

The Chair  
**CABINET POLICY COMMITTEE**

## **CLIMATE CHANGE: POLICY ISSUES FOR “ACT I” RATIFICATION LEGISLATION**

### **Proposal and Executive Summary**

1 This paper is the first in a series of four papers on the ratification of the Kyoto Protocol.

2 On 3 September 2001 Cabinet agreed to the adoption of a two-stage approach to Kyoto Protocol ratification, with passage of minimum legislation required for ratification (Act I) to be followed by the introduction, if possible prior to ratification, of legislation specifying detailed policy measures (Act II). (CAB min (01) 27/5A refers).

3 The minimum requirements for Act I ratification legislation are the creation of legal mechanisms, where they do not already exist, to allow for: a national registry to record holdings of emission units; a national inventory to record New Zealand's greenhouse gas emissions; and powers for the Crown to trade and manage holdings of emission units to meet New Zealand's obligations under the Protocol. The legislation will specify details of the powers, duties and responsible institutions necessary to implement these minimum requirements. As the choice of agency or agencies to carry out inventory and registry functions and Crown trading functions will have fiscal and institutional implications, officials are to complete further work on this and report back to POL by November 7.

4 It is proposed that drafting instructions for the Act I Bill for Parliamentary Counsel Office (PCO) are to be completed by 15 November following Cabinet decisions on institutional arrangements. Consultation on ratification, including the proposed content of the Act I Bill, is to be conducted from October to December. The decision on whether to ratify and proceed with Act I legislation will be informed by the result of this consultation, but it is likely that the actual content of Act I legislation will only be able to reflect consultation to the extent that the legislation can be amended during the parliamentary process. There is a very short timeline for the ratification process, and this is subject to the risk that criticisms of the consultation process and the content of legislation will lead to delays in select committee.

5 If the Government did nothing other than this legislation and did not utilise sink credits to cover the cost of excess emissions, there would be potentially significant fiscal implications arising from this legislation. However, the Government has signalled that it does not intend to rely on Act I only as it will put in place policy measures to manage emissions, which will be implemented using Act II legislation.

6 Although there are scenarios under the policy options being explored where the policy measures alone might not be sufficient to meet the Kyoto Protocol target, it is unlikely that there will be any fiscal liability to the Government. Most of the policy options under discussion involve some form of cost recovery and any residual fiscal risk can be dealt with through the use of sink credits to balance the remaining excess emissions. The Crown's Kyoto Protocol compliance requirements will need to be

considered as a factor when a decision is made on what proportion of sink credits are allocated to those undertaking sink activities, and what proportion is retained by the Crown. It should also be noted that allocation of a proportion of sink credits to those undertaking sink activities may result in significant tax revenue, depending on the proportion of sink credits allocated and their tax treatment.

7 It is expected that New Zealand as a whole will experience an increase in income from Kyoto Protocol ratification, as forest sink activities are projected to generate a substantial quantity of sink credits (about 110 million tonnes over 2008-2012), which is larger than projected excess emissions. This is discussed in more detail in the accompanying paper "Climate Change: Domestic Policy Options".

8 You are asked to: **direct** officials to report to POL by 7 November with a proposal inviting the Minister of Energy to issue drafting instructions to Parliamentary Counsel Office for an 'Act I' Climate Protection Bill for Kyoto Protocol ratification; **agree** to the proposed content of the legislation, **agree** to the proposed timeline and process for development of Act I legislation; **note** that the Act I Bill will be approximately 55 clauses and will be narrower in scope than the approved bid on the Government's legislative programme for a 120 clause Climate Protection Bill; **note** that officials will report back to POL by 7 November seeking approval for the institutional arrangements for the registry and inventory agencies and Crown trading functions; **note** that officials will report back on the fiscal implications for the institutional arrangements for the registry and inventory agency/agencies and Crown trading functions at the same time as approval is sought for the institutional arrangements themselves; **note** that when officials report back to POL by 7 November approval will be sought for any further policy decisions required for the issue of drafting instructions to Parliamentary Counsel Office; **note** the benefits of the Act I legislative process; **note** the risks of the Act I legislative process ; **note** the fiscal implications of compliance by means of Act I legislation only; and **note** that the policy options outlined in the accompanying policy options paper in most cases either provide a possible means for funding purchase of emission units for compliance requirements or devolve the role of purchase of emission units to the private sector.

