

To keep emissions on a downward trend, many are expecting a carbon tax to be implemented in Malaysia soon. To understand carbon tax, we must study carbon pricing mechanisms. Simply put, carbon pricing is the act of putting a price on pollution. By imposing some form of carbon pricing mechanism on businesses and industries that produce GHG through their operations, the government aims to encourage businesses to lower their GHG output, which



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predominantly comprises carbon dioxide (CO₂). In principle, carbon pricing can take the form of carbon taxes or emissions trading schemes (ETS).

Carbon taxes are usually fixed rates taxed per tonne of carbon dioxide emission (tCO₂e). Singapore introduced carbon taxes in 2019, which are levied on all facilities with annual direct GHG emissions of 25 kilo tonnes of carbon dioxide (ktCO₂e) or more, and no exemptions were provided. During the first five years, Singapore's carbon tax rate is set at S\$5/tCO₂e and this will increase fivefold to

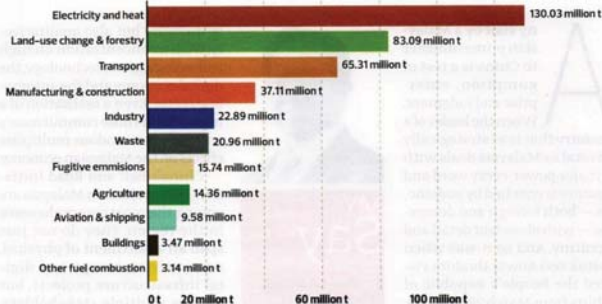
S\$25/tCO₂e in 2024 and 2025, and subsequently to S\$45/tCO₂e in 2026 and 2027. Singapore expects to collect a total of US\$1 billion in revenue from the first five years of its carbon tax scheme.

The potential of additional tax revenue enhances the appeal of implementing a carbon tax, which is easier to manage administratively and can also be applied at various points of the production chain where large emitters are identified, and heavy taxes are implemented on those sectors. However, the possibility exists where large emitters may circumvent the issue and choose to pay the penalty without making actual efforts to reduce GHG emissions.

For this reason, some jurisdictions introduce ETS as a form of carbon pricing on top of the carbon tax, such as seen in Switzerland and Canada. Leveraging ETS, also known as a cap-and-trade programme,

Greenhouse gas emissions by sector in Malaysia (2019)

Emissions are measured in carbon dioxide equivalents (CO₂eq). This means non-CO₂ gases are weighted by the amount of warming they cause over a 100-year timescale.



the government will set a limit on the total level of covered GHG emissions (that is, cap) and a free market exists between entities to trade carbon pricing instruments.

For example, the European Union Emissions Trading System (EU ETS), one of the world's largest emissions trading markets, set a cap of 1,572 MtCO₂e in 2021 and is expected to decrease by 2.2% annually. The emission allowances under the cap are then distributed by way of free allocation and auctions depending on the sectors. This approach allows lawmakers to legally set an ETS cap to reduce GHG emissions on a national scale.

The ETS approach is already being explored in Malaysia. Further to the release of the National Guidance on International Voluntary Market Mechanisms by Malaysia's Ministry of Environment and Water

in 2021, Bursa Malaysia recently launched the Bursa Carbon Exchange (BCX).

BCX is the country's voluntary carbon market exchange that offers high-quality standardised carbon credits for both buyers and suppliers to transact at transparent prices via a rules-based carbon exchange. According to BCX, entities may purchase these credits to offset their carbon footprint while the sale of carbon credits, in return, is used to help steer the development of reduction and removal of domestic GHG emission solutions.

It remains to be seen if a regulatory-based ETS will be introduced by the Malaysian government, similar to that of BCX with a tighter compliance regulation scheme, or if a carbon tax would be introduced, similar to that of Singapore, or

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possibly a combination of both.

For certain, our government will not have an easy time determining a carbon pricing mechanism that will be equally received by all affected parties. Its effectiveness in reducing carbon emissions will be heavily reliant on the availability of clear guidelines and support provided. There is also the concern that imposing stringent climate policies will affect Malaysia's competitive standing in the short term, compared with other jurisdictions that are less stringent in policies.

But there is no doubt that a form of carbon pricing mechanism is imminent for Malaysia as a manageable way to achieve the national net zero ambition by 2050. Therefore, businesses should approach carbon taxes proactively (and not reactively) so they can be in a stronger position to identify opportunities and challenges, not only from a tax perspective but also from a sustainability perspective.

Businesses will have to look into how their accounting costs and margins will be affected, especially if they are heavily reliant on carbon-intensive products and sources. Additional compliance costs may

need to be taken into consideration with the implementation of carbon taxes. It is also crucial that businesses look into investing in cleaner technologies with reduced carbon footprints. Paired with the green incentives that the government continuously introduces, this will drive the interest in making more green solutions available nationwide and result in relatively cheaper green technologies.

Sweden was among the early adopters of carbon tax 32 years ago, and its experience demonstrated that progress on a national scale is possible with political will, introduction of policies that are supportive and inclusive, and with committed cooperation between the government, academia, businesses and society as a whole. Since 1990, Sweden has successfully decreased its GHG emissions by 33% and also reported that its gross domestic product grew by 92% during the period up until 2021.

Our future depends on what we can achieve within the next decade, so let's collectively roll up our sleeves and get started. **E**

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