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Ministry for the
Environment
Manatū Mō Te Taiao



ETS Review Panel recommendations – Work programme and priorities for the February 2012 Cabinet paper

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Purpose

	Action Sought	Deadline
Minister for Climate Change Issues Hon Dr Nick Smith	Agreement to the ETS review work programme and priorities for the Feb 2012 Cabinet paper.	19 October 2011
Minister of Forestry Minister of Agriculture Hon David Carter	Agreement to the ETS review work programme and priorities for the Feb 2012 Cabinet paper.	19 October 2011

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Executive Summary

1. This briefing seeks your agreement to the proposed work priorities for the February 2012 Cabinet paper. It also provides you with an initial risk assessment should the Government decide not to pursue legislative change in 2012.
2. The ETS 2011 Review Panel (the Panel) provided its final report to the Minister for Climate Change Issues on 30 June 2011. On 18 July 2011, Cabinet invited the Minister for Climate Change Issues to report to Cabinet by February 2012 with proposed changes to the ETS based on the Panel's recommendations [Cab min (11) 27/15 refers].

3. Given the possible breadth and range of matters that could be considered for the February Cabinet paper, the relatively tight timing if legislation is to be passed by the end of 2012, and available departmental resources, it is necessary to prioritise.
4. It is also likely that different policy proposals will be at different stages by February, and therefore that the Cabinet paper will include:
 - a. a set of final and detailed policy proposals to modify the ETS;
 - b. a set of proposals for consultation; and
 - c. issues for further detailed analysis which would then be consulted on via the Select Committee process.
5. Given the need to prioritise:
 - officials propose that a number of the Panel's recommendations be progressed in 2012 but not form part of legislative amendment in 2012. This includes the response to the Panel's recommendation on averaging for post-1989 forests, which officials propose be widened in scope and reported to Ministers later in 2012.
 - Ministers are also asked to indicate whether they would like to progress the Panel's recommendations for changes to the transition phase and allocation for agriculture given that a review of agriculture's entry into the scheme has been foreshadowed for 2014. The proposed change to allocation is technical; but the proposal to introduce a transition phase is more substantive.
 - Officials propose that Ministers agree that no further work be undertaken on the Panel's recommendations on the Field Measurement Approach (FMA). Analysis on changing the 100ha threshold was undertaken when designing the FMA and indicated it would involve significant fiscal and compliance costs.
6. Subject to your agreement, officials will continue to progress the priorities for the February 2012 report-back as outlined in this briefing. Officials will brief the Minister for Climate Change Issues and the Ministers of Agriculture and Forestry as early as possible after the election to seek a steer on the content of the February Cabinet paper.
7. At the request of the Minister for Climate Change Issues officials have also considered what risks could be posed if the Government decided not to pass legislation to amend the ETS next year. Clearly it would not be possible to implement a number of the Panel's more significant recommendations (e.g. those relating to the transitional arrangements).
8. Officials have considered whether the likely gap in binding international agreement post 2012 will create any risks for the operation of the ETS should the Climate Change Response Act 2002 (the Act) not be amended in 2012. The obligations and process created by the Act as to allocation and the surrender of units aren't directly linked to, or dependant on, the existence or particular wording of the Kyoto Protocol. In addition, the issuing of New Zealand Units (section 68) specifically anticipates the possibility of no international protocol post 2012 and sets out a process to follow for issuing units.
9. However, there is some uncertainty about the nature of international carbon markets post 2012, which may mean that participants in the ETS will be at greater risk of price volatility should the international emission unit supply decrease substantially. Officials are currently gathering information on the likely availability of international units post 2012 and assessing the issues that may be created. Key risks and options for managing them will be addressed in the February 2012 Cabinet report-back.
10. In addition, agencies involved with the administration of the ETS have identified a range of possible amendments to the Act that, while not required for the ETS to operate, would improve its operation.

Situation Analysis

11. This briefing seeks your agreement to the proposed work priorities for the February 2012 Cabinet paper. It also provides you with an initial risk assessment should the Government decide not to pursue legislative change in 2012.
12. The ETS 2011 Review Panel (the Panel) provided its final report to you on 30 June 2011. The report contains 61 recommendations. Should the Government wish to accept them, a number of these recommendations would require amendments to the Climate Change Response Act 2002 (the Act) in 2012.
13. On 18 July 2011, Cabinet invited the Minister for Climate Change Issues to report to Cabinet by February 2012 (through the relevant Cabinet committee) with proposed changes to the NZ ETS based on the Panel's recommendations, developments in and discussions with Australia and further analysis [Cab min (11) 27/15 refers].
14. In subsequent discussion with officials the Minister for Climate Change Issues requested advice on the risks if the Government decides not to pass amendment legislation in 2012.
15. On 15 September the Minister for Climate Change Issues released the Panel's report and announced that the government is advancing the detailed work on the 61 recommendations, noting that there are both upside and downside fiscal implications in different recommendations that will need to be considered.

