

In-Confidence

Office of the Minister for Climate Change

Cabinet Environment, Energy and Climate Committee

Consultation on Government's proposed action on agricultural emissions

Proposal

1. I seek approval to:
 - 1.1. release a discussion document (Appendix 1) for a short, focused public consultation on the Government's proposed response to the Interim Climate Change Committee's recommendations on agriculture;
 - 1.2. instruct the Parliamentary Counsel Office to begin tentative drafting options based on all legislative proposals in this paper, noting final drafting is subject to consultation and final policy decisions by Cabinet.

Executive Summary

2. This year, the Government is introducing two separate Bills to amend the Climate Change Response Act 2002 (the Act):
 - 2.1. the Climate Change Response (Zero Carbon) Amendment Bill (ZCB) sets the overarching, enduring framework to drive the transition to a low-emissions and climate-resilient New Zealand, including an interim 2030 target and long-term 2050 target to reduce biogenic methane emissions;
 - 2.2. The Climate Change Response Amendment Bill (CCRAB) makes a targeted set of improvements to strengthen the overall operation of the New Zealand Emissions Trading Scheme (NZ ETS).
3. Agriculture will play a key role in how New Zealand meets its domestic and international climate change commitments. In 2017, biological emissions from agriculture, largely methane and nitrous oxide, accounted for 48 percent of New Zealand's total emissions. Despite widespread productivity and efficiency gains since 1990, agricultural emissions have increased by 13.5 percent. Without policies aimed directly at reducing these emissions, we risk the cost of targets falling inefficiently and inequitably on taxpayers and the rest of the economy. We could also miss opportunities to incentivise action by the agricultural sector and to demonstrate international leadership.
4. To begin making progress on agriculture, we tasked the Interim Climate Change Committee (Interim Committee) to provide independent evidence, analysis and recommendations on how surrender obligations could best be arranged if methane and nitrous oxide emissions entered into the NZ ETS. To answer this question, the Interim Committee considered the full range of

options to deliver efficient emissions reduction, consistent with the objective of a just transition to a low-emissions, climate-resilient New Zealand.

5. On 30 April 2019, I received the Interim Committee's final report (the report), which makes seven key recommendations for action on agricultural emissions:
 - 5.1. specify in law a farm-level levy/rebate scheme to price livestock emissions, with mandatory reporting by 2023 and obligations by 2025;
 - 5.2. price livestock emissions in the NZ ETS at processor level in the interim;
 - 5.3. price fertiliser emissions in the NZ ETS at processor level;
 - 5.4. provide the assumed 95 percent rate of free allocation to offset the full impact of emissions pricing and support farmers in the transition;
 - 5.5. establish an Agricultural Emissions Fund to recycle all funds back to mitigation, including a ring-fenced portion for iwi/Māori landowners and a Board with sector and iwi/Māori representation;
 - 5.6. investigate opportunities to recognise and reward on-farm offsetting, including counting pre-1990 forests and small on-farm plantings; and
 - 5.7. investigate opportunities to address non-climate regulatory barriers, stimulate innovation and create new markets for low-emissions products.

6. Cabinet agreed to hold a short, focused consultation on the report's recommendations [CAB-18-MIN-5042 refers], but held off releasing the report until a response was agreed. An extended consultation period would not enable agricultural provisions to be included at the beginning of the CCRAB Parliamentary process as intended. I note the Interim Committee consulted widely in developing its views, and interested parties will be able to submit at the Select Committee stage.

7. I propose Cabinet agree to release a discussion document (Appendix 1) for a four-week consultation on the Government's proposed response to the report. The discussion document proposes a legislative commitment to pricing emissions in the NZ ETS at farm level by 2025. However, given concerns around the technical feasibility and cost-effectiveness of farm-level pricing, there will be flexibility to review this timeframe. The specific proposals include:
 - 7.1. applying voluntary farm-level reporting on livestock emissions in the NZ ETS from 2023 and mandatory farm-level reporting from 2024;
 - 7.2. requiring farm-level obligations on livestock emissions in the NZ ETS from 2025, subject to the responsible minister(s) tabling a report in Parliament by 2022 on:
 - 7.2.1. whether farm-level pricing is feasible by this time, and if not, whether a processor-level price is necessary by default; and
 - 7.2.2. any other legislative and regulatory amendments required;

- 7.3. investigating opportunities to recognise and reward carbon removals from on-farm vegetation.
8. I note, however, in light of the urgent action needed to meet our short-term climate change goals, we cannot wait until 2025. There are opportunities to get started on reducing agricultural emissions in the interim. There are two options identified by the Interim Committee as interim measures (described below).

Option A: Processor-level obligations for livestock emissions in the NZ ETS

9. This first option is consistent with the Interim Committee's recommendations to:
- 9.1. price livestock and fertiliser emissions in the NZ ETS at processor level as soon as practicable (expected to enter into force from 2021);
 - 9.2. provide free allocation at 95 percent and recycle all funds to the sector to support investment in mitigation, and afforestation (more information on processor-level allocation is provided in Appendix 2); and
 - 9.3. develop a joint action plan with the sector and iwi/Māori towards making a farm-level pricing scheme workable and effective, including a potential emissions reduction incentives scheme.