## Background

9 On 3 September POL agreed to a staged approach to legislation to allow New Zealand to ratify the Kyoto Protocol by 2 September 2002. This will involve examination of a National Interest Analysis<sup>1</sup> by Parliament followed by introduction of the minimum legislation required for ratification (Act I) occurring broadly in parallel with further consultation on development of the domestic policy mix (CAB min (01) 27/5A refers). The legislation will contain the legal mechanisms required to enable the Crown to meet directly, and without devolution to other legal entities, legal obligations under the Protocol. Any legislation required to implement the domestic policy mix (Act II) would if possible be introduced prior to ratification.

10 This paper is the first in a series of four papers on the ratification of the Kyoto Protocol.

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<sup>1</sup> Standing Orders require the presentation of a National Interest Analysis to Parliament prior to ratification and, typically, the introduction of any legislation necessary to give effect to the obligations being entered into. The National Interest Analysis reports on the obligations being entered into and, among other things, the social, economic, environmental and cultural implications of ratification.

## Minimum Legal Requirements for Ratification

11 It is a well established constitutional practice that New Zealand only ratifies a treaty after it has in place the legislative and other measures that are necessary to enable full compliance with the Treaty once it enters into force for New Zealand. To allow ratification Act I legislation must, at a minimum, provide for all the measures required to implement the legal obligations of the Kyoto Protocol that are not provided for in existing New Zealand law.

12 Under the Protocol, the primary legal obligation is that the Government must demonstrate that emissions of greenhouse gases during 2008 – 2012 do not exceed New Zealand's total assigned amount (also referred to as emission units<sup>2</sup>). Under the Protocol, New Zealand has an initial quantity of emission units stemming from our target.<sup>3</sup> Additional units can be derived from forest sinks and from purchase of (or international trading in) emission units or through participation in project based activities recognised under the Protocol.<sup>4</sup>

13 In order to meet the obligations, legislation is required to enable New Zealand to achieve compliance. Initially, under Act I, the Crown will be responsible. Later, under Act II, the responsibility will be further devolved to include legal entities as well as the Crown. Stated another way, the Crown will be required to take responsibility for New Zealand's greenhouse gas emissions in excess of 1990 levels between 2008 and 2012. If our emissions exceeded our assigned amount, the Government would need to purchase emission units on the international market.

14 To quantify and to meet New Zealand's responsibility for emissions legal mechanisms must be available to implement the following:

- **Crown powers to trade** on the international market and to issue emission units, including sink credits, into the Crown's registry account. The Crown has a general legal authority to carry out commercial transactions in the national interest, however it is advisable to specify this responsibility and allocate it to a Minister in legislation.
- A **national inventory** to record New Zealand's total emissions of greenhouse gases and removals covered by the Protocol, and report data on emissions and removals.
- A **national registry** of emission units to record trading transactions and the amount of units held in accounts and report data on emission units. Following the first commitment period (in 2012) New Zealand is required to reconcile Crown holdings of units in the registry against national emissions as recorded by the inventory.

15 In addition to requirements relating directly to taking responsibility for emissions, New Zealand has a number of other obligations relating to provision of inventory reports and their verification internationally. Furthermore, before New

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<sup>2</sup> The term "emission unit" is intended to cover in an informal way the concepts of the assigned amount unit ("AAU"), the certified emission reduction unit ("CER") earned from clean development mechanism projects in developing countries, and the emission reduction unit ("ERU"), earned through joint implementation projects with other nations with targets under the Protocol. All of these units may be added together to determine whether New Zealand has sufficient assigned amount.

<sup>3</sup> New Zealand's initial assigned amount is equal to five times the 1990 level of emissions.

<sup>4</sup> Information collection and recording systems are also required to verify and account for assigned amount and emissions.

Zealand will be eligible to trade on the international market for emission units, the UNFCCC must be satisfied that New Zealand has established a valid registry and inventory system, and has adequately reported certain required inventory information prior to the first commitment period.

