

Climate Change: A Three Stage Process for Developing and Implementing Negotiated Greenhouse Agreements with Industry

Attached is the Minute of decisions made by the Cabinet Policy Committee on recommendations for the Negotiated Greenhouse Agreement (“NGA”) process, and the paper submitted for the Cabinet Policy Committee’s consideration on 4 April 2001.

Please note that the original recommendations in the paper were amended as reflected in the Minute. This amendment allows flexibility for the generic NGA and Heads of Agreement to proceed in parallel, rather than sequentially. These changes were prompted by signals from some industry participants that they desired to focus on Heads of Agreement sooner rather than later in the process. The paper has been released in full, even though the revised approach, with the initial emphasis on Heads of Agreement, is not reflected in the paper itself or the attached draft generic agreement.

The draft generic NGA and the outline of matters that may be included in a Heads of Agreement (annex 1 to the attachment) have largely been overtaken by developments. In addition, the Government is receiving ongoing legal advice about how its commitments under NGAs and Heads of Agreement can be given effect and their legal form. Therefore the draft generic NGA and the outline of matters for a Heads of Agreement are not practical starting points for negotiations. For these reasons, the paper is released without prejudice to negotiations. To facilitate further discussions, the Government will provide an updated outline Heads of Agreement to prospective NGA partners.



Cabinet Policy Committee

POL Min (01) 7/3

Copy No:

Minute of Decision

This document contains information for the New Zealand Cabinet. It must be treated in confidence and handled in accordance with any security classification, or other endorsement. The information can only be released, including under the Official Information Act 1982, by persons with the appropriate authority.

Climate Change: A Three Stage Process for Developing and Implementing Negotiated Greenhouse Agreements with Industry

On 4 April 2001 the Cabinet Policy Committee:

1. **noted** that in July 2000 Cabinet agreed that:

“... in order to facilitate consultation, particularly in enhanced industry agreements, that emitters should be informed by officials that actions taken by emitters under any pre-2008 price measure implemented by the government will not disadvantage them for the allocation of any units for a post-2008 domestic emissions trading system (or any other post-2008 price measure)...”

[CAB (00) M 25/4C]

2. **noted** that in January 2001 Cabinet:

“agreed in principle, subject to the outcomes of formal consultation on the Government’s overall climate change policy package, that Negotiated Greenhouse Agreements form part of the pre-2008 policy package, which in total will aim to encourage firms, households and communities to reduce their greenhouse gas emissions in the period prior to 2008”...

“directed officials to report to the Committee with a recommended draft generic NGA”

[CBC Min (01) 3/4]

Three Stage Process for Negotiated Greenhouse Agreements

3. **agreed** to a three-stage process for developing negotiated greenhouse agreements (NGAs) incorporating:

- development of a generic framework (incorporating common assumptions and methodologies);
 - a heads-of-agreement stage (incorporating an intention to proceed and agree on information collection and sharing and NGA structure); and
 - final completion of the agreement with explicit targets (once the legal status of NGAs is confirmed);
4. **noted** that the stages in paragraphs 3.1 and 3.2 may proceed in parallel;

Developing a generic NGA framework

5. **noted** that the generic NGA attached to POL (01) 27 was developed by officials utilising input from earlier consultations and material subsequently provided by the Greenhouse Policy Coalition (GPC);
6. **noted** that the GPC is independently developing legislative recommendations and a draft agreement for the consideration of Ministers and officials;
7. **directed** officials from departments participating in the pre-2008 working group to consult with potential NGA participants using the draft generic agreement outlined in the attachment to POL (01) 27;
8. **directed** officials to refine the generic framework, taking into account feedback received, with as many common assumptions and methodologies as possible and to report back to the Ministerial Group on Climate Change by 31 July 2001;
9. **authorised** the Ministerial Group on Climate Change to finalise the generic framework agreement;

Heads-of-agreement NGAs

10. **noted** that heads-of-agreement are intended to provide a common understanding between Government and Industry participants on the content and process for negotiating an NGA;
11. **agreed** that the Convenor, Ministerial Group on Climate Change, in consultation with other Ministers on the Group, be delegated authority to negotiate draft heads-of-agreement with firms or collective groups of firms;
12. **invited** the Convenor, Ministerial Group on Climate Change to report back to the Cabinet Policy Committee on the proposed heads-of-agreement, prior to their signature;

Completing negotiations of NGAs

13. **noted** that the Convenor, Ministerial Group on Climate Change will be making recommendations on the timing and process for initiating negotiations for concluding NGAs, once the process identified in the heads-of-agreement has been established;

Other matters

14. **noted** that work is progressing on carbon charge impacts and revenue recycling options; and
15. **noted** that a previous reporting directive concerning public education and communication will be the subject of a separate paper shortly [CBC Min (01) 3/4].