Option B: A formal agreement between Government and industry

10. An alternative option involves a formal agreement between the Government and agricultural sector. We have received a proposal from the Primary Sector Leaders Group¹, which sets out a five-year Programme of Action to reduce on-farm emissions and support farm-level pricing by 2025, including by:
- 10.1. developing emission estimation and reporting systems;
 - 10.2. integrating climate change into audited Farm Environment Plans for all farms by 2025;
 - 10.3. building farm and rural professional climate change knowledge;
 - 10.4. increasing investment in research and development to expand the tool box available to farmers;
 - 10.5. engaging with the One Billion Trees programme to enhance on-farm carbon sinks to offset farm emissions;
 - 10.6. developing strategies for on-farm climate change adaptation; and
 - 10.7. engaging internationally to encourage global momentum on matters related to agriculture emissions.
11. Both options have trade-offs in terms of providing regulatory and investment certainty for climate change policy, compared with giving the sector fuller

¹ Current member organisations are: Federated Farmers, DairyNZ, DCANZ, Beef+Lamb New Zealand, Meat Industry Association, Irrigation NZ, Apiculture NZ, Foundation of Arable Research, Deer Industry NZ, Federation of Māori Authorities, and Horticulture NZ.

control over how to manage a range of diverse environmental outcomes (including fresh water and biodiversity). I propose the discussion document consult on both options to seek feedback from the sector, iwi/Māori and the public on the preferred interim measure in the transition to farm-level pricing.

12. section 9(2)h

Potential disproportionate impacts on iwi/Māori will be further considered in regulatory impact analysis undertaken to inform any final policy decisions.

13. section 9(2)(f)(iv)

Background

Cabinet decisions created a long-term framework for climate change policy

14. The Coalition Agreement between the New Zealand Labour Party and New Zealand First (Coalition Agreement) included the following commitments:
 - 14.1. introduce a Zero Carbon Act and an independent Climate Commission, based on the recommendations of the Parliamentary Commissioner for the Environment; and
 - 14.2. if agriculture is to be included in the ETS, then upon entry, the free allocation to agriculture will be 95 percent but with all revenues from this source recycled back into agriculture in order to encourage agricultural innovation, mitigation and additional planting of forestry.
15. On 6 May 2019, Cabinet agreed the following components of a greenhouse gas emissions reduction target to be included in the Climate Change Response (Zero Carbon) Amendment Bill (ZCB):
 - 15.1. net-zero emissions for all greenhouse gases, except biogenic methane, by 2050;
 - 15.2. a reduction in gross emissions of biogenic methane within the range of 24-47 percent below 2017 levels by 2050; and
 - 15.3. an interim requirement to reduce gross emissions of biogenic methane by 10 percent below 2017 levels by 2030.
16. Cabinet has also agreed two tranches of amendments designed to improve the NZ ETS, as part of a separate Climate Change Response Amendment Bill (CCRAB). Tranche one amendments were agreed by Cabinet in December

2018 [CAB-18-MIN-0606.01 refers] and the Parliamentary Counsel Office has commenced drafting. Tranche two included several papers earlier this year.

We established the Interim Committee to begin making progress on agriculture

17. Cabinet established the Interim Committee as a precursor to the independent Commission to begin making progress on agriculture and renewable electricity [CAB 17-MIN-0547.01 refers]. The Interim Committee is an independent Ministerial Advisory Group without decision-making authority or powers.
18. In April last year, Cabinet agreed to the terms of reference for the Interim Committee [CAB-18-MIN-0108 refers] to provide evidence and analysis on:
 - 18.1. how surrender obligations could best be arranged if agriculture methane and nitrous oxide enter into the NZ ETS; and
 - 18.2. planning for the transition to 100 per cent renewable electricity by 2035.
19. On 1 June 2018, the members of the Interim Committee updated me on their work programme and their broad interpretation of the terms of reference to:
 - 19.1. deliver evidence and analysis on ways of delivering efficient emission reductions in the agriculture sector that are consistent with the Government's objective for a just transition; and
 - 19.2. consider the full suite of options that could deliver those reductions while recognising that the NZ ETS would be a key focus of their work.
20. In November 2018, Cabinet agreed in principle to change the Interim Committee's terms of reference to extend its role to provide recommendations, alongside evidence and analysis, on agriculture and renewable electricity [CAB-18-MIN-0542 refers]. This change was confirmed by a delegated group of ministers, following targeted engagement with iwi/Māori and key stakeholders.

The Interim Committee makes seven key recommendations on agriculture

21. After I received an embargoed copy of the Interim Committee's report on 18 April, I updated Cabinet on the report's recommendations and the initial advice from officials on a proposed Government response. Cabinet decided not to release the report publicly until a Government response was agreed.
22. On 30 April 2019, I received the Interim Committee's final report. The report makes the following seven key recommendations for Government action on agricultural emissions:
 - 22.1. specify in law a farm-level levy/rebate scheme to price livestock emissions, with mandatory reporting by 2023 and obligations by 2025;
 - 22.2. price livestock emissions in the NZ ETS at processor level in the interim;
 - 22.3. price fertiliser emissions in the NZ ETS at processor level;

- 22.4. provide the assumed 95 percent rate of free allocation to offset the full impact of emissions pricing and support farmers in the transition;
- 22.5. establish an Agricultural Emissions Fund to recycle all funds back to mitigation, including a ring-fenced portion for iwi/Māori landowners and a Board with sector and iwi/Māori representation;
- 22.6. investigate opportunities to recognise and reward on-farm offsetting, including counting pre-1990 forests and small on-farm plantings; and
- 22.7. investigate opportunities to address non-climate regulatory barriers, stimulate innovation and create new markets for low-emissions products.

Comment

I seek agreement to consult on Government's proposed response to the report

23. I seek approval to release a discussion document (Appendix 1), alongside the Interim Committee's report and technical appendices, for a short, focused consultation of four weeks on the Government's proposed response to the report.
24. **Table 1**, over the page, provides more detail on the report's recommendations and how the proposed response to each recommendation is reflected in the discussion document. This includes proposed legislative changes in 2019, as well as policy decisions to signal future work.