16 It should be emphasized that the details of the inventory and registry outlined above represent the minimum mechanisms required to implement Kyoto Protocol obligations prior to taking further necessary decisions in connection with Act II.

### **Scope of Act I Ratifying Legislation**

17 It is important to note that Act I legislation relates only to Crown management of responsibilities for and costs of Kyoto Protocol commitments, and does not provide for any devolution of responsibility and costs to sectoral and individual levels. Particularly, it should be noted that powers to issue sink credits into the Crown account are given in the context of the Crown's assumption of any liabilities that may arise for sinks, pending later measures in Act II to devolve sink benefits and obligations to entities.

### **Content of Proposed Ratification Legislation**

18 A legislative bid has been approved for a 120 clause Climate Protection Bill to be submitted to Parliamentary Counsel Office in November 2001. It is now proposed that the 'Act I' Climate Protection Bill be narrower in scope and contain approximately 55 clauses. Later approval will be sought for a place on the legislative programme for an 'Act II' Bill of approximately 80 clauses. It is proposed that the Act II Bill would take the form of an amendment to the Act I legislation.

### **Purpose and scope of legislation**

19 The opening provisions of the Act I Bill relating to purpose and scope will reflect that this Bill is the initial 'minimum' legislation for ratification. It is proposed to state that the purpose of the legislation is to give effect to New Zealand's international obligations under the United Nations Framework Convention on Climate Change (UNFCCC) and the Kyoto Protocol to that Convention. When the Bill is supplemented by a later amendment relating to domestic measures, the purpose and scope sections will need to be amended.

#### *Relationship to the Resource Management Act*

20 It is not necessary to have specific provisions on the interface with the RMA in Act I legislation as the only area of specific overlap will be in relation to the information-collection provisions of the Act I Bill. As discussed in Annex 2, inventory information collection provisions are to be developed to reduce this overlap.

#### *Provision for Negotiated Greenhouse Agreements (NGAs)*

21 The Government is at a preliminary stage in the process of developing negotiated greenhouse agreements, which will create obligations for participating firms to manage their greenhouse gas emissions prior to the start of the first commitment period under the Protocol. If a requirement to include recognition of NGAs in Act I arises during negotiations, it is possible that the legislation can be amended accordingly during the Parliamentary process. However, officials do not consider that it is appropriate to refer to NGAs in Act I legislation. If legislative recognition of NGAs are required it would be more appropriate to do this in the context of the policy package in Act II.

## **Crown Control of New Zealand's Compliance Equation**

22 To enable ratification, the Act I legislation must provide the Crown with sufficient powers to enable it to control and ensure New Zealand is able to meet its "compliance equation". More specifically, the Crown must ensure that at the end of the first commitment period<sup>5</sup>, New Zealand has a sufficient assigned amount to cover New Zealand's actual emissions of greenhouse gases. This may require the Crown to purchase emission units on the international market in or after 2012, if domestic measures have not reduced emissions to the level of Crown holdings by that time.

23 The legislation will provide that the Minister appointed by the Prime Minister with responsibility for New Zealand's compliance ("the Minister") will manage the Crown's holding of emission units on behalf of New Zealand. In accordance with international obligations, the Minister will issue the initial assigned amount into the Crown account in the registry, to be held as emission units.

24 The Minister will be able to add to or subtract from the assigned amount, in accordance with the international requirements, if New Zealand has increases or decreases in carbon sinks eligible for sink credits, and must add to or subtract from assigned amount where New Zealand buys, sells or cancels emission units.

25 The Minister will be able to buy and sell, or otherwise acquire or transfer, units on the international market, if it is necessary (this is unlikely as discussed in the fiscal implication section below. Transfer of units is restricted by the international requirement to retain sufficient holdings of assigned amount in the registry to comply with the "commitment period reserve". The commitment period reserve is the equivalent to the lower of 90% of the Crown's initial assigned amount or five times New Zealand's emissions in the most recent year for which a reviewed inventory is available. As a matter of policy, the Minister will not purchase emission units that have been derived from nuclear projects.