Advice

The Cabinet report-back in February 2012

16. Officials have started work on an ETS Review response project (the project). The project comprises of analytical work on the response to the 2011 ETS Review Panel's recommendations, other matters identified by Ministers, officials, advisory groups (such as the Agricultural ETS Advisory Committee) and stakeholders; and minor technical amendments to improve the operation of the ETS. The output will be advice to Ministers in 2012 on amendments to the Act.
17. A number of the changes (if agreed) would need to be legislated before 2013. Therefore the timeframe for this work is relatively tight. There are a number of proposals that would likely require consultation (subject to Cabinet agreement), and consultation would need to occur early in 2012 in order to allow sufficient time for the passage of legislation. Therefore any matters which the Government wishes to progress ideally need to be agreed to in February 2012.
18. Given the possible breadth and range of matters that could be considered as part of the project, the relatively tight timing if legislation is to be passed by the end of 2012, and available departmental resources, it is necessary to prioritise the issues to be progressed for the February Cabinet paper.
19. Some matters falling outside this priority will be progressed over a longer time period. In some instances we recommend that you agree that certain issues will not be progressed at all or be deferred to the next ETS review to consider.

Nature of decisions in February

20. Given the range of matters and the time scale for the project it is likely that different policy proposals will be at different stages by February. It is therefore likely that the Cabinet paper will seek a range of decisions including:

- a) a set of final and detailed policy proposals to modify the ETS;
- b) a set of proposals for consultation in March/April 2012, with a view to making decisions on any resulting legislative amendments by May 2012;
- c) issues for further detailed analysis by May 2012, either through this project or related work (which would then be consulted on via the Select Committee process).

21. There have been a number of recent consultation opportunities in relation to the ETS, and officials therefore recommend any further consultation on the matters already raised be focused and targeted. For example, officials consider that there has been sufficient consultation in relation to the transition arrangements, especially given the Panel specifically asked about current and expected impacts of the ETS in its consultation. Where there has been less or no consultation, such as on the Panel's recommendations on offsetting and the treatment of synthetic greenhouse gases, further consultation may be necessary to fully understand the issues and quantify the impacts of the proposed changes.

22. Ministers also need to consider whether (and if so when) they wish to issue a formal response to all of the Panel's 61 recommendations. As previously advised, the CCRA requires that the Minister for Climate Change Issues prepare a response (and present a copy of this report to the House of Representatives) if the Panel recommends any legislative change in relation to allocation. Only two of the Panel's recommendations relate to legislative change to allocation (the recommendations to change the 1.3% phase out rate).

ETS review: Focus and priorities for amendment to the CCRA in 2012

23. Given the need to prioritise, officials propose the February 2012 Cabinet paper focus on matters that require legislative change in 2012 and that Ministers have already identified as a priority for 2012 (e.g. extending the transitional arrangements and offsetting); and minor and technical amendments. More specifically officials propose that the February report-back covers:

A set of final and detailed policy proposals to modify the ETS

24. Issues Cabinet could take final decisions on in February 2012, including:

- Confirmation of objectives of the ETS; and how it relates to the Government's overall level of ambition to 2020.
- Areas where the Panel has consulted, the options are well defined and the regulatory impacts are well assessed, including:
 - the Panel's recommendations regarding the transition phase for sectors currently in the scheme; and
 - changes to the 1.3 percent phase out of allocation
- Technical or minor amendments (including a number not addressed by the Panel) where a high level of consultation would not be required, such as drafting or cross-referencing errors.

A set of preferred policy options for consultation in March/April 2012, with a view to making decisions on any resulting legislative amendments by May 2012

25. Areas where further consultation would be necessary in order to fully understand the issues and quantify the impacts of the proposed changes, including:

- The Panel's recommendations (and alternate options where agreed) where analysis is complete on the merits of the options but consultation may be required (because of limited consultation previously or because further information is needed to quantify the likely impacts), including:
 - Panel recommendations on offsetting for pre-1990 forests and a claw-back of the second tranche of pre-1990 forestry allocation
 - ETS treatment of the synthetic greenhouse gas sector
- Further analysis currently underway may lead officials to make additional recommendations for amendment. This work includes:
 - Withheld under Section 9(2)(g) This work will include consideration of: auctioning, operation of the scheme 'cap', carbon market availability and linking provisions (including any initial outputs from the Australia New Zealand Carbon Pricing Officials Group that might be made in relation to linking with the Australian scheme).
 - Follow-up on the Panel's recommendation to re-examine eligible emissions sources and treatment of recycled materials and biofuels.
- More substantive technical amendments where consultation is required or highly desirable, such as recommended amendments to the section 99 information sharing provisions in order to allow for more effective auditing of participants and review of the scheme.

26. Recommendations from the Agriculture ETS Advisory Committee first report where analysis is complete but consultation is required because of limited consultation previously or because further information is needed to quantify the likely impacts. This would include:

- excluding layer hens from the ETS;
- enabling DCDs to be included a removal activity in the ETS (noting that further analysis and consultation will be required on how to include DCDs as a removal activity through regulations).

27. In addition to these matters reported to Cabinet in February, officials believe it is possible that additional issues that have legislative implications will arise from the above and other work. These will need to be considered by Cabinet in May 2012, noting that if Cabinet approves further changes at this point there will not be time for consultation, other than through the select committee process.

Issue proposed not to be part of the legislative review in 2012

28. Given the need to prioritise, officials propose that the February Cabinet report back (and decision for legislative change in 2012) not include the following:

Issues being progressed on a longer time frame

29. A number of other ETS related policy areas will be progressed in 2012 but are not anticipated to be part of legislative amendment in 2012. These include:

- Response to a number of Panel's recommendations concerning small-scale farm/forestry operations, which officials propose to consider as part of the response to the Agriculture ETS Advisory Committee report in late 2012

- Policy work required for the response to the Afforestation Schemes Review, particularly as it relates to the ETS and linkages with Panel's recommendations on Māori participation, which will be coordinated with the wider response to the Panel recommendations and reported back to Ministers in March 2012.
- The matters addressed by the Panel that do not require legislative change and will be progressed within existing work programmes, including:
 - responding to the Panel's education and awareness recommendations;
 - accepting late applications for pre-1990 forest allocations and exemptions where there is justification for doing so; and
 - extending the availability of the tree weed exemption beyond 2012.