Table 1. Proposed Government response to the Interim Climate Change Committee’s recommendations on agriculture

Recommendation	Recommended Government action	Government’s preferred response
1. Introduce a farm-level levy/rebate scheme on livestock emissions by 2025	a. Specify in legislation that farmers will start reporting their emissions in 2023, and face obligations for their livestock emissions under a levy/rebate scheme by 2025	<p>Partially agree – The Government’s preference is to amend the Climate Change Response Act 2002 (the Act) to:</p> <ul style="list-style-type: none"> i. require farm-level surrender obligations on livestock emissions in the NZ ETS from 2025; ii. apply voluntary farm-level reporting on livestock emissions from 2023 and mandatory farm-level reporting from 2024; iii. require the responsible minister(s) to table a report in Parliament by 2022 on: <ul style="list-style-type: none"> • whether farm-level pricing is feasible by this time, and if not, whether a processor-level pricing is necessary by default; and • any other legislative and regulatory amendments required.
	b. Develop an action plan with the agriculture sector and iwi/Māori, including owners of Māori land, outlining the necessary processes to introduce a farm-level levy/rebate scheme on livestock emissions by 2025	<p>Agree – The Government agrees to develop a work programme to design and implement a workable and effective farm-level pricing scheme with the agricultural sector and iwi/Māori. What form this action plan takes will depend on the Government’s chosen interim measure (refer to Recommendation 2 below).</p>
	c. Outline in law the process by which any decisions will be made on changes to the price on methane to achieve different targets for different gases.	<p>Agree in principle – more work required – Officials will undertake further work on including the process for making decisions on the management of methane in relation to a long-term, farm-level pricing scheme.</p>
4. Price livestock emissions at processor-level through the NZ ETS in the interim	Amend the Climate Change Response Act to price methane and nitrous oxide emissions from livestock at processor level in the NZ ETS as soon as practicable.	<p>In the interim transition, the Government proposes EITHER:</p> <ul style="list-style-type: none"> A. amending legislation to price livestock and fertiliser emissions in the NZ ETS at processor level as soon as practicable (expected to enter into force from 2021); OR B. developing a formal agreement with the sector that includes specific commitments to reduce emissions and support the transition to farm-level pricing by 2025.
5. Price nitrogen fertiliser emissions through the NZ ETS	Amend the Climate Change Response Act to price synthetic nitrogen fertiliser emissions at the manufacturer and importer level in the NZ ETS as soon as practicable.	See Recommendation 2. In the long term, fertiliser emissions would be priced at the processor level. This is because farm-level pricing would incur additional administrative costs without any additional incentive to reduce nitrous oxide emissions from fertiliser.
6. Assisting farmers and rural communities through free allocation	a. Use a hybrid of output- and land-based allocation for livestock emissions in a farm-level levy/rebate scheme, subject to further work and consultation on: <ul style="list-style-type: none"> • a suitable proxy for the productive capacity of land • determining the ratio of output-based to land-based allocation • eligibility rules. 	<p>Agree in principle – more work required – Farm-level allocation will be considered as part of work to investigate and design a long-term, farm-level price. The Government will focus on providing 95 percent free allocation at the processor level in the interim.</p> <p>For free allocation at the processor level, the Government intends to consult on the output-based method as the preferred option (see Appendix 2 for more information).</p>
	b. Consider an option for farmers to capitalise their allocation in exchange for facing the full costs of their livestock emissions for the period covered by the lump-sum.	<p>Agree in principle – more work required – This recommendation will be considered as part of work to design and implement a long-term, farm-level price.</p>
	c. Set livestock-related allocation factors so that they reduce in line with	<p>Agree – The Government agrees to set a process for updating livestock-related</p>

Recommendation	Recommended Government action	Government's preferred response
	<p>expected improvements in emissions intensity, with periodic reviews to account for less predictable changes in emissions intensity.</p> <p>d. Outline in law the process by which any decisions on the phase down of the free allocation rate will be made.</p>	<p>emissions and allocation factors in line with expected improvements in emissions intensity, with periodic reviews to account for less predictable changes in emissions intensity.</p> <p>Agree – The Government agrees that any phase-down of the free allocation rate for agriculture will be outlined in legislation in a manner consistent with other sectors in the NZ ETS (i.e. industrial allocation).</p>
10. Recycling funds through an Agricultural Emissions Fund	<p>Recycle funds generated from pricing methane and nitrous oxide emissions from agriculture directly back into programmes that help farmers to reduce emissions, specifically including:</p> <ol style="list-style-type: none"> The establishment of an Agricultural Emissions Fund The establishment of a Board to oversee spending of the Fund that ensures co-governance with the agricultural sector and iwi/Māori, including owners of Māori land. All Board members must understand and take into account the unique characteristics of Māori land Criteria for allocating money from the Fund, including providing appropriate support to owners of Māori land The requirement for the Board to report annually on how funds have been spent and the effectiveness of that spending. Criteria for allocating money from the Fund, including providing appropriate support to owners of Māori land The requirement for the Board to report annually on how funds have been spent and the effectiveness of that spending. 	<p>Agree – The Labour-New Zealand First Coalition Agreement states:</p> <p>“if the Climate Commission determines that agriculture is to be included in the ETS, then upon entry, the free allocation to agriculture will be 95% but with all revenues from this source recycled back into agriculture in order to encourage agricultural innovation, mitigation and additional planting of forestry.”</p> <p>The Government will undertake further work to design the recycling of funds, including their governance and specific uses. Introducing a scheme to reward farmers who take early action could be a key focus of this work.</p>
11. Counting carbon sequestration by trees and vegetation on farm	<ol style="list-style-type: none"> Prioritise work underway to improve the NZ ETS for forestry, to make it easier for forest owners to identify eligible forest land and register it in the NZ ETS Investigate opportunities to recognise and reward forestry management practices that store additional carbon in pre-1990 forests Investigate opportunities to recognise and reward small plantings on farms Investigate the feasibility of ‘netting-off’ carbon removals and agricultural emissions within the farm-level levy/rebate scheme. 	<p>Agree - The Government agrees to include these aspects in a joint action plan with the sector and iwi/Māori, as either (a) supporting measures for processor-level emissions pricing in the NZ ETS or (b) part of the formal agreement with the sector to reduce emissions and support the transition to farm-level pricing.</p>
12. Opening up opportunities	<ol style="list-style-type: none"> Investigate barriers to reducing emissions created by non-climate regulation and options to remove them investigate how to facilitate opportunities to create new markets for low-emissions products. 	<p>Agree - The Government agrees to begin work on this recommendation.</p>