Chair

Cabinet Policy Committee

CLIMATE CHANGE: PRE-2008 CROSS-SECTORAL AND PRICE MEASURES

Executive Summary

This paper seeks Cabinet's agreement to a three-stage process for developing and implementing negotiated greenhouse agreements (NGAs) with industry. The three-stage process is proposed as a means of enabling prompt completion of NGAs once their relationship to other policy options is clarified in the ratification legislation likely to be introduced into Parliament early in 2002. Certainty of regulatory framework is an issue of high importance to industry. The three stages involve a period of consultation with industry plus analysis to confirm a generic agreement framework, a heads-of-agreement stage and finally completion of an agreement.

Context

1. Negotiated Greenhouse Agreements (NGAs) are proposed agreements between Government and industry that will set greenhouse gas emissions limits for industry participants until 2008, when New Zealand will have binding emissions reduction commitments if it ratifies the Kyoto Protocol. NGAs are intended to follow on from and extend the existing Voluntary Agreement programme between Government and a number of major industrial emitters.
2. The Climate Change: Pre-2008 Cross-Sectoral and Price Measures paper considered by the Cabinet Business Committee on 31 January 2001 included consideration of a range of policy options [ref. POL (00) 217]. These included objectives for decisions on pre-2008 measures, feedback from early consultations concerning negotiated greenhouse agreements (NGAs), the need for a pre-2008 element in the proposed communication and consultation package, plus work related to use of a carbon charge, non-price measures and pilot emission trading.
3. At that meeting Cabinet agreed in principle that NGAs would form part of the pre-2008 policy package, subject to consultation on the Government's overall climate change policy package [ref. CBC Min (01) 3/4]. It was also noted that it might not be practical to develop NGAs in some sectors or with smaller industrial emitters. Officials were directed to prepare a recommended draft generic NGA covering key design issues and report to the Cabinet Policy Committee (POL) in March 2001. Officials were also directed to consult with potential NGA participants while developing the draft generic NGA.

Proposal

4. This paper reports progress on developing a generic NGA and seeks approval for a 3-step process to develop and implement NGAs via further consultation with potential participants, including joint working groups to advance methodological and technical matters. Approval is also sought for the Ministerial Group on Climate Change, once it has approved the generic NGA framework, to approve negotiation of heads-of-agreement for individual NGAs. Other (non-NGA) matters considered on 31 January are either reported on briefly in this paper or included in a separate paper on public education and communication.

Industry focus on a legislated framework for NGAs

5. It was clear from the October 2000 second industry consultation and subsequent views expressed by the Greenhouse Policy Coalition (GPC) at their November 2000 seminar (and via direct Ministerial contacts) that having a legislative framework is seen as a precursor to development of NGAs. The Climate Change Steering Group are presently considering and will soon advise Ministers concerning the scope and timeline of the legislative requirements for the ratification of the Kyoto Protocol.

The proposed three-stage NGA process

6. Delaying NGA development until the legislative and incentive frameworks are in place potentially reduces their usefulness as a measure to manage emissions. This delay can be minimised by breaking the process into discrete steps and proceeding promptly with those that are technically based. The following three-stage process is suggested.

Confirming a generic NGA

7. A draft generic NGA is included as an attachment to this report and includes drafting comments that will be removed following a process of consultation and analysis. It was developed by officials and incorporates feedback from the earlier industry consultations and material subsequently provided by the GPC. The GPC and other potential industry partners will also have considered what form a generic NGA might have. It is recommended that the attached draft generic NGA forms a starting point for consultations with industry, who can contribute their perspectives. It will be necessary to use a number of smaller 'reference groups' to promptly address technical matters associated with NGAs such as those outlined in Annex 4 of the draft generic NGA. This process should be the focus of NGA development in the coming months, with officials reporting progress back to the Ministerial Group by 31 July 2001.

