



# Cabinet Economic Growth and Infrastructure Committee

EGI Min (12) 10/3

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.*

---

### Emissions Trading Scheme: Forestry, Agriculture and Other Technical and Operational Changes

**Portfolios: Primary Industries / Climate Change Issues**

On 30 May 2012, the Cabinet Economic Growth and Infrastructure Committee (EGI), having been authorised by Cabinet to have Power to Act [CAB Min (12) 18/20]:

#### Background

- 1 **noted that:**
  - 1.1 a statutory review of the New Zealand Emissions Trading Scheme (ETS) was completed in 2011;
  - 1.2 the ETS Review Panel made 61 recommendations, largely focused on improving the operation of the ETS and slowing the transition to full obligations under the scheme;
- 2 **noted that** on 18 July 2011, Cabinet invited the Minister for Climate Change Issues to report back to EGI by February 2012 with proposed changes to the ETS based on the ETS Review Panel's recommendations, developments in and discussions with Australia, and further analysis [CAB Min (11) 27/15];
- 3 **noted that** because of the complexity and number of issues covered, advice on proposed ETS amendments is being provided over a series of papers, and that the paper under EGI (12) 80 is the third paper in that series;
- 4 **noted that** a number of proposed amendments to the Act, aimed at implementing key recommendations of the ETS Review Panel and key commitments in the National Party's Manifesto, have recently been subject to a public consultation process [CAB Min (12) 8/7];
- 5 **noted that** the paper under EGI (12) 80 proposes 27 specific technical and operational changes to the ETS that are more minor in nature to those previously considered by Cabinet, and are aimed at improving the operational effectiveness of the ETS;
- 6 **noted that** these changes relate to:
  - 6.1 forestry;
  - 6.2 forestry, Māori land and the Māori Trustee;

- 6.3 agriculture;
  - 6.4 energy sector;
  - 6.5 allocation;
  - 6.6 registry, compliance and Crown accounts;
  - 6.7 other minor technical amendments;
- 7 **noted** that all the policy proposals outlined below are for “in principle” decisions, and will be subject to the broader outcomes of the current ETS consultation process;
- 8 **noted** that the Minister for Climate Change Issues will report back to EGI by July 2012, reporting on the results of the consultation and seeking final policy decisions on an overall package of proposed amendments to the Act;

## Forestry

### De minimus deforestation and boundary management

- 9 **noted** that pre-1990 forest landowners are likely to breach the two hectare deforestation threshold through routine forest management activities, and that there is no *de minimus* threshold available to post-1989 forestry participants;
- 10 **noted** that any deforested area on the outer boundary of an area of forest land counts towards a pre-1990 forest landowner’s, or post-1989 forestry participant’s, deforestation, but that internal gaps that are less than 1 hectare or have an average width of less than 15 metres are permitted;
- 11 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that clearing on the outer boundary of a forest land area that results in a reduction compared to the forest land area that existed on 31 December 2007 for pre-1990 forest land, or that was registered in the ETS for post-1989 forest land, is not treated as deforestation, provided that:
- 11.1 each cleared area is less than 1 hectare, or less than 30 metres wide; and
  - 11.2 the reduction is part of normal forest management; and
  - 11.3 the cleared area is not used for any other land use;

### Tree weeds

- 12 **noted** that the control of tree weeds on pre-1990 forest lands will be an ongoing activity;
- 13 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to extend pre-1990 tree weed exemptions beyond 2012 for up to 200,000 NZUs per annum;
- 14 **noted** that post-1989 tree weeds may be registered in the ETS and earn carbon credits, and that this creates a financial incentive for landowners to retain tree weeds;

- 15 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to prevent the registration in the ETS of naturally regenerated tree weeds on post-1989 forest land, unless the Environment Protection Authority is satisfied that the risk of the tree spread is low;

**Natural regeneration of indigenous species on pre-1990 forest lands**

- 16 **noted** that, after clearing, land that is regenerating to indigenous forest often takes longer to meet the forest land definition than currently permitted in the Act, and that this inadvertently creates deforestation liabilities;
- 17 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that forest land that is regenerating to indigenous forest is not to be treated as deforested where:
- 17.1 4 years after clearing, the land is regenerating to forest land; and
  - 17.2 10 years after clearing, the land is forest land; and
  - 17.3 20 years after clearing, predominantly indigenous forest species are growing that have tree crown cover of more than 30 percent from forest species that have reached 5 metres in height;

**Re-establishing poplar and willow forest lands**

- 18 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that land is not to be treated as deforested where:
- 18.1 the forest land was established for erosion control; and
  - 18.2 four years after clearing, the land is forest land where the forest species are poplars or willows, provided that at least 100 stems per hectare are established;