I propose transitioning to a farm-level price on emissions in the long term

25. I agree with the Interim Committee that a farm-level price incentive for livestock emissions should be the ultimate objective. This is because it can incentivise a wider, more targeted range of mitigation measures and better stimulate behaviour change and innovation. However, this is unlikely to be technically feasible or administratively cost-effective in the short term.
26. The concerns around technical feasibility and cost-effectiveness relate to the level of sophistication required for monitoring, reporting and verification across approximately 30,000 diverse farms in New Zealand. That level of sophistication does not exist in the tools and systems we currently have available, in order to capture the wider range of mitigation practices and incentivise behaviour change at the farm level.
27. Nevertheless, I consider it is important for regulatory and investment certainty to signal the transition to farm-level obligations in the long term. Therefore, I propose to amend the Act to:
- 27.1. apply voluntary farm-level reporting on livestock emissions in the NZ ETS from 2023 and mandatory farm-level reporting from 2024; and
- 27.2. require farm-level surrender obligations on livestock emissions under the NZ ETS at 2025.
28. Given concerns around feasibility, however, it will also be critical to provide flexibility around these timeframes. Therefore, I also propose amending the Act to require the Minister(s) responsible to table a report in Parliament by 2022 on:
- 28.1. whether farm-level pricing is feasible under this timeframe, and if not, whether processor-level pricing is necessary by default; and
- 28.2. any other legislative and regulatory amendments required.

If priced, fertiliser emissions should remain in the NZ ETS at processor level

29. The Interim Committee notes the only currently recognised way to reduce nitrous oxide emissions from fertiliser is to use less. There would be no additional benefit from a farm-level obligation, as the incentive for farmers to reduce fertiliser emissions is the same whether they are priced at processor or farm level. Including around 5,000 horticulture and arable farmers in the NZ ETS would simply result in additional administrative and transaction costs.
30. Therefore, I propose that, if priced, fertiliser emissions should enter and remain in the NZ ETS at processor level. The Government could review this decision at a later stage if there are scientific developments that demonstrate the impacts of on-farm variables (e.g. soil type, regional variation) on the incentives to reduce nitrous oxide emissions from fertiliser.

I propose to consult on two options for interim progress on livestock emissions

31. Notwithstanding the above proposals, reducing agricultural emissions cannot wait until 2025. There are opportunities to make progress now and avoid further delays in the sector's contribution to the transition to a low-emissions economy.

32. The Interim Committee discussed two ways of encouraging interim progress:
- 32.1. pricing agricultural emissions at the processor level (to expose farmers to an emissions price indirectly); or
- 32.2. developing a formal agreement between the Government and sector.
33. Pricing agricultural emissions at the processor level would create some incentives for the available mitigation options to be taken up now and to facilitate the transition to farm-level obligations. This would provide short-term regulatory and investment certainty and encourage the sector to factor the cost of mitigation into decision-making. It could also reduce the long-term fiscal risk to the Government of meeting our climate change targets.
34. A formal agreement would provide comparatively less regulatory and investment certainty. However, it would give fuller control to the sector to integrate emissions reduction outcomes within existing strategies. This includes potential integration within Farm Environment Plans to manage diverse environmental outcomes such as freshwater quality and biodiversity.
35. The Interim Committee recommended a processor-level price on emissions in the NZ ETS, in order to provide certainty about the future direction of policy. The Interim Committee compared this with the risk of further delay and the significant additional investment associated with a formal agreement.
36. Both options are worth considering and seeking feedback on preferences from the sector, iwi/Māori and the general public. I propose to consult on both options, described in further detail in **Table 2**, below:

Table 2. Options for an interim measure to incentivise emissions reduction

Option A: Processor-level obligations in the NZ ETS	Option B: Formal Government-industry agreement
<p>Proposes to amend the Act to:</p> <ul style="list-style-type: none"> • price livestock and fertiliser emissions in the NZ ETS at processor level as soon as practicable (expected to enter into force from 2021); • provide free allocation at 95 percent, using an output-based method (refer to Appendix 2 for more detail). <p>Also proposes policy decisions to:</p> <ul style="list-style-type: none"> • develop a joint action plan with the sector and iwi/Māori towards making a farm-level pricing scheme workable and effective; • recycle all funds through an Agricultural Emissions Fund, with a Board including sector and iwi/Māori representatives, to encourage innovation, mitigation and afforestation; and • establish an emissions reduction incentives scheme to recognise and 	<p>Proposes a formal agreement with the sector to reduce on-farm emissions and support progress towards farm-level pricing by 2025, including:</p> <ul style="list-style-type: none"> • developing emission estimation and reporting systems; • integrating climate change into audited Farm Environment Plans for all farms by 2025; • building farm and rural professional climate change knowledge; • increasing investment in research and development to expand the tool box available to farmers; • engaging with the One Billion Trees programme to enhance on-farm carbon sinks to offset farm emissions; • developing strategies for farm climate change adaptation; and • engaging internationally to encourage global momentum on matters related

reward carbon removals on farm.	to agricultural emissions.
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I propose a short, focused consultation on Government's proposed response