A heads-of-agreement NGA

8. Once the generic NGA framework and conventions have been confirmed it is recommended that officials begin to negotiate heads-of-agreement NGAs as outlined in Annex 1 of the attached draft generic NGA. A heads-of-agreement NGA involves

confirming an intention to sign an NGA, agreeing on information collection and sharing, some timetable and reporting conventions as well as beginning to negotiate a target. This approach maximises progress towards an NGA while the incentive and legal frameworks are separately developed.

Completing the NGA

9. The draft heads-of-agreement includes a time limit of a year for the completion of an NGA from the time of the initial signing. This should enable the passage of the ratification legislation before any heads-of-agreement reach their expiry point. It is expected that the third stage will involve the final negotiation of a target in a more certain legislative framework and thus encourage participation.

Consulting over the generic NGA

10. It is recommended that Cabinet approves officials consulting with potential industry partners, including the use of small 'reference groups' to advance specific technical issues, and report back to the Ministerial group on Climate Change by 31 July 2001. The objective is to advance the technical aspects of NGAs while their legislative status is clarified as part of the development of the ratification legislation.

Proceeding with a heads-of-agreement NGA

11. Once officials have reported on progress with the generic NGA framework, and if the Ministerial Group on Climate Change is satisfied that the proposed framework is robust, then approval is sought to begin to negotiate heads-of-agreement. This will start a timetable that is intended to enable NGAs to be completed promptly once the legislative framework, incentive and liability issues are confirmed.

Other matters

Carbon charge

12. In July 2000 Cabinet directed officials to undertake further analysis of the rate and corresponding sectoral, distributional and competitiveness impacts of a carbon charge and revenue recycling options [ref. CAB (00) M 25/4C]. Officials have prepared a draft summary of sectoral impacts, and have requested tenders from economic consultants to carry out distributional, competitiveness and revenue recycling analyses. It is expected that these analyses will be completed in late May, from which a report will be finalised and submitted to the Minister of Finance in June.

Public education & communication

13. The direction to report to POL by the end of March 2001 [ref CBC Min (01) 3/4] is covered by a separate paper as part of this series.

Financial and legislative implications

14. This paper has no immediate financial implications and its legislative implications will be part of the ratification legislation work-stream.

Consultation

15. The following departments have been consulted during the preparation of this paper and agree with its recommendations: Agriculture and Forestry, Economic Development, Environment, Foreign Affairs and Trade, Transport, Research, Science and Technology, the Treasury and Te Puni Kokiri. The Department of Prime Minister and Cabinet and the Energy Efficiency and Conservation Authority have also been involved in the preparation of this paper.

Recommendations

16. It is recommended that the Committee:

- a) **Note** that Cabinet has already decided that “*..in order to facilitate consultation, particularly in enhanced industry agreements, that emitters should be informed by officials that actions taken by emitters under any pre-2008 price measure implemented by the government will not disadvantage them for the allocation of any units for a post-2008 domestic emissions trading system (or any other post-2008 price measure)..*” [ref. CAB (00) M 25/4C];
- b) **Agree** to a three-stage process for developing NGAs incorporating:
 1. development of a generic framework (incorporating common assumptions and methodologies);
 2. a heads-of-agreement stage (incorporating an intention to proceed and agreeing on information collection and sharing and NGA structure); and
 3. final completion of the agreement with explicit targets (once the legal status of NGAs is confirmed).