**Natural disturbance events preventing forest land re-establishment**

- 19 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that where forest land is cleared due to natural cause or event and the area cannot be re-established due to the land conditions, then the land is not considered to be deforested;

**Forestry operational issues**

- 20 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to extend the emissions return period for post-1989 forest land activities to six months from the end of the period to which the return relates;

**Forestry, Māori land and the Māori Trustee**

**Māori Trustee and the less than 50 hectares exemption for pre-1990 forests**

- 21 **noted** that unrelated pre-1990 forest landholdings of a sole professional trustee, including the Māori Trustee, are counted towards the 50 hectare threshold for a less than 50 hectare exemption, preventing an exemption application for these land holdings;

- 22 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that unrelated pre-1990 forest landholdings of a sole professional trustee, including the Māori Trustee (ie, landholdings of unrelated trusts or of a Trustee in personal/non-trustee capacity), are not counted towards the 50 hectare threshold for an exemption application by such trustee, in respect of a trust;
- 23 **noted** that a trustee appointed under the Te Ture Whenua Māori Act 1993 is not a professional trustee for the purposes of the Climate Change Response Act 2002;
- 24 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act so that:
- 24.1 for the purposes of an application for a less than 50 hectare exemption, a trustee appointed under the Te Ture Whenua Māori Act 1993 is treated as a professional trustee;
- 24.2 unrelated pre-1990 forest landholdings of a trustee appointed under the Te Ture Whenua Māori Act 1993 are not counted towards the 50 hectare threshold for an exemption application by such trustee, in respect of a trust;

## **Agriculture**

### **Exclusion of egg producers from the ETS**

- 25 **noted** that including egg producers in the ETS imposes significant administration and reporting costs on both the sector and the government relative to future emissions charges recovered;
- 26 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to remove egg producers as an activity under Schedule 3 of the Act;
- 27 **noted** that, when administrative cost savings are included, the net fiscal impact for the Crown of the above proposal is a saving of \$50,000 for the period 2012/13 to 2015/16, and a saving of \$8,000 for the overall period 2012/13 to 2019/20;

### **Meat processors: de minimus threshold**

- 28 **noted** that the current exclusion of retail butchers in the Act is too broad and may exclude a wider range of meat processors than intended;
- 29 **noted** that there are no fiscal risks or costs associated with changing the retail butcher exemption;
- 30 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to:
- 30.1 remove the retail butcher exemption from Schedule 3 of the Act;
- 30.2 clarify the existing activity definition to the slaughter of ruminant animals, pigs, horses or poultry by a person required under the Animal Products Act 1999 to operate under a risk management programme for that activity (ie, the activity of slaughtering);

## Energy sector

- 31 **noted** that the own-use of crude oil or other liquid oil products by miners is a new emissions source in New Zealand which did not exist when the ETS was established, and that the Act does not require these emissions to be reported;
- 32 **noted** that changes in the liquid fuels sector since the ETS was established have given rise to new industry participants for whom the ability to opt in would be appropriate;
- 33 **noted** that there is apparent ambiguity in the way the obligation for geothermal participants is defined;
- 34 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to:
- 34.1 add the combustion of crude oil or oil products by a miner as an activity in Schedule 3;
- 34.2 extend the coverage of Part 3, Schedule 4 to include all liquid fuels;
- 34.3 clarify that if a geothermal user supplies exhaust steam or other geothermal material to another party, that other party is not also a mandatory participant;

## Allocation changes

- 35 **noted** that the ETS Review Panel recommended a change to the phase-out of allocations which would ensure that allocations are eventually phased out entirely;
- 36 **noted** that monitoring and enforcement activities are essential for the effective administration of allocations, and that the Act does not explicitly include these under “administering allocations” as a function of any agency;
- 37 **noted** that the current rules allow early applications for industrial allocations, and that this creates administrative costs for no real benefit to applications;
- 38 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to:
- 38.1 change the calculation of phase out for industrial and agricultural allocations so that the phase out will continue until these allocations are entirely withdrawn;
- 38.2 clarify that the Environmental Protection Authority’s functions in section 87 include monitoring and enforcement activities over eligible persons;
- 38.3 specify that all applications for industrial allocations must be made between 1 January and 30 April in the relevant year;

## Administration of the Unit register, ETS accounts and emission returns

- 39 **noted** that the excess emissions penalty of \$30 per unit on units not surrendered or repaid is sometimes waived, and cannot be re-imposed if a participant fails to make a re-set deadline, leaving no effective penalty in these cases;
- 40 **noted** that participants are currently required to deregister when they stop an emitting activity, even temporarily, and to re-register when they resume that activity;