Panel's recommendation of averaging for post-1989 forests

30. The Panel's recommendation on averaging proposes one possible solution to two problems: (i) encouraging afforestation; and (ii) helping small foresters to manage their harvesting liabilities.
31. While averaging has some potential to assist with these problems, analysis done in 2009 shows that it also involves costs/risks and may not be the most cost effective mechanism to address these problems.
32. Averaging may nonetheless have some advantage in helping the Crown to manage its risk of picking-up the liability of forest owners who default on their harvesting liabilities. Whether this is the case requires further analysis about the post-1989 forest harvesting profile in 2020-2035 and implications for the Crown fiscal position from default risk.
33. Officials therefore recommend that averaging not be included as an option for legislative change in 2012 but that a broader approach is taken covering all of the related issues mentioned above. As it will not be possible to complete this analysis in time for the February report back, officials propose to respond in mid-2012

Panel's recommendations regarding agriculture (point of obligation, transitional arrangements, and allocation phase out rate)

34. Officials understand that Ministers do not propose to take decisions on the inclusion of agriculture in the scheme from 2015 as part of the 2012 amendments. Ministers have indicated they wish to progress amendments to exclude layer hens from the ETS and include DCDs as a removal activity, and there are a number of other Panel recommendations regarding agriculture that could either be progressed in 2012 or deferred until later.
35. Officials recommend that the Panel's recommendation on the point of obligation be considered as part of the existing work programme on this issue and that any response be coordinated with the response to the Agriculture ETS Advisory Committee, which is due to report on this issue in November 2012.
36. With regard to the Panel's recommendations on the introducing transitional arrangements from 2015 and a technical change to the 1.3 percent allocation phase out rates for agriculture, a decision is needed as whether to progress these changes as part of the 2012 legislative amendment or whether to defer them until a later date given that a review of agriculture's entry into the scheme has been foreshadowed for 2014. The change to allocation phase out rules is largely technical and aligns with the change proposed for other sectors. The introduction of transitional arrangements for agriculture,

however, is more substantive and Ministers may wish to consider this at a later time as part of the broader review of agriculture's entry into the scheme.

Areas officials propose not to progress

37. Officials propose that no further work is progressed on the Panel's recommendations on the Field Measurement Approach (FMA). Analysis on changing the 100ha threshold was undertaken when designing the FMA and indicated it would involve significant fiscal and compliance costs.

Full list of Panel recommendations

38. Appendix 1 contains a full list of the Panel's 61 recommendations with further detail on the timing of the Government's response in accordance with the priorities discussed above.

Risks created by not amending legislation in 2012

39. At the Minister for Climate Change Issues' request officials have also considered what risks could be posed to the effective functioning of the ETS if the Government decided not to pass legislation to amend the ETS next year or in the next parliamentary term.
40. Clearly it would not be possible to implement a number of the Panel's more significant recommendations without legislative change. For example, it is not possible to continue and phase out the current transitional arrangements without legislation meaning the transitional arrangements would expire at the end of 2012 as currently legislated.
41. Ministers have indicated that should they implement pre-1990 forest offsetting they may wish to claw-back some or all of the second-tranche of free allocation to pre-1990 forest owners. Forest owners expect to receive their second-tranche of free allocation in early 2013 and without amending legislation passed in 2012 or early 2013 it may not be possible to claw-back the second-tranche. Note that it would not be possible to do offsetting without legislative change in any case.

42.

Withheld under section 59(2)(j)

43. However, uncertainty about the nature of the international carbon market post 2012 may pose some risks. Participants in the NZ ETS will be at greater risk of price volatility should international emission unit supply decrease substantially. In addition it is also uncertain how or whether the export of units can occur after 2012, as NZUs are currently backed with AAUs issued under the Kyoto Protocol for the purposes of export.

Withheld under section 59(2)(j)

44.

Withheld under Section 59(2)(j)

45. Agencies involved with the administration of the ETS have identified a range of possible amendments to the CCRA that, while not required for the ETS to operate, would improve its operation. It will not be possible to make these improvements if there is no Amendment Bill in 2012, although the necessary amendments could be made at a later time. The most significant of these may pose some risk to the Government if they are not amended in 2012. These include:

- Section 99 restrictions on MfE and MED in relation to not allowing the sharing information regarding surrenders and allocations.
- Section 159 provisions relating to Crown liabilities following insolvency or non-payment. These provisions expose the crown to significant fiscal risks arising from companies that have either gone bankrupt/insolvent or have failed to meet their obligations.

46. In conclusion, officials have not been able to identify any significant issues that would prevent the operation of the ETS post 2012 (as currently legislated). But there are some potential risks in not amending legislation next year; the most significant of which arise from the uncertain international market. Officials are currently gathering information on the likely availability of international units post 2012 and assessing the issues that may be created. Key risks and options for managing them will be addressed in the February 2012 Cabinet paper.

Next steps

47. Subject to your agreement officials will continue to progress the priorities for the February 2012 report-back as outlined in this briefing. Given the timing of the election we propose to brief the Minister for Climate Change Issues and the Ministers of Agriculture and Forestry as early as possible after the election to seek a steer on the content of the February 2012 Cabinet paper.