37. In November 2018, Cabinet agreed to hold a short, focused consultation on the Interim Committee's final report to enable the public, including key stakeholders and iwi/Māori, to have their say [CAB-18-MIN-0542 refers]. I noted a short, focused consultation on a significant policy issue may attract criticism of the Government's process, but this is necessary to enable any resulting legislative changes to be included as part of the CCRAB when introduced into the House.
38. I propose a short, focused consultation of four weeks to seek feedback on the Government's proposed response to the report's recommendations. Consultation will include public release of the discussion document (Appendix 1), alongside the Interim Committee's report and technical appendices.
39. Officials have engaged with a number of agriculture sector representatives, including members of the Biological Emissions Reference Group, on their respective views, issues and concerns on agricultural emissions policy. I intend for consultation to include workshops with targeted stakeholders and interested members of the public to seek feedback on the Government's proposals.
40. Consultation follows up on officials' pre-engagement with iwi/Māori on climate change policy, as part of the Ministry for the Environment's new Te Ao Māori Strategy. The Strategy is a response to requests for a 'joined-up' or integrated approach to partnering with iwi/Māori on environment policy. In May 2019, Ministry officials carried out 16 regional hui, the first of an ongoing quarterly hui cycle. A series of phone calls also established key relationships with iwi/Māori leaders and flagged the upcoming consultation on agricultural emissions policy.
41. In this context, it was not considered beneficial to hold ad hoc hui outside the quarterly regional hui cycle. Nevertheless, consultation will involve a follow-up series of phone calls, and one-on-one hui for those based in Wellington, to outline the Government's proposals and assist iwi/Māori to make submissions.


Consultation

42. The following agencies have been consulted on this paper: the Department of Conservation; Energy Efficiency and Conservation Authority; Environmental Protection Authority; Ministry for Primary Industries; Ministry of Business, Innovation and Employment; Ministry of Foreign Affairs and Trade; Ministry of Transport; Office for Māori Crown Relations (Te Arawhiti); Te Puni Kōkiri; and the Treasury. The Department of Prime Minister and Cabinet was informed.

Financial Implications

43. Including agricultural processors in the NZ ETS will result in increased costs faced by farmers, growers and their families, given processors are likely to pass on the costs of an emissions price to their farm suppliers. The Government's proposal to provide 95 percent free allocation will help to mitigate potential negative social costs faced by farmers and their rural communities. As a result, the impact on pay-out to farmers is expected to be about \$0.01 per kg of milk solids, \$0.01 per kg of beef, \$0.03 per kg of sheep meat and \$0.04 per kg of venison. Costs per tonne of urea are estimated at \$2.92.
44. A processor-level price on agricultural emissions in the NZ ETS (with 95 percent free allocation) would generate approximately \$50m. Assuming the sector contributed this amount under a formal agreement, the same financial implications would arise.
45. Consultation with the public on the Government's proposals will provide a chance to hear from rural stakeholders and experts on risks and other potential impacts on rural communities, which will be factored into my advice to Cabinet seeking final policy decisions, including any legislative changes.

Legislative Implications

46. The proposals in this paper would require changes to the Act, as well as subsequent regulatory amendments. The breadth of changes will depend on final decisions taken by Cabinet in relation to the form and scope of the interim policy measure, which is yet to be decided.
47. section 9(2)(f)(iv)

48. I note more detailed legislative and regulatory amendments would also be required in 2022/2023 to give effect to farm-level pricing from 2025.

Regulatory Impact Analysis

49. The Regulatory Quality Team (RQT) at the Treasury has determined that the Interim Climate Change Committee's report and the discussion document will substitute for a Regulatory Impact Assessment. RQT is confident that the report and discussion document will together form a good basis for Cabinet deliberation and for consultation.
50. RQT notes the formal agreement option was proposed late in the policy development stage after an approach by members of the agriculture sector. The discussion document summarises the proposed action plan, but could be clearer about what is additional to Government commitments. If the sector's proposal is unclear, the discussion document could be transparent about this.

51. The option is also presented as an alternative to pricing agriculture emissions at the processor level in the interim period before 2025. The discussion document could consider whether there is a third option being to both price emissions and pursue a formal agreement in the interim period.
52. Notwithstanding consultation the Interim Committee has already undertaken, the proposed consultation period is very short for the public, iwi/Māori and industry to make meaningful submissions on what are relatively significant proposals. Such limited consultation might mean that the impact analysis of the final proposals presented to Cabinet is not sufficiently robust to help ministers to determine how best to meet the Government's objectives.

Crown-Māori Partnership

53. Iwi/Māori have significant interests in agribusiness and forestry, through both investment and settlement assets. Policies to address agricultural emissions could affect these investments, assets and interests in different ways. These potential impacts create identifiable Treaty of Waitangi obligations and risks.

54. section 9(2)h



55. section 9(2)h



56. section 9(2)h



Under the Ministry for the Environment's Te Ao Māori strategy, there will also be ongoing opportunities to engage with iwi/Māori through quarterly regional hui. This strategy will support the long-term work programme with iwi/Māori and the sector, including any specific engagement structures required.

57. In the proposed process leading to the introduction of a farm-level obligation, there would be further widespread consultation, including with iwi/Māori and agricultural groups. I note a farm-level obligation would have the potential to affect individual property owners far more than a processor-level obligation

would, and understanding respective viewpoints and options will be critical to good decision-making.

Human Rights

58. The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Gender Implications

59. There are no gender implications associated with this paper.

Disability Perspective

60. There are no disability implications arising from the proposals in this paper.

Publicity

61. There will be an announcement on consultation following Cabinet agreement to the proposals in this paper.

Proactive Release

62. I propose to release this paper proactively on the Ministry for the Environment's website in whole, subject to redactions as appropriate equivalent to those under the Official Information Act 1982, once public announcements have been made.