Developing a generic NGA framework

- c) **Note** that the generic NGA included as an attachment to this report was developed by officials utilising input from earlier consultations and material subsequently provided by the GPC;
- d) **Note** that the GPC is independently developing legislative recommendations and a draft agreement for the consideration of Ministers and officials;
- e) **Direct** officials from departments participating in the pre-2008 working group to consult with potential NGA participants using the draft generic agreement outlined in the attachment;

- f) **Direct** officials to refine the generic framework taking into account feedback received with as many common assumptions and methodologies as possible and report back to the Ministerial Group on Climate Change by 31 July 2001;
- g) **Agree** that the Ministerial Group on Climate Change be delegated authority to finalise the generic framework agreement;

Heads-of-agreement NGAs

- h) **Agree** that once the Ministerial Group on Climate Change has approved the reported back generic agreement, the Convenor of the Group, in consultation with other Ministers on the Group, be delegated authority to direct officials to conclude heads-of-agreement with firms or collective groups of parties;

Completing negotiations of NGAs

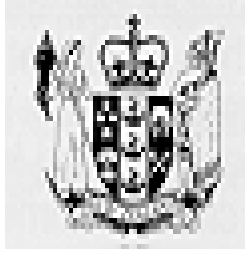
- i) **Note** that officials will report to Cabinet Policy Committee (POL) on progress with heads-of-agreement NGAs and recommendations on the timing and process for initiating negotiations for concluding NGAs by 30 November 2001;
- j) **Note** that the Convenor of the Ministerial Group on Climate Change will be seeking delegated authority to enter into those agreements at that time;

Other matters

- k) **Note** that work is progressing on carbon charge impacts and revenue recycling options; and
- l) **Note** that a previous reporting directive concerning public education and communication is included as a separate paper in this series [ref CBC Min (01) 3/4].

Hon Pete Hodgson
Convenor, Ministerial Group on Climate Change
Minister of Energy & Acting Minister for the Environment

ATTACHMENT



DRAFT ONLY

NEGOTIATED GREENHOUSE AGREEMENT

BETWEEN

THE GOVERNMENT OF NEW ZEALAND

AND

[Industry Partner]

2002 – 2007


**Wellington
New Zealand
[Date]**

Preamble

DRAFT ONLY

Recognising the serious environmental threat of climate change and the urgent need for global action to control greenhouse gas emissions New Zealand has signed the Kyoto Protocol to the United Nations Framework Convention on Climate Change. New Zealand intends to ratify the Kyoto Protocol by mid 2002. Following ratification and subject to the Kyoto Protocol entering into force New Zealand will be required to take responsibility for its greenhouse gas emissions in excess of 1990 levels, on average, during the period from 2008 – 2012.

The Government is implementing measures prior to the first commitment period to build national capacity to meet targets, and to allow New Zealand to meet early requirements of the Protocol. Article 2 of the Protocol requires parties to implement and further elaborate policies and measures in areas such as: enhancing energy efficiency; protecting and enhancing sinks and reservoirs; and promoting sustainable agriculture. Article 3 requires Annex I parties to show “demonstrable progress” towards meeting reduction commitments by 2005.

New Zealand’s -2008 measures to meet these requirements include the implementation of a wide range of programmes to promote the uptake of energy efficiency and renewable energy. This includes product energy efficiency labelling, more demanding building standards, and government and industry leadership programmes, leading up to the likely use of emissions trading and other measures in 2008-2012. In addition the National Energy Efficiency and Conservation Strategy will be issued by 1 October 2001. It is intended that Negotiated Greenhouse Agreements (NGAs) between Government and Industry will be a vital component of early action measures.

The Government recognises the efforts to date by industry to take responsibility for their greenhouse gas emissions through participation in the Voluntary Agreements programme, and the importance of continued cooperation between Industry and Government to achieve Kyoto Protocol targets. The Government wants increased certainty on how it will manage future emissions.

Industry recognises the importance of engaging constructively with Government at an early stage to achieve Kyoto Protocol targets in a manner which minimises distortions to the economy and trade competitiveness impacts. Industry wants flexibility to determine the best methods for meeting reduction commitments balanced by certainty in the rules to be applied to its relationship with government. Industry also wants assurance that they will not be disadvantaged for taking early action.

Government and Industry intend that NGAs, developed and implemented through a structured process as described in Annex X to this agreement¹, will reduce greenhouse gas emission intensity of New Zealand industry in a way that addresses both Government and Industry concerns and objectives.

¹ Developing and implementing negotiated greenhouse agreements is a three-stage process comprising:

1. Consultation with potential NGA participants concerning common issues for NGAs, leading to a generic framework.
2. Negotiation of a heads-of-agreement document with individual firms or collective groupings that intend to complete an NGA.
3. Negotiation of this final agreement.