Recommended Action

MAF and MfE recommend that you:

- a) **Note** that the ETS Review Panel provided the Minister for Climate Change Issues with its final report on 30 June 2011 and that the report contains 61 recommendations, some of which would require changes to legislation in 2012
- b) **Note** that on 18 July 2011 Cabinet invited the Minister for Climate Change Issues to report to Cabinet by February 2012 (through the relevant Cabinet committee) with proposed changes to the NZ ETS based on the Panel's recommendations, developments in and discussions with Australia and further analysis [Cab min (11) 27/15 refers]
- c) **Note** that officials believe that a number of the proposed changes to the ETS would require consultation early in 2012 in order to meet timeframes for the legislative process and therefore would need to be signalled in the Feb 2012 paper

- d) **Note** that because of the breadth and range of matters that could be considered as part of the project, the relatively tight timing if legislation is to be passed by the end of 2012, and available departmental resources, it is necessary to prioritise this work
- e) **Agree** that the February 2012 Cabinet paper covers matters that require legislative change in 2012 and that Ministers have already identified as a priority for 2012 (e.g. extending the transitional arrangements and offsetting); and minor and technical amendments

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- f) **Note** that, in general, officials propose to progress the more substantive recommendations that require legislative change for the February report-back, and to progress those non-legislative or more minor recommendations on a longer timeframe (with some exceptions outlined below)
- g) **Agree**, in relation to agriculture, that previous decisions on excluding layer hens from the ETS, and including DCDs as a removal activity in the ETS, be included in the February Cabinet paper with the intention of making any amendments to primary legislation in 2012

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- h) **Agree** that the issue of point of obligation for agriculture remain on the existing work programme of the Agriculture ETS Advisory Committee and its report on this be sent to Ministers in November 2012 as planned

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- i) **Agree** that the Panel's recommendation for a technical change to the 1.3 percent allocation phase out rate for agriculture be considered (alongside the same change recommended for other sectors) for legislative amendment in 2012

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- j) **Agree** with regard to the Panel's recommendation to extend transitional arrangements for agriculture from 2015, to:

EITHER

- a. Include this amendment for consideration in the February 2012 Cabinet paper
(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

OR

- b. defer the decision until a later date when final decisions are made about the entry of agriculture to the ETS

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- k) **Agree** that the Panel's recommendation to introduce averaging not be progressed for legislative amendment in 2012 and that a wider piece of work be commissioned and reported back to Ministers in mid-2012

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- l) **Agree** to the proposed approach to the Panels 61 recommendations as outlined in appendix one

(Minister Smith) Agreed / Not Agreed

(Minister Carter) Agreed / Not Agreed

- m) **Note** that while officials have not identified any significant issues that would prevent the operation of the ETS post 2012 (as currently legislated); some risks may be created not amending legislation next year. These include risks created by the uncertain international climate market, the inability to claw-back the second tranche of free allocation to pre-1990 forest owners and risks to operational efficiency.

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APPENDIX 1. THE PANEL'S RECOMMENDATIONS AND WHERE THEY ARE BEING CONSIDERED

Actioned prior to February 2012 Cabinet paper

<p>Forestry</p> <p>Rec 5.7: Pre-1990 allocations and exemptions</p> <p>The Government reviews applications for pre-1990 allocations and exemptions in November 2011 and considers whether there is a need to extend the current application timeframes.</p> <ul style="list-style-type: none"> • No legislative change required, as Ministers have agreed that MAF will accept late applications for forestry allocations and exemptions where justification exists [MAF B10-503 refers].
<p>Maori</p> <p>Rec 6.4: Extensions to deadlines for Māori owners</p> <p>The Government should explore whether temporary extensions to the exemption and allocation deadlines for Māori owners are necessary, while these issues are being addressed.</p> <ul style="list-style-type: none"> • [As per Rec 5.7] No legislative change required, as Ministers have agreed that MAF will accept late applications for forestry allocations and exemptions where justification exists [MAF B10-503 refers].
<p>ETS Operation</p> <p>Rec 9.6: Consider HFC CER risks</p> <p>The Government should urgently consider whether HFC CERs pose a significant risk and whether a time limit should be imposed on their eligibility.</p> <ul style="list-style-type: none"> • Cabinet has already decided to consult on banning HFC CERs (and N₂O CERs) from industrial gas destruction projects with a view to banning them from 1 January 2012 or 2013. The consultation document has been published.

To be Addressed through Legislative Amendments in 2012 (February 2012 Cabinet Paper)

<p>Transition measures</p> <p>Rec 3.1 and 3.4: Price Cap</p> <p>The price cap should be retained after 2012, but should increase by \$5 per annum from 2013 to 2017, starting at \$30 per NZU in 2013 and reaching \$50 per NZU in 2017 (Rec 3.1).</p> <p>The price cap should be available to all the new sectors entering the scheme after 2012, including the agriculture, synthetic greenhouse gases and waste sectors (Rec 3.4).</p> <ul style="list-style-type: none"> • Being assessed against status quo and other options for the Feb 2012 Cabinet paper.
<p>Rec 3.3 and 3.5: Scaling up to Full Obligation</p> <p>For the liquid fossil fuels, stationary energy and industrial processes sectors, the one-for-two surrender obligation should scale up to a full surrender obligation progressively from 2013 to 2015, increasing at equal intervals per annum, that is to 67 per cent in 2013, 83 per cent in 2014, and 100 per cent in 2015 (rounded to the nearest percentage).</p>

Participants in the synthetic greenhouse gases and waste sectors should have access to a 67 per cent obligation in 2013 and an 83 per cent obligation in 2014, and should assume full surrender obligation from 2015 (3.5)

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 3.7: Ban on export of NZUs

The ban on NZU exports from non-forestry sectors should be removed when the price cap is removed, or sooner if the price cap is significantly above the international carbon price (and hence the risk of arbitrage is minimal).

