



Joint Briefing: Options for providing point of obligation transition for the agriculture sector

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Action Sought

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Minister for Climate Change Issues Hon Dr Nick Smith	Confirm your preferences on options set out in this briefing.	2 June 2009
Minister of Agriculture and Forestry Hon David Carter	Confirm your preferences on options set out in this briefing.	2 June 2009
Associate Minister of Climate Change Hon Tim Groser	Note	None

Contact for Telephone Discussion (if required)

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Background

Officials have been working to give effect to your preferred option of providing maximum flexibility in the entry dates for agriculture in the NZ ETS amendment Bill [briefing 09-B-01409 refers].

Ministers subsequently requested the ability for the Government to set the point of obligation at the processor level initially and transition to the farm level later. In designing this additional level of flexibility, it has become clear that there is range of options; each with its own nuance. This brief outlines these options and requests your guidance.

We think there are two main options for you to achieve the desired flexibility. These are:

Option 1 - Default processor point of obligation with transition to farm level; or
Option 2 - Government can choose either processor or farm level

Both of these options could be tailored to include:

- Decision criteria for making a point of obligation decision; and/or
- Intermediate steps to stage the transition to farm level; and/or
- The ability to reverse the farm level point of obligation decision.

Analysis

Option 1 – Default processor point of obligation initially with transition to farm level

Under this option Government would set the reporting dates by OIC, but the point of obligation would default to the processor at the outset. This reflects the current situation where the Government does not need to make an active decision about the point of obligation. Once the reporting dates are set, the point of obligation is processor level unless the government overrides it. Mandatory reporting periods must be at least one year but could continue for as long as desired. When the Government saw fit, it could make another OIC to begin surrender obligations.

A further OIC would be required to begin reporting at the farm level. The government would have to make an OIC for surrender obligations to begin at farm level.

In the example below, the Government made an OIC in 2014 to begin reporting at farm level in 2016. As shown, the processors continue to surrender units during the farm level reporting years to create continuity. The obligation to surrender units would only switch from processor to farmer once the Government made an OIC. In principle, the situation could exist where farmers are reporting indefinitely, while processors are surrendering. The benefit of this is that it would allow any reporting issues at farm level to be resolved before the obligation to surrender actually moves.

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Processor (default)	Make Reporting Date OIC ¹		Voluntary reporting	Mandatory Reporting Make OIC for surrender	Surrender obligations accrue	Surrender	Surrender	Surrender	
Farmer					Make Point of Obligation OIC		Voluntary reporting	Mandatory Reporting Make OIC for surrender	Surrender

Option 2 - Government can choose either processor or farm level

This option is similar to that above, but the Government would initially need to choose either farm level or processor level obligation. There would be no presumption of where the point of obligation lies from the outset. If processor was chosen initially, then at any time after that the Government could pass an OIC to begin reporting at farm level. A further OIC would be required to switch the obligation to surrender units from processor to farmer.

In the example below the Government has chosen a processor level obligation from the outset (illustrated by the arrow) and later switched to the farm level. Surrender obligations would continue for the processor until another OIC was passed to move the surrender obligations to the farm.

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Processor	↑		Voluntary reporting	Mandatory Reporting Make OIC for surrender	Surrender obligations accrue	Surrender	Surrender	Surrender	
	Make Point of Obligation OIC				Make Point of Obligation OIC				
Farmer					↓		Voluntary reporting	Mandatory Reporting Make OIC for surrender	Surrender

Both Option 1 and Option 2 will result in complex legislation, but option 2 is somewhat less complex. Also, legal advice is that the provisions above are very unusual and likely to be criticised for their wide ranging executive powers.

¹ Note that depending on when in the calendar year the Government made an Order in Council to begin reporting, the delay before the sector began voluntary reporting could be between 12 and 23 months. This is because the ETS runs on a calendar year.