The model heads-of-agreement document for this NGA is attached as Annex 1; assumptions and conventions relevant to this agreement are attached as Annex 4.

Parties to this agreement

DRAFT ONLY

This agreement is between [the industry partner]² and the Minister of Energy representing the Government of New Zealand.

[Options: *[the industry partner]* may be:

1. *A single firm; or*
2. *A group of firms in a sector, represented by a sector association in the process of negotiation and development of the NGA but on the understanding that they will be individually responsible for compliance with this agreement; or*
3. *Any group of firms that wish to form an association for the purpose of negotiating an NGA and determining a composite emissions target. They will be jointly and severally liable for their commitments under this agreement. Any such approach must have transparency of relationships, a clearly identified administrator and clarity of negotiation and distribution of the collective target.]*

Target and reporting commitments

[The industry partner] undertakes to:

- Meet a target of...

[Options for target definition:

1. *GHG emissions to be limited to a specified level for each reporting year. The level may be defined directly as an agreed figure for total tonnes as CO₂-equivalent, or may be derived as a reduction against an agreed baseline (refer to Annex 5 for baseline definition); or*
 2. *GHG emissions per unit of a measure of output to be limited to a specified level for each reporting year. Refer to Annex 4 for definition of the measure of output.]*
- Report annually as described in Annex 4 progress in implementing the target; and
 - Respond as described in Annex 4 to [the scheme administrator's] reports.

[The Government] undertakes to:

- Maintain and publish information and reports on NGA participants, agreements and performance as described in Annex 4; and
- Respond as described in Annex 4 to annual reports submitted by [the industry partner].

Other provisions

Term of Agreement

The following time limits are placed on this agreement:

DRAFT ONLY

² Eligibility to enter into an NGA could be managed by whether government agrees to negotiate with a party. For smaller parties the Government could suggest that their size makes the agreement uneconomic and that they might like to engage in sector groups.

- This agreement enters into force when both parties deposit signed copies at the Office of the Minister of Energy
- This agreement covers greenhouse gas emissions by [the industry partner] up to 31 December 2007.
- *[Reporting requirements after 2007]*
- This agreement may be terminated as provided in the provisions on review and renegotiation below.

Project-based activities

[The industry partner] may include mitigation by investment in projects that achieve reductions outside its own activities.

Industry partner not to be disadvantaged

The Government agrees that emission reductions achieved under this NGA will not disadvantage [the industry partner] for the allocation³ of any units for a post-2008 domestic emissions trading (DET) system (or any other post-2008 price measure).⁴ *[How to provide a means of enforcing/assuring it will occur?]*

Review and renegotiation of this agreement

Parties may request a review of this agreement at any time after two years have passed from the date of entering this agreement.

The parties to this agreement will meet before 31 March 2005 to review progress towards meeting the NGA target.

Following a review, a renegotiation of the target may be initiated by [the industry partner] only if there has been:

- Relevant and significant changes in environmental requirements that influence its greenhouse gas emissions; or
- Unanticipated market changes requiring investment in new products or processes that influence greenhouse gas emissions; or
- Major structural or company ownership changes *[financial difficulty?]* that materially affects the ability of [the industry partner] to achieve its agreed target; or
- *[Any other general government initiatives that have a significant impact on the ability of parties to meet commitments.]*

Following a review, the Government may initiate renegotiation of this agreement only where, [in the opinion of the scheme administrator] [the industry partner] has failed to comply with reporting commitments under this agreement.

DRAFT ONLY

³ An issue to consider is the treatment of an industry partner that is not a point of obligation. Is this irrelevant or would they have some form of allocation?

⁴The original reference is to the minutes of the June 2000 Cabinet paper on pre-2008 cross-sectoral and price measures. Should there be reference here to any provisions on non-disadvantage if included in the Climate Protection Bill?

Where parties renegotiate this agreement the revised agreement shall be entered within six months of the commencement of negotiations.

[Where an agreement is not reached within 6 months of negotiations commencing should there be provision for one or the other of the parties to terminate the NGA?]

Verification of reported results

[The industry partner] agrees that reports made under the provisions of this agreement will be made available for [*independent*] verification at the discretion of [the scheme administrator]. This may cover greenhouse gas inventory data, calculation of emissions baselines and project based activities under this agreement as outlined in Annex 4.