- 41 **noted** that under section 65 of the Act, the Crown cannot sell units surrendered by participants, and that there is expected to be a surplus of Kyoto units which are currently valued in the Crown accounts at their market value;
- 42 **noted** that section 159 of the Act requires the Crown to purchase units on behalf of a participant who is in default or is insolvent, and that this requirement will no longer be necessary if NZUs are not backed by international units;
- 43 **noted** that section 159 of the Act specifies that the cost of units for a participant who is in default or is insolvent is an unsecured debt, and that the status of such a debt is a factual matter that does not need to be specified in the Act;
- 44 **noted** that participants may use a “consolidated group account” to submit emission returns and surrender units for a group of related companies, but are not currently able to use the consolidated group account to apply for and receive allocations;
- 45 **noted** that section 63 of the Act makes participants responsible for “each whole tonne” of emissions, and that this may be interpreted as meaning that the rounding of numbers in an emissions calculation must be done in a way that compromises accuracy;
- 46 **noted** that the Act does not make provision for regulations to be made setting criteria, other than thresholds, to be set for all removal activities in Subpart 1, Part 2 of Schedule 4 of the Act;
- 47 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to:
- 47.1 make a \$30 per unit excess emissions penalty available when there is a failure to surrender or repay units under a notice issued by the Environmental Protection Authority;
- 47.2 require a participant to de-register only when they stop an emitting activity permanently, and allow for the submission of a nil (i.e. zero emissions) emission return;
- 47.3 allow for the possible future sale of Kyoto units in the surrender account which are surplus to New Zealand’s current international obligation or equivalent level of domestic effort at the time of sale;
- 47.4 remove the requirement for the Crown to purchase units on behalf of a participant, and to remove the reference to an unsecured debt to the Crown;
- 47.5 allow the use of a consolidated group account for allocation purposes;
- 47.6 clarify that rounding calculations can be made under the Act, which would permit rounding up to the nearest tonne as part of an emissions calculation;
- 47.7 create a regulation-making ability that will allow the setting of criteria for activities in Subpart 1, Part 2 of Schedule 4;

### **Minor technical amendments**

- 48 **noted** that successive amendments to the Act have resulted in some cross-referencing errors;

- 49 **noted** that deadlines for participants are specified in inconsistent ways in different parts of the Act, so that the exact due date for an action is not always clear;
- 50 **noted** that section 204 of the Act specifies that the holder of a coal or gas mining permit “under any Act” is the mandatory participant for these activities;
- 51 **agreed in principle**, subject to final decisions on the overall ETS package, to amend the Act to:
- 51.1 correct cross-referencing errors;
- 51.2 specify deadlines consistently so that the due date is made clear;
- 51.3 specify that permits under section 204(2)(a) only refer to permits under the Crown Minerals Act 1991;

### Fiscals costs and implications

- 52 **noted** the following indicative fiscal implications, not including administrative cost savings, of the proposals in paragraphs 9 to 51 above:

\$ million	Increase/(decrease) in operating balance					Total
	2011/12	2012/13	2013/14	2014/15	2015/16	
Excluding layer hens from the ETS (not including admin. cost savings)	-	-	-	(0.013)	(0.028)	(0.041)
Extending the Pre-1990 tree weed exemption to 2015/16	-	(1.04)	(2.08)	(2.08)	(2.08)	(7.280)
<b>Total</b>	-	<b>(1.04)</b>	<b>(2.08)</b>	<b>(2.093)</b>	<b>(2.108)</b>	<b>(7.321)</b>

- 53 **noted** that:
- 53.1 administrative cost savings from the exclusion of layer hens from the ETS are likely to total \$93,000 over the forecast period;
- 53.2 fiscal implications will be considered when Cabinet makes decisions on the final package of ETS changes by July 2012;

### Legislative implications

- 54 **invited** the Minister for Climate Change Issues to issue drafting instructions to the Parliamentary Counsel Office based on the “in principle” decisions on the policy proposals presented in the paper under EGI (12) 80;
- 55 **authorised** the Minister for Climate Change Issues, in consultation with the Minister for Primary Industries as appropriate, to further clarify and develop policy matters relating to the amendments proposed in the paper under EGI (12) 80, in a way that is consistent with Cabinet’s decisions;

## Communication and public consultation

- 56 noted that on 12 March 2012, Cabinet authorised the Minister for Climate Change Issues to be responsible for communication and engagement with stakeholders and iwi regarding the proposed amendments and response to the ETS Review Panel's recommendations [CAB Min (12) 8/7].

Committee Secretary

Reference: EGI (12) 80

---