Recommendations

The Minister for Climate Change recommends that the Committee:

Establishment of the Interim Committee

1. **Note** the Interim Climate Change Committee (Interim Committee) was tasked with providing independent evidence, analysis and recommendations on how surrender obligations could best be arranged if methane and nitrous oxide emissions entered into the New Zealand Emissions Trading Scheme (NZ ETS);
2. **Note** that, in completing its deliverables, the Interim Committee considered the full suite of options to deliver efficient emission reductions in the agriculture sector that are consistent with the Government's objective for a just transition;

The Interim Committee's recommendations on agriculture

3. **Note** the Interim Committee's report (the report) makes the following recommendations for Government action on agricultural emissions:
 - 3.1. specify in law a farm-level levy/rebate scheme to price livestock emissions, with mandatory reporting by 2023 and obligations by 2025;

- 3.2. price livestock emissions in the NZ ETS at processor level in the interim;
- 3.3. price fertiliser emissions in the NZ ETS at processor level;
- 3.4. provide the assumed 95 percent rate of free allocation to offset the full impact of emissions pricing and support farmers in the transition;
- 3.5. establish an Agricultural Emissions Fund to recycle all funds back to mitigation, including a ring-fenced portion for iwi/Māori landowners and a Board with sector and iwi/Māori representation;
- 3.6. investigate opportunities to recognise and reward on-farm offsetting, including counting pre-1990 forests and small on-farm plantings; and
- 3.7. investigate opportunities to address non-climate regulatory barriers, stimulate innovation and create new markets for low-emissions products;

Government's response: a long-term transition to farm-level pricing

4. **Agree** to release the discussion document (Appendix 1), alongside the report and its technical appendices, for a short, focused consultation on Government's proposed response to the report's recommendations, including:

The long-term transition to farm-level pricing:

- 4.1. pricing livestock emissions in the NZ ETS at farm level from 2025;
- 4.2. pricing fertiliser emissions in the NZ ETS at processor level from 2025;
- 4.3. applying voluntary farm-level reporting in the NZ ETS from 2023 and mandatory farm-level reporting from 2024; and
- 4.4. requiring the responsible minister(s) to table a report in Parliament by 2022 on:
 - 4.4.1. whether farm-level pricing is feasible by 2025, and if not, whether processor-level pricing is necessary by default; and
 - 4.4.2. any other legislative and regulatory changes required;

An interim measure to incentivise livestock emissions reduction:

- 4.5. developing a joint action plan with the sector and iwi/Māori towards making a farm-level price workable and effective (including recognising and rewarding on-farm carbon removals), which could support either:
 - 4.5.1. Option A: pricing livestock and fertiliser emissions in the NZ ETS at processor level as soon as practicable (expected to enter into force from 2021); or
 - 4.5.2. Option B: developing a formal agreement with the sector that commits to reducing emissions and supporting the move to farm-level pricing;

A short, focused consultation on the Government's proposed response

5. **Note** Cabinet agreed to hold a short, focused consultation on the report to enable the New Zealand public and iwi/Māori to have their say [CAB-18-MIN-0542 refers];

6. **Note** a short, focused consultation is necessary to enable final policy decisions on agriculture to be included as part of the Climate Change Response Amendment Bill (CCRAB);
7. **Note** the Minister for Climate Change's intention for a short, focused consultation of four weeks to seek feedback on the proposals, including:
 - 7.1. a follow-up series of phone calls with iwi/Māori (and hui for those based in Wellington) to build on understanding and relationships established by pre-engagement and assist iwi/Māori to make submissions; and
 - 7.2. workshops with targeted stakeholders and interested public;
8. **Agree** to delegate authority to the Minister for Climate Change to make minor, editorial changes to the discussion document before consultation;

section 9(2)(h)

9. section 9(2)h

10. section 9(2)h

11. section 9(2)h

Legislative implications

12. **Note** the proposals in this paper would require changes to the Act, as well as subsequent regulatory amendments, which depend on the form and scope of the interim policy measure yet to be decided by Cabinet;
13. **Invite** the Minister for Climate Change to issue drafting instructions to the Parliamentary Counsel Office (PCO) on preparatory drafting options, as outlined in the proposals in Recommendations 4.1–4.5, to assist Cabinet decision-making after consultation;

DRAFT

Action on Agricultural Emissions:

A discussion document on policy proposals to address agricultural greenhouse gas emissions

This is not released under section 18(f) as this document is already available on our website. <https://www.mfe.govt.nz/sites/default/files/media/Climate%20Change/action-on-agricultural-emissions-discussion-document.pdf>

Appendix 2.