- **This will be considered as part of the work on the wider post 2012 issues and reported in the Feb 2012 Cabinet paper.**

Rec 3.11: Eligible Emission Sources

The Government further examines the potential inclusion of additional eligible emission sources for determining eligibility and allocative baselines under the Act.

- **Further analysis and recommendations will be provided in the Feb 2012 Cabinet paper.**

Rec 3.12: Recycled Materials

The Government further examines the potential inclusion of fossil fuel proxies for biofuels and new material proxies for recycled materials as eligible emission sources for determining eligibility under the Act.

- **Further analysis and recommendations will be provided in the Feb 2012 Cabinet paper.**

Rec 3.13: Phase-out rate

The current phase-out rate of 1.3 per cent per annum of the previous year's allocation should be revised to an annual reduction of 1.3 percentage points, to clarify the exact phase-out rate and the year in which the free allocation of NZUs will cease.

- **To be included in Feb 2012 Cab paper; little further analysis required**

Rec 3.14: Allocation for new eligible activities

The Government gives consideration to the risks associated with the potential for new, emissions-intensive activities to significantly expand the volume of allocation, and options to mitigate these risks.

- **Further analysis and recommendations will be provided in the Feb 2012 Cabinet paper.**

Rec 3.15 Allocation cap

The potential introduction of an allocation cap should be further considered in the next ETS review.

- **Whilst the review recommended deferring this work until 2017, officials plan to consider this in the context of wider matters relating to the post 2012 period (in connection with the operation of the "true up mechanism" in Section 86(f) of the Act).**

Agriculture

Rec 4.3: Agriculture allocation phase-out rate

The free allocation of NZUs for agriculture should be 90 per cent of a baseline initially, phased out at 1.3 per cent per annum on a straight-line basis from 2016.

- **Decision required whether to progress this in 2012 or later. As this recommendation is aligned to that for other sectors (rec 3.13) and does not have significant impacts in the**

short-term, officials recommend progressing in February 2012.

Forestry

Rec 5.4 and 5.5: Offsetting

Subject to recommendation 5.1, pre-1990 forestry offset planting should be introduced within the rules for pre-1990 forestry from 2012 (Rec 5.4).

The Government should introduce a claw-back provision for the second tranche of the pre-1990 forestry allocation, if offset planting is introduced into the ETS (as recommended by the Panel – see recommendation 5.4) and taken up by a participant (Rec 5.5).

- **Requires legislative change, so work underway now for Cabinet policy decisions in February 2012.**

Synthetic Greenhouse Gases

Rec 7.1: SGG point of obligation

The point of obligation under the ETS should be on users of SF6 in electrical switchgear rather than importers of SF6.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.2: Electrical switchgear obligation

The ETS obligation of users of SF6 in electrical switchgear should be based on estimates of actual emissions.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.3: SF6 present at disposal

The Government should consider the treatment of SF6 contained within equipment and still remaining upon disposal.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.4: Bulk imports of SF6

No changes should be made to the current ETS framework for bulk imports of non-SF6 synthetic greenhouse gases.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.5: SGG import levy

A levy, equivalent to the market price of emission units and reflecting the transition phase arrangements, should be placed on imported goods containing synthetic greenhouse gases which are not for personal use and that the current exemption for small importers of motor vehicles should be removed.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.6: Levy administration

The Government should ensure such a levy is administratively simple for importers while minimising competitive distortions with New Zealand manufacturers.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 7.8: Prohibit SGG release

The Government should prohibit knowingly releasing synthetic greenhouse gases into the atmosphere.

- **Advice will be included in the Feb 2012 Cabinet paper.**

Waste

Rec 8.1: Discretionary landfill exemptions

The Government should introduce a discretionary power to exempt landfills from obligations under the ETS that are (i) geographically isolated, (ii) have a low volume of waste disposed of, and (iii) do not have alternative disposal options.

- **Being assessed against status quo and other options for the Feb 2012 Cabinet paper.**

Rec 8.2: Landfill size criteria

The Government works with Local Government New Zealand to define criteria relating to landfill size.

- **Being further assessed and defined for the Feb 2012 Cabinet paper.**

ETS Operation

Rec 9.1: Retain current ETS administration

No changes should be made at this stage in relation to the administration of the ETS across government.

- **The Panel recommends maintaining the status quo in relation to the administration of the ETS. Operational agencies have identified a number of technical issues (mostly of a minor nature) we propose to progress in Feb 2012 Cabinet paper.**

Rec 9.3: Registry security

The security of the ETS register should be subject to periodic assessment/review (9.3)

- **Officials will include consideration of legislative changes proposed by the registry to further protect the security of the register for inclusion in the February Cabinet paper.**

To be addressed over a longer timeframe

Transition Measures

Rec 3.2: Price cap after 2017

The next review of the ETS should consider whether a price cap is needed after 2017.