Possible additional considerations:

Decision criteria for making a point of obligation decision

Officials believe that a useful addition to the options above would be to specify certain criteria that the Minister must consider before making an OIC for the point of obligation. The criteria the Minister might have regard to might include:

- The ability to verify information in emission returns;
- The costs including administrative and compliance costs
- The availability of farm specific mitigation options

These criteria would help ensure a robust decision although it also increases legal risk of judicial review if the Minister has incorrectly applied the criteria. On balance, we think including these criteria in the Act would assist in demonstrating the government's commitment to working towards the implementation of a farm level point of obligation. Also, MAF considers that if the sector is committed to a farm level point of obligation as its preference, the criteria may motivate the sector to help resolve verification issues that exist with a farm level obligation.

Intermediate steps

Moving to a farm level point of obligation will create significant administrative challenges because of the sheer number of participants that must be registered. These challenges will occur regardless of the lead-in time. We therefore think that another useful addition would be to provide the Government with broad powers to stage the transition to the farm level.

A staged approach might involve, for example, beginning reporting obligations for one sector at a time or by size of farm. A staged approach would smooth the registration process. It is likely to work for the reporting years, but is not likely to work well for surrender obligations.

Ability to reverse the farm level Point of Obligation decision

There are likely to be unforeseen issues involved in a farm level point of obligation. It may therefore be useful to draft the legislation so that a Minister can reverse a decision to move to a farm level obligation. However, a negative impact of this option is that the ability to reverse the decision adds a further layer of uncertainty in respect of the agriculture sector.

Further legislative amendments are likely to be required for a farm level obligation

The options above will provide Ministers with the maximum flexibility for agriculture in terms of the point of obligation. However, it is important to note that further legislative amendments are likely to be required to allow a farm level point of obligation to function properly. For example, the agTAG determined that the participant should be the farmer landowner rather than livestock owners who are the current participants under the Act.

Alignment of sectoral treatment

Both the options above involve stripping all the entry dates from the Act for agriculture. This is different from the other sectors where the reporting dates will remain. There is a risk that this could be viewed as differential treatment for agriculture, or even a move away from inclusion of the agriculture sector in the NZ ETS. This may impose communications risks.

If Ministers were concerned about this, there is an option to provide flexibility for the entry date (the surrender date), but to move the decision date and the reporting years out by say two years. The farm-

level transition provision could also be provided. This would allow a similar level of flexibility as other sectors in the NZ ETS, although the entry of agriculture would be delayed until 2015 at the earliest. A two year delay would have an approximate fiscal impact of \$300m. This approach could also lead to a situation where processors end up mandatory reporting for some extended period of time, but the agTAG analysis indicates that this is relatively inexpensive.

Recommendations:

We recommend that you:

1. Include in the Climate Change Response (Emissions Trading Sector Entry) Amendment Bill (officials' preference shown in bold):

Option	Ministers' preference
a. Option 1 - Processor point of obligation as initial default with ability to transition to farm level;	Yes / No
OR	
Option 2 - Government can choose either processor or farm level initially and, if processor is chosen, transition to the farm level later.	Yes / No
b. That the Bill specify certain criteria that the Minister must have regard to before making an Order in Council for the point of obligation;	Yes / No
c. Assuming your preference is to include criteria in the Bill as outlined above in b, for the following criteria to be used:	
d.	Yes / No
i. The ability to verify information in emission returns;	
ii. The costs including administrative and compliance costs;	Yes / No
iii. The availability of farm specific mitigation options	Yes / No
e. That the Bill include broad powers to stage the transition to the farm level;	Yes / No
f. That Bill allow a Minister to reverse a decision to move to a farm level obligation;	Yes / No

2. Note that additional legislative amendments are likely to be required for a farm level obligation to function properly;

Noted

3. Note that there is a risk that Options 1 and 2 could be perceived as differential treatment for the agriculture sector, or even a move away from inclusion of the agriculture sector in the NZ ETS;

Noted

4. Note that a further option for setting the point of obligation and reporting dates would be to move the decision date and reporting years by a fixed period of time. This option would align treatment of the agriculture sector more closely with other sectors but it would delay entry dates for the agriculture sector and have associated fiscal implications.

Noted

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