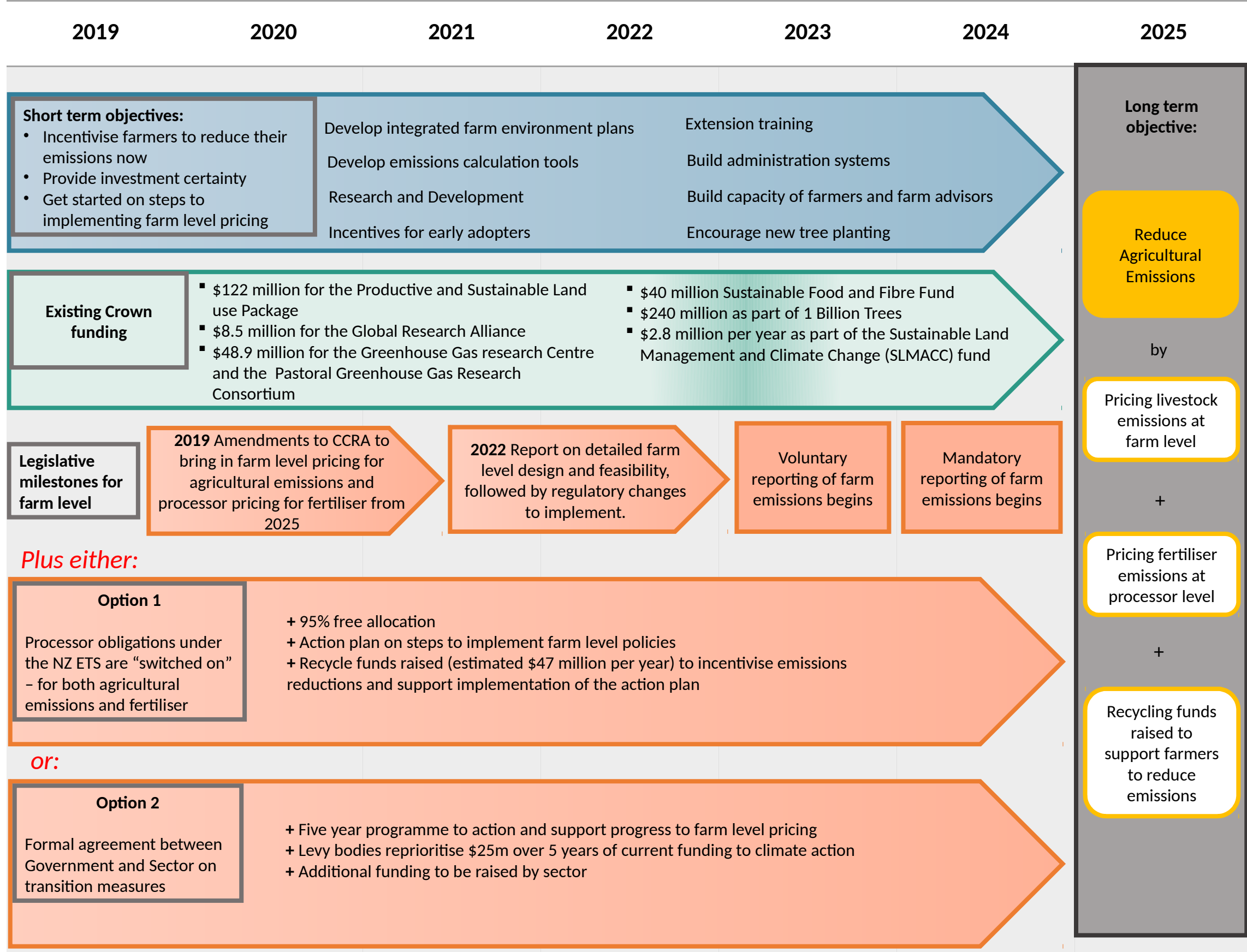
Further information on free allocation to agriculture at the processor level

1. Free allocation of units in the NZ ETS can offset the impacts of emissions pricing on the productivity, profitability and trade competitiveness of New Zealand's agricultural sector, as well as wider regional and distributional economic impacts.
2. The Interim Committee and officials advise me if agricultural emissions are included in the NZ ETS at the processor level, the only practical option available for introducing obligations in 2021 would be to allocate free units to processors who would be included in the NZ ETS, rather than directly to farmers.
3. The Interim Committee's report identifies two viable methods for free allocation at the processor level:
 - 3.1 output-based – where allocation is based on a processor's annual production multiplied by an allocation rate (e.g. 95 percent); or
 - 3.2 proportional – where allocation is simply a fraction of a processor's emissions.
4. Both the proportional and output-based methods result in similar incentives and cost impacts for processors (and, therefore, farmers). This is because at the processor level, both emissions and free allocation are calculated based on output, i.e. emissions per kilograms of milk solids, meat or fertiliser.
5. The one key difference with an output-based method of free allocation is that some processors may be able to work with farmers to undertake specific mitigation activities and gain the benefit from more accurate calculations through the use of Unique Emissions Factors (UEFs).¹ In this case, output-based allocation could differ from proportional allocation by providing some reward for changes in practices on farm that improve emissions intensity.
6. I propose to consult on the output-based method as the preferred option for processor-level allocation. I also propose that free allocation is provided only when the total emissions obligation is due and that any change to the level of free allocation over time should be informed by robust, objective analysis developed by the independent Commission. This was recommended by the Interim Committee and is being considered for industrial allocation as part of proposed changes to the NZ ETS consulted on recently.
7. I also propose, as recommended by the Interim Committee, that the Act set a process for updating livestock-related emissions and allocation factors in line with

¹ Processors could apply for a Unique Emissions Factor (UEF) upon demonstrating their emissions on average are lower than the national average emissions factor.

expected improvements in emissions intensity, with periodic reviews to account for less predictable changes in emissions intensity.

Action on Agricultural Emissions: proposals for consultation





Cabinet

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.