Sanctions

Sanctions for non performance will be outlined in the Climate Protection Bill and could include:

- *Loss of future access to any Government assistance programmes for a period*
- *Reporting publicly on individual NGA non-achievement*
- *Rescinding agreements*
- *Fines*
- *Loss of non-disadvantage or privileges*

Annex 1 – Heads-of-Agreement

DRAFT ONLY

Parties to Heads-of-Agreement

This agreement is between [the industry partner] and [*the Convenor of the Ministerial Group on Climate Change*]⁵ representing the Government of New Zealand and indicates an intention by both parties to complete a Negotiated Greenhouse Agreement (NGA).

Commitments

[The industry partner] undertakes to:

- Within one year after signing this heads-of-agreement create a timetable for implementing the commitments below;
- Enter an NGA within 12 months of signing this heads-of-agreement document;
- Prepare and report a greenhouse gas emissions inventory covering the years 1990, 1995, 2000 [*or other*]. This should record both its on-site emissions of greenhouse gas emissions and off-site emissions from purchased electricity and steam;
- Carry out energy audit[s] in accordance with AS/NZS 3598:2000 covering [*specify facilities or processes*] to be completed by [*date*]⁶;
- Share information between the NGA heads-of-agreement partners (as per the agreed confidentiality conditions) [*as specified in Annex 4*];
- Develop investment criteria for the assessment of emission reduction projects identified by the audit [*and other processes*];
- Prepare a preferred ranking of emission abatement projects; and
- Negotiate emission limitation targets and an indicative timetable based on the preferred list of projects, in addition to other aspects of an NGA.

[The Government or the agency] undertakes to:

- Make parties who sign heads-of-agreement and NGAs eligible for assistance under [xyz] audit support programme for the energy audits [under certain conditions];
- Keep confidential data provided as part of this head-of-agreement or a related NGA as outlined in Annex 4.
- Prepare a draft publicly available summary of the proposed NGA for consideration by both parties; and
- Negotiate targets, indicative timetables and other aspects of an NGA.

⁵ It will be necessary to get a legal opinion on whether the Minister can delegate signing authority for the HOA.

⁶ It is not possible to do an energy audit for non-energy emissions.

Annex 2 – Proposed activities

DRAFT ONLY

To include a description of the projects or actions (with an indicative timetable) that are planned to enable the target to be met.

Annex 3 – Company profile

[Relevant information on the activities of the industry partner.]

DRAFT ONLY**Annex 4 – Assumptions (rules) and conventions**

[The material included in this annex will be a major focus of the next consultation and will most likely require a “reference group” approach to develop/agree on detail. It is important that as much of this annex as possible is common across agreements. This may not be possible for all matters for all industry partners or additional assumptions may be required in some cases (e.g. associated with unique processes). If so then this annex could be split into common and specific sections.]

Annex 4 is likely to contain the following elements:

- The methodology and assumptions for the treatment of purchased electricity and steam;
- A methodology and emission factors to allow recognition of the avoided emissions benefits of co-generation plants and additional renewable energy;
- A description of verification methodologies or standards;
- Conventions regarding emissions-per-output targets;
- Conventions regarding business-as-usual projections;
- Conventions regarding confidentiality requirements;
- Conventions regarding meeting targets and timetables with a focus on just under what circumstances sanctions are invoked and whether there are options to “put right” non-achievements;
- Conventions regarding a range of sanctions that might apply;
- Conventions and detail regarding the 2005 review and conditions where renegotiation would be possible *[or adequately covered in the NGA itself?]*;
- Minimum reporting requirements and times re what annual reporting and NGA summary documents might include;⁷ *[This will include details of the annual reporting and review process and deadlines for Government responses to annual reports and industry responses to scheme administrator’s reports.]*
- Others.....

Annex 5 – Baseline relevant to this agreement

- A clear description of historical emissions and a business-as-usual projection to enable an NGA target to be negotiated (consistent with an aggregate NGA objective);
- Clear definition of targets relative to a specific baseline; and
- Baseline descriptions as required for any project-based-activities.

⁷ What if an industry group and their electricity supplier bubble? Does this necessitate a re-shaping of the NGAs?