## **National Registry**

26 The legislation will provide for the establishment and maintenance of a national registry to ensure accurate accounting of the issuance, holding, transfer, acquisition, cancellation, retirement and carry-over of emission units. The establishment of the registry is a requirement of the Kyoto Protocol. Its primary function is to account for changes in New Zealand's assigned amount. A record of assigned amount is crucial for enabling New Zealand to demonstrate, internationally, compliance with its obligations under the Protocol (i.e. that New Zealand's greenhouse gas emissions do not exceed the assigned amount held in the registry). The choice of registry agency is discussed in the section on institutional arrangements for the registry and inventory below.

27 The form and content of the registry will be based largely on the technical guidelines that have been created under the Kyoto Protocol and will be supplemented by elements usual to our domestic registries. In particular, the register will be in the form of a standardised electronic database and a Registrar will be appointed to oversee the operation of the registry. The Registrar will have certain duties and powers, including the duty to record the issuance, holding, transfer, acquisition, cancellation and retirement of emission units, and carry over of emission units to subsequent commitment periods.

28 The legislation will provide for the Crown to hold at least one account to hold emission units at the registry. The legislation will also provide for other legal entities

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<sup>5</sup> 2008 - 2012

to have accounts at the registry, where authorised pursuant to certain criteria and procedure. Even without more general devolution under a domestic emissions trading regime, the Crown may wish to authorise certain legal entities to hold emission unit accounts.

29 See Annex 1 for a detailed exposition of the design of the registry.

## **National Inventory**

30 A national system for reporting greenhouse gas emissions and removals by sinks is required to comply with the Protocol. New Zealand is already required to report national inventory data under the UNFCCC to the extent that its capacities permit. The Ministry for the Environment (MfE) currently takes primary responsibility for reporting a national inventory of greenhouse gas emissions and removals by sinks to the Secretariat to the UNFCCC. The Ministry collects information from a variety of sources. This includes both mandatory and voluntary collection.

31 Although MfE already collates this information for the inventory, arrangements need to be formalised in Act I because:

- for ratification of the Protocol, there needs to be certainty that the information can continue to be collected and used for the purpose of reporting emissions and removals; and
- reporting requirements (including timelines and quality) under the Protocol will be stricter than under the UNFCCC.

32 The functions of the inventory agency in the Act I Bill will reflect international requirements. The primary function of the inventory is to estimate New Zealand's emissions by sources and removals by sinks of greenhouse gases covered by the Kyoto Protocol. The inventory will also be required to perform other functions such as: archiving test data, emission factors and other documentation; keeping records of changes that occur in the collection of data and use of methodologies and emission factors; implementing national verification systems; and co-operating with international review teams.

33 In addition to stating the functions of the national inventory in Act I legislation, the Act I legislation will also need to include:

- Data collection and monitoring provisions;
- Powers of the inventory agency (e.g. search and a limited power of seizure);
- Offence provisions and penalties; and
- Confidentiality of information provisions.

34 The nature of these provisions is outlined more fully in Annex 2. Appropriate regulation making powers are likely to be required, although the regulations themselves may not be needed until the Protocol enters into force.

## **International Reporting Requirements**

35 It is proposed that a Minister (the Minister) appointed by the Prime Minister will be responsible, in consultation with other relevant Ministers, for reporting of inventory and registry information required to the UNFCCC in accordance with international requirements. These include the requirement to report annually on changes in the national inventory system, changes in the national registry, and information regarding minimisation of adverse impacts on developing nation Parties under Article 3.14 to the Protocol. Importantly, New Zealand will also be required to report information on additions to and subtractions from assigned amount (including sink credits issued for forestry activities).

36 The Minister will also be required to direct the Registrar of the national registry to report information each calendar year on the total of each type of emission unit issued, acquired, transferred, cancelled, retired or carried-over.

## **Institutional Arrangements for the Registry and Inventory and Crown Trading Functions**

37 The choice of inventory and registry agencies may have significant fiscal and institutional implications. Inventory and registry functions are essentially separate, and it is possible to either establish a combined registry and inventory body or two separate bodies. Crown trading functions may also be delegated by the responsible Minister.