Report of the Cabinet Environment, Energy and Climate Committee: Period Ended 28 June 2019

On 1 July 2019, Cabinet made the following decisions on the work of the Cabinet Environment, Energy and Climate Committee for the period ended 28 June 2019:

out of scope	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]
[Redacted]	[Redacted]	[Redacted]

Portfolios: Energy and Resources / Environment

ENV-19-MIN-0039

**Consultation on the Government's Proposed
Action on Agricultural Emissions**

CONFIRMED

Portfolio: Climate Change

out of scope [Redacted]

[Redacted]

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[Redacted]

[Redacted]

[Redacted]

Michael Webster
Secretary of the Cabinet

Hard-copy distribution:
Cabinet Environment, Energy and Climate Committee



Cabinet Environment, Energy and Climate Committee

Minute of Decision

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Consultation on the Government's Proposed Action on Agricultural Emissions

Portfolio Climate Change

On 27 June 2019, the Cabinet Environment, Energy and Climate Committee:

- 1 **noted** that the Interim Climate Change Committee (Interim Committee) was tasked with providing independent evidence, analysis and recommendations on how surrender obligations could best be arranged if methane and nitrous oxide emissions entered into the New Zealand Emissions Trading Scheme (NZ ETS);
- 2 **noted** that, in completing its deliverables, the Interim Committee considered the full suite of options to deliver efficient emission reductions in the agriculture sector that are consistent with the government's objective for a just transition;

The Interim Committee's recommendations on agriculture

- 3 **noted** that the Interim Committee's report (the report) makes the following recommendations for government action on agricultural emissions:
 - 3.1 specify in law a farm-level levy/rebate scheme to price livestock emissions, with mandatory reporting by 2023 and obligations by 2025;
 - 3.2 price livestock emissions in the NZ ETS at processor level in the interim;
 - 3.3 price fertiliser emissions in the NZ ETS at processor level;
 - 3.4 provide the assumed 95 percent rate of free allocation to offset the full impact of emissions pricing and support farmers in the transition;
 - 3.5 establish an Agricultural Emissions Fund to recycle all funds back to mitigation, including a ring-fenced portion for iwi/Māori landowners and a Board with sector and iwi/Māori representation;
 - 3.6 investigate opportunities to recognise and reward on-farm offsetting, including counting pre-1990 forests and small on-farm plantings;
 - 3.7 investigate opportunities to address non-climate regulatory barriers, stimulate innovation and create new markets for low-emissions products;
 - 3.8 Government's response: a long-term transition to farm-level pricing

4 **agreed** to release the discussion document, in Appendix 1, to the paper under ENV-19-SUB-0039 subject to paragraph 8 below, alongside the report and its technical appendices, for a short, focused consultation on government's proposed response to the report's recommendations, including:

The long-term transition to farm-level pricing:

- 4.1 pricing livestock emissions in the NZ ETS at farm level from 2025;
- 4.2 pricing fertiliser emissions in the NZ ETS at processor level from 2025;
- 4.3 applying voluntary farm-level reporting in the NZ ETS from 2023 and mandatory farm-level reporting from 2024;
- 4.4 requiring the responsible minister(s) to table a report in Parliament by 2022 on:
 - 4.4.1 whether farm-level pricing is feasible by 2025, and if not, whether processor-level pricing is necessary by default;
 - 4.4.2 any other legislative and regulatory changes required;

An interim measure to incentivise livestock emissions reduction:

- 4.5 developing a joint action plan with the sector and iwi/Māori towards making a farm-level price workable and effective (including recognising and rewarding on-farm carbon removals), which could support either:
 - 4.5.1 Option A: pricing livestock and fertiliser emissions in the NZ ETS at processor level as soon as practicable (expected to enter into force from 2021); or
 - 4.5.2 Option B: developing a formal agreement with the sector that commits to reducing emissions and supporting the move to farm-level pricing;
- 4.6 a short, focused consultation on the government's proposed response:

5 **noted** that Cabinet agreed to hold a short, focused consultation on the report to enable the New Zealand public and iwi/Māori to have their say [CAB-18-MIN-0542];

6 **noted** that a short, focused consultation is necessary to enable final policy decisions on agriculture to be included as part of the Climate Change Response Amendment Bill (CCRAB);

7 **noted** that the Minister for Climate Change's intention for a short, focused consultation of four weeks to seek feedback on the proposals, including:

- 7.1 a follow-up series of phone calls with iwi/Māori (and hui for those based in Wellington) to build on understanding and relationships established by pre-engagement and assist iwi/Māori to make submissions;
- 7.2 workshops with targeted stakeholders and interested public;

8 **agreed** to delegate authority to the Minister for Climate Change to make minor, editorial changes to the discussion document before consultation, including proposed amendments from the Primary Sector Leaders Group that the Minister proposed to accept at the meeting;

section 9(2)(h)

9 section 9(2)(h)

10 section 9(2)(h)

11 section 9(2)(h)

Legislative Implications

- 12 **noted** that the proposals in the paper under ENV-19-SUB-0039 would require changes to the Act, as well as subsequent regulatory amendments, which depend on the form and scope of the interim policy measure yet to be decided by Cabinet;
- 13 **invited** the Minister for Climate Change to issue drafting instructions to the Parliamentary Counsel Office (PCO) on preparatory drafting options, as outlined in the proposals in paragraphs 4.1–4.5 above, to assist Cabinet decision-making after consultation;
- 14 **noted** that preparatory drafting does not pre-empt the consultation or final decision-making and is intended only to assist any potential drafting process if Cabinet decides to progress with legislative options after consultation;
- 15 **noted** that the Minister for Climate Change’s intention to return to Cabinet for final policy decisions on agriculture to be available in time for the beginning of the CCRAB Select Committee;
- 16 **noted** that more detailed legislative and regulatory amendments would also be required in 2022/2023 to give effect to the farm-level obligation from 2025;
- 17 **agreed** that the Minister for Climate Change may share this Cabinet paper, drafts of further Cabinet papers on related issues, drafting instructions to the PCO, subsequent drafts of amendments to the Act, and related documents, with the Environmental Protection Authority as a key agency under the Act.

Vivien Meek
Committee Secretary

Present:

Rt Hon Winston Peters
Hon Dr Megan Woods
Hon David Parker (Chair)
Hon Shane Jones
Hon James Shaw
Hon Eugenie Sage

Officials present from:

Office of the Prime Minister
Officials Committee for ENV

Hard-copy distribution:

Minister for Climate Change