- **Whilst the review recommend deferring this work until 2017 officials plan to consider this in work related to linking with the proposed Australian carbon pricing scheme.**

Rec 3.8: Price Floor

An ETS price floor should not be introduced.

- **The issue of a price floor will need to be reconsidered in the context of possible linking with the proposed Australian carbon pricing scheme.**

Rec 3.6: Agriculture one-for-two surrender obligation

Participants in the agriculture sector should have a one-for-two surrender obligation in 2015 and 2016,

a 67 per cent obligation in 2017, and an 83 per cent obligation in 2018, and should assume full surrender obligation from 2019.

- **Decision required whether to progress this in 2012 or later.**

Agriculture

Rec 4.1: Agriculture in the ETS

Agriculture remains within the ETS on the timetable that is currently legislated, with mandatory reporting beginning in 2012 and surrender obligations beginning in 2015.

- **No proposal to re-assess this question in 2012, noting however that Ministers have indicated that they will revisit this question in 2014 before agriculture fully enters the scheme.**

Rec 4.2: Farmer point of obligation

The point of obligation for agriculture should be at the farmer level rather than the processor level.

- **Ministers have already indicated they wish the Agricultural ETS Advisory Committee to explore the practicality of moving the point-of-obligation to the farm level, which it is doing and will report by November 2012.**
- **Response to this recommendation will not be progressed as part of Feb 2012 report-back but will be reported to Ministers in December 2012.**

Forestry

Rec 5.2: Associated Persons' Test

The forest ownership associated persons' test rules should be reviewed to determine whether the associated persons' percentage thresholds should be increased or varied to recognise the situation of related family farming operations.

- **As this primarily concerns small-scale farm/forestry operations, the response will be in December 2012 and co-ordinated with work on related farm/forestry issues.**

Rec 5.3: Income Tax Act 2007

The Government should undertake further study on the amalgamation of smaller forestry blocks and the application of section CB25 of the Income Tax Act 2007.

- **As this primarily concerns small-scale farm/forestry operations, and no legislative change is necessary in 2012, the response will be in December 2012 and co-ordinated with work on related farm/forestry issues. (Note also that this issue affects forestry beyond the climate change context.)**

Rec 5.9: Accounting of post-1989 forest contingent liabilities

The Government should ask the International Accounting Standards Board and the soon-to-be-established New Zealand External Reporting Board to look into the treatment of post-1989 forest actual and contingent liabilities (of future harvesting) in financial accounts.

- **No requirement for Cabinet decision in February 2012. Propose to progress over 2012.**

Rec 5.10: Harvested wood products

Subject to recommendation 5.1, the ETS rules in relation to post-1989 harvested wood products should be modified to reflect an 'emissions to atmosphere' approach if agreement on this has been reached internationally.

- **MAF has initiated work to assess the impact of an 'emissions to atmosphere'/HWP rule. The international rule will not be known by February 2012, so response mid-to-late 2012 depending on progress of international negotiations.**

Rec 5.11: Averaging

Averaging should be available as an option from 2012 for post-1989 forests. The Government should consider whether a ceiling on the maximum size of forest that could participate in this option would be required (Rec 5.11)

- **Proposed not to be addressed in February 2012 report-back but later in 2012 as part of the work programme focussing on the post-1989 forest harvesting profile in 2020-2035 and implications for the Crown fiscal position from default risk.**

Rec 5.12: Self-insurance for post-1989 forests

The Government gives consideration to, and consults on the establishment of, a self-insurance pool of units for post-1989 forests, along the lines of that proposed in Australia (5 per cent retention). Such a scheme would have no recourse to the Government and should not result in any further liabilities to the Government.

- **As this primarily concerns small-scale farm/forestry operations, the response will be in December 2012 along with response to the Agriculture ETS Advisory Committee.**

Rec 5.15: Tree weed exemption

The pre-1990 tree weed exemption should be available beyond 2012.

- **This raises a question about the possible use of current tree weed allocation after 2012, which would require a Cabinet decision. It does not require legislative change, however, so a decision will be sought later in 2012.**

Rec 5.16: Voluntary ETS for pre-1990 indigenous forests

The Government should consider the appropriateness and means of introducing a voluntary ETS equivalent for pre-1990 indigenous forests.

- **No report-back in February 2012, but could be revisited later in 2012 if Ministers wish.**

Māori

Rec 6.2: Afforestation schemes

The Government continues, and considers strengthening, the existing afforestation schemes to encourage greater Māori participation in respect of post-1989 forests and to take into account the particular issues faced by Māori.

- **A response to this recommendation will form part of the response to the Afforestation Schemes Review due in March 2012.**

Rec 6.3: Application requirements for Māori land

The Government develops amendments to the Act that address the application requirements that affect Māori land, including:

- reducing the application requirements for Māori freehold land in multiple ownership or owned by trustees of Māori trusts
- ensuring the Māori Trustee can apply for the 50-hectare exemption on the basis of individual Māori trusts' ownership rather than on the basis of its total landholding.

- Ministers have already agreed to examine this issue further in 2013 in light of the volume of Māori-owned pre-1990 forest land that did not gain an exemption or allocation [MAF B10-503 refers].

Synthetic Greenhouse Gases

Rec 7.7: Recycle levy revenue

The Government should recycle a proportion of the levy revenue into industry-led initiatives which will reduce synthetic greenhouse gases emissions

- This recommendation is dependent on the government agreeing to a levy based approach. Further advice therefore will be provided on this after initial decisions have been made in Feb 2012.

Review Process

Rec 1.1: Consider issues in submissions

The Government considers those issues raised during the Panel's consultation which it has not been able to reach a recommendation on using the *Summary of Submissions* as a starting point.

- Each workstream lead will review the summary of submissions (and individuals submissions if necessary) to ensure all substantive issues have been considered.

To be Addressed through Current Work Programme (legislative amendments not required)

International context

Rec 2.1: Develop carbon markets

The Government continues to accord priority in international negotiations, as well as in wider bilateral and regional engagements, to the development of international carbon markets generally, and specifically to ensure New Zealand has the ability to sell NZUs and buy international emission units

- MFE continues to promote the development of international carbon markets through the UNFCCC international negotiation process.

Withheld under Section 56(a)

A working group of senior officials from New Zealand and Australia has been established to explore how the New Zealand and proposed Australian emissions trading schemes could be linked. New Zealand continues to engage with our countries planning to introduce emission trading schemes with a view to linking with these schemes through other fora, such as the bilateral agreements and the World Banks' Partnership for Market Readiness.

Rec 2.2: Monitor Australian developments

The Government continues to monitor the development of the carbon pricing mechanism in Australia and that, while it is desirable for the New Zealand and Australian schemes to work broadly in harmony, we should not be bound by the features of any particular overseas scheme.

- MFE officials are in regular contact with their Australian counterparts to monitor development of their proposed scheme. In addition, a working group of senior officials from New Zealand and Australia has been established to explore how the two schemes could be linked.

Agriculture

Rec 4.4: Technology transfer

To support farmers within the ETS, the Government and industry should continue to focus on technology transfer for existing mitigation options and the development of future options and tools to reduce emissions.

- **MAF has three programmes of work running over the next three years to:**
 - **Develop resources and tools to assist farmers to reduce GHG emissions;**
 - **Upskill rural professionals on climate change issues; and**
 - **Demonstrate the integration of mitigation options through workshops and field-days with farmers and growers in the sheep & beef, arable & vegetable, forestry, kiwifruit, and pork sectors.**

Forestry

Rec 5.1: Hard Headed Assessment

The Government should make a hard-headed assessment of the Panel's recommended changes to the domestic ETS forestry rules after 2012, taking account of the international position, the potential fiscal impact/risk and financial impact/benefit to foresters and other stakeholders, with a view to changing the ETS forestry rules along the lines recommended, if necessary unilaterally.

- **This will occur as part of the response to the other recommendations.**

Rec 5.7: Pre-1990 allocations and exemptions

The Government reviews applications for pre-1990 allocations and exemptions in November 2011 and considers whether there is a need to extend the current application timeframes.

- **No legislative change required and Ministers have already agreed that MAF will accept late applications for forestry allocations and exemptions where justification exists [MAF B10-503 refers].**

5.8 Promote understanding of forest liabilities

The Government continues to promote understanding within the forestry and land-use sectors about post-1989 harvesting liabilities and options for managing these.

- **MAF has extensively promoted understanding of post-1989 harvesting liabilities and options for managing these through a nation-wide series of seminars in 2010 that explicitly addressed these issues. On-going promotion of understanding is achieved through the regional network of MAF programme advisers who provide information to existing and potential participants. These advisers regularly provide information to, and address meetings of, service providers such as forestry consultants, legal and accounting firms on post-1989 ETS issues.**

Māori

Rec 6.1: Complementary measures

The continuation of complementary measures such as the home insulation programme in order to mitigate the impacts on vulnerable households, including Māori.

- **This recommendation will be referred to the relevant agencies**

Rec 6.5: Māori Trustee

The Government should establish a working group to work with the Māori Trustee to address the application requirement issues, as suggested by the Māori Trustee.

- **MAF has been working with TPK and the Māori Land Court since 2010 to identify Māori owned properties in order to provide targeted assistance and information. It has also engaged with the Māori Trustee Office to identify and resolve issues, provide assistance in identifying properties with forests, and advise on applications.**

Rec 6.6: Support Māori land trust capacity

The Government should monitor the level of engagement and capacity of Māori land trusts in relation to the ETS and consider ways to provide support where appropriate.

- **MAF continues to work with TPK, the Māori Land Court, and the Māori Trustee Office to identify and resolve issues and provide information about ETS requirements, including application requirements.**

ETS Operation

Rec 9.4: Education

The Government should consider what further education resources could be provided to enhance current levels of understanding of the ETS (9.4).

- **Being progressed over 2012 – does not have legislative implications and will not be specifically addressed in the Feb 2012 Cabinet paper.**

Continuation of Status Quo, or No Response Proposed

Transition Measures

Rec 3.9: Allocation Thresholds

The existing allocation thresholds of 90 per cent allocation for highly emissions-intensive activities and 60 per cent allocation for moderately emissions-intensive activities should be maintained.

- **The Panel recommends maintaining the status quo in relation to allocation thresholds. Initial analysis suggests that there is no significant issue with the allocation thresholds. Therefore, officials do not propose to undertake any significant new analysis on allocation thresholds for the February 2012 Cabinet paper.**

Rec 3.10: Value-added test

A value-added test for determining eligibility for industrial allocation should not be introduced.

- **The Panel recommends maintaining the status quo in relation to the value-added tests. Initial analysis suggests that there is no significant issue with this. Therefore, officials do not propose to undertake any significant new analysis on the value-added test, for the February 2012 Cabinet paper.**

Forestry

Rec 5.13: Field measurement option

The Panel recommends that owners of less than 100 hectares of forest have the option, at their cost, of undertaking actual measurement.

- **Analysis of this question was undertaken when designing the Field Measurement Approach and indicates it would involve significant fiscal and compliance costs. It is proposed not to revisit the question now, although it can be considered in the next**

NZ ETS review.

Rec 5.14: 100-hectare threshold

The Panel recommends that the Government consider whether the 100-hectare [FMA] threshold should be increased.

- Analysis of this question was undertaken when designing the Field Measurement Approach and indicates it would involve significant fiscal and compliance costs. It is proposed not to revisit the question now, although it can be considered in the next NZ ETS review.

Rec 5.6: Two-hectare pre-1990 deforestation threshold

There should be no changes to the two-hectare pre-1990 deforestation threshold.

- The Panel recommends maintaining the status quo; initial analysis suggests that there is no significant issue with this, therefore, it will not be progressed in the Feb 2012 Cabinet paper.

ETS Operation

Rec 9.2: Penalties in Act

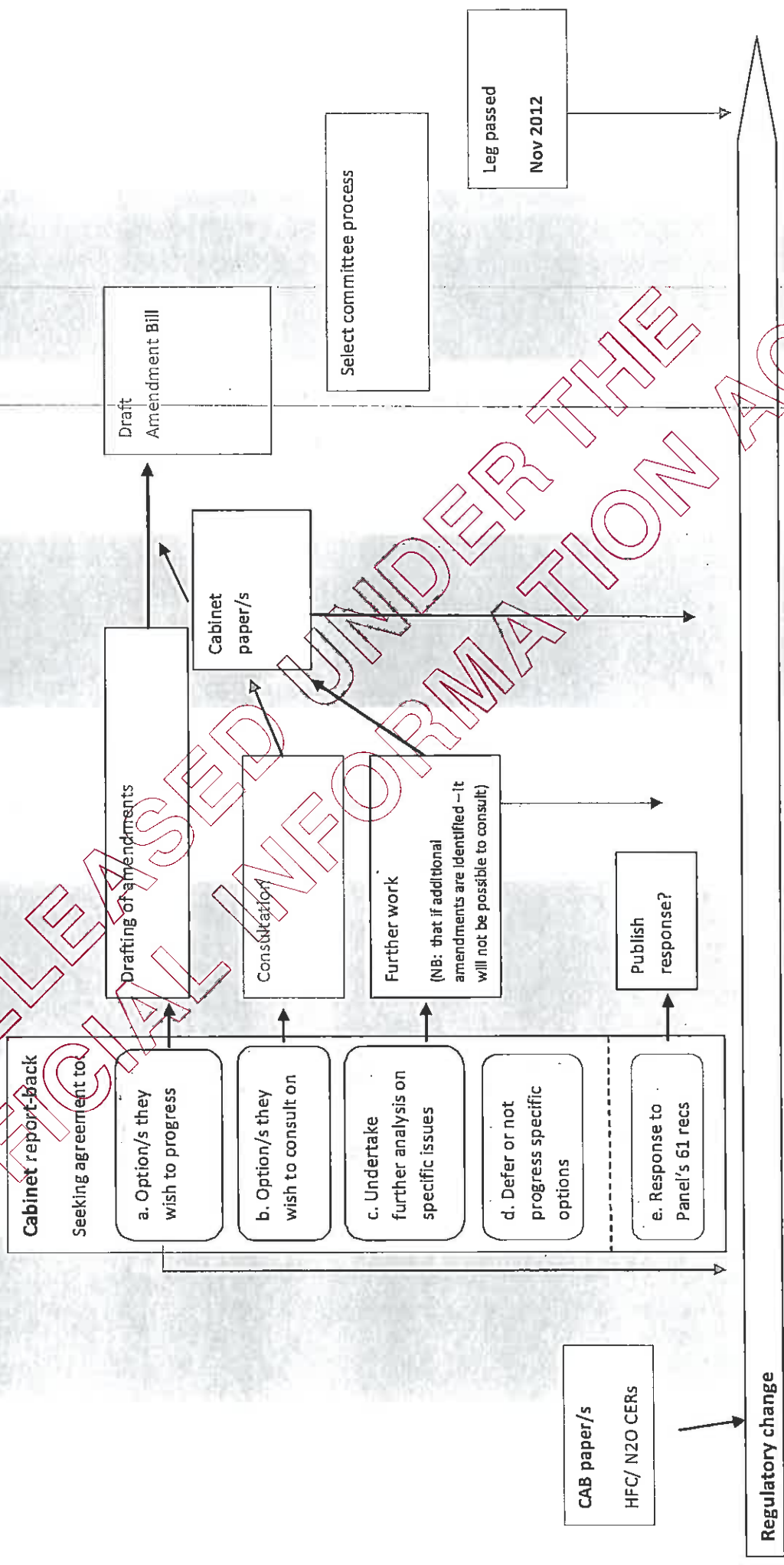
No changes should be made at this stage to the penalties in the Act.

- The Panel recommends maintaining the status quo; initial analysis suggests that there is no significant issue with this. Therefore, in the Feb 2012 Cabinet paper, there will not be any significant advice on the penalties in the Act.

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APPENDIX 2 – ETS Review Project Timeline 2011/12

SEP -DEC JAN FEB MAR APR MAY JUNE JULY AUG - DEC



Operational change

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