38 The broad options for choice of the inventory agency identified by officials to date are to: retain the functions within the Ministry for the Environment (with powers to use enforcement officers from other agencies); give the inventory functions to another Government department or crown entity; or create a new Government entity to act, inter alia, as the inventory agency.

39 The options currently identified for the registry agency are to use an existing government department (for instance, the Ministry of Economic Development) or, to establish a new Government entity or a new branch of an existing Government Department responsible for both inventory and registry functions.

40 Officials intend to complete further work on institutional arrangements and report back to POL by 7 November for approval in a separate paper prior to finalising drafting instructions for Act I legislation.

## **Process and Timeline for the Development of Act I Legislation**

41 A timeline for development of Act I legislation is attached as Annex 3. This is essentially the same as the timeline accepted by Cabinet in the September paper, "Climate Change: Next Steps for Ratification of the Kyoto Protocol". (CAB min (01) 27/5A refers), with the addition of further detail regarding report backs to POL for any decisions needed during the drafting process.

42 Consultation on matters relating to ratification, including on Act I legislation, will run from October to December and drafting instructions for Act I legislation will be sent to Parliamentary Counsel Office (PCO) by November 15. It should be noted that the consultation phase is likely to be largely independent of the development of drafting instructions, as PCO will start the drafting process for the Act I Bill before the end of ratification consultation. A Cabinet decision will be made in March 2002 on whether to ratify. This decision will be informed by consultation on the content of Act I legislation, within the broader ratification policy consultation. Scrutiny of the Bill during the select committee process will also be informed by this consultation.

However, given timing constraints it is likely that it will not be possible to amend the content of the Bill prior to introduction to the House to take into account the results of consultation. However, amendments could be made to the Bill during the parliamentary process, subject to limitations contained in Standing Orders of parliament, such as the requirement for amendments to be within the scope of the legislation introduced.

43 The development of Act I legislation is linked to consultation on the impacts of ratification, including the economic, social and cultural impacts of implementing Act I legislation. The NIA will also note the results of consultation on ratification and the proposed Act I legislation. Cabinet will be presented with a draft NIA when deciding whether to ratify. Select Committees must then consider the NIA prior to the introduction of the Act I Bill to Parliament.

44 Development of Act II domestic policy measures is intended to progress in parallel with the development of Act I legislation, with consultation on policy options commencing in October 2001. The Government will, if possible, introduce Act II legislation before ratification.

### **Legislation Process Benefits and Risks**

45 The adoption of a phased approach to ratification enables the minimum legislation required for ratification to be enacted in time for the World Summit on Sustainable Development in early September 2002, consistent with the Government's objective of displaying international leadership on climate change. A phased approach will also allow time for full consultation on later policy measures to be implemented under Act II legislation. The use of a phased approach to legislation is discussed in more detail in the September Cabinet paper "Climate Change: Next Steps for Ratification of the Kyoto Protocol" (CAB min (01) 27/5A refers).

46 The timeline for development of Act I legislation is very tight, with little room for slippage. A number of potential risks and criticisms will need to be addressed.

### **Criticism of ratification and process**

47 The Act I legislation and development process is likely to be subject to criticism on the following points:

- **Short timeframe for consultation.** There will only be one phase of two months consultation on the proposed content of the legislation.
- **Uncertainty regarding the future policy framework.** Stakeholders are likely to raise concerns that decisions to proceed with the ratification process are being made before the policy framework is known. It should be noted, however, that it is intended that by mid-March Cabinet will have released a second consultation paper on its preferred policy mix for consultation before the NIA and Act I Bill are introduced into the House.
- **Constraints on ability to modify legislation based on input from consultation prior to introduction.** As noted in paragraph 43 above, it is likely that there will not be an opportunity to amend the Act I Bill to take into account the results of consultation prior to its introduction to the house. It should be noted, however, that there is potential to modify the legislation during the select committee process.
- **General resistance to Kyoto Protocol ratification.** A number of stakeholders have expressed concerns about the potential costs of Kyoto Protocol ratification.

It is to be expected that there will be considerable opposition from some stakeholders during the select committee process. The Government will have an opportunity to respond to these concerns during the select committee process.

### **Risk of delays in Select Committee**

48 Following presentation to the House, the NIA will be referred to the Foreign Affairs Defence and Trade Select Committee for examination (which may refer it to another Select Committee). The Act I Bill should not be introduced until the relevant select committee has reported, or 15 sitting days have elapsed since the date of presentation, whichever is sooner.

### **Regulations Review Committee scrutiny**

49 The Regulations Review Committee will scrutinise regulation-making powers in the Bill, leading to possible delays.

### **Consultation**

50 The following Departments have been consulted and support the recommendations in this paper: The Ministries of Environment, Economic Development, Research Science and Technology, Agriculture and Forestry, Transport, Foreign Affairs and Trade and the Treasury. The Department of Prime Minister and Cabinet, Ministry of Justice and Te Puni Kokiri were also consulted in the preparation of this paper.

### **Treaty of Waitangi Implications**

51 Under Act I legislation the Crown will retain the benefits and obligations arising from Kyoto Protocol ratification. Act I does not devolve benefits or obligations to individuals and does not have effects on Māori that are likely to distinguish them from the population as a whole. Consequently, it is not proposed that reference be made to the Treaty of Waitangi in the Act I legislation. Policy options chosen for Act II legislation may have Treaty implications and would be subject to detailed consultation with Māori.

### **Fiscal Implications**

52 Work on the development of Act I legislation can be met through existing baselines. The institutional arrangements chosen for the registry and inventory and Crown trading functions would have fiscal implications. As noted in paragraph 41 above officials will report back to POL by November 7 on further work related to institutional arrangements, including fiscal implications.

53 If the Government did nothing other than this legislation and did not utilise sink credits to cover the cost of excess emissions, there would be potentially significant fiscal implications arising from this legislation. Current projections indicate that if New Zealand as a whole continues on its current emissions track total greenhouse gas emissions will be 14 -20% above 1990 levels during 2008-12. This equates to excess emissions of 50-75 million tonnes of carbon dioxide equivalent over these five years. However, New Zealand is expected to receive additional emission units from forest sinks (forests planted after 1990, - "Kyoto forests" - which absorb carbon dioxide) equivalent to around 110 million tonnes of carbon dioxide equivalent. Cabinet has previously agreed in principle that all or most of the sink credits derived from sink activities would be tradable within an international emissions trading market and noted that **some proportion** of the sink credits would go to those undertaking the sink activities. (Cab (00)M 25/4C refers).

54 The Government has signalled in previous policy decisions that it will put in place additional domestic policies to manage emissions. Some policies are already in place to reduce emissions, such as the National Energy Efficiency and Conservation Strategy, (which is expected to reduce up to 20 million tonnes of carbon dioxide) and funding for research on emission reductions. Final decisions on what further policies are required will be made after the two rounds of consultation planned over the next year. The policy options outlined in paper 2 of this series “Climate Change: Domestic Policy Options” provide a range of options for meeting the Crown’s Kyoto Protocol compliance requirements. These include:

- Government retaining responsibility for emissions and/or sinks.
- the provision of a possible means for funding purchase of emission units for compliance requirements (ie levies and emissions charges);
- the provision of incentives for emission reductions, thus reducing the quantity of emission units that would need to be purchased for compliance purposes (ie emissions charges, emissions trading and projects);
- the devolution of the responsibility to purchase emission units to the private sector (ie emissions trading).

55 Although most of these options have some level of cost recovery, there are scenarios under these options where the policy measures alone might not be sufficient to meet the crown’s obligation to ensure that the quantity of emission units corresponded to the quantity of emissions. There is also the possibility that lack of compliance with the requirements could lead to a residual liability for the Crown (i.e. the emitters do not pay the levy or the points of obligation default on their requirement to have sufficient emissions units to cover their emissions).

56 In such situations, Cabinet has previously noted that *some proportion* of the sink credits would go to those undertaking the sink activities (Cab (00)M 25/4C refers) – indicating that a proportion would therefore be retained in the Crown account. There has not yet been a decision about what this proportion will be. The Crown’s Kyoto Protocol compliance requirements will need to be considered as a factor when a decision is made on the proportion of sink credits that should be allocated to those undertaking sink activities. In making this decision, the Government would need to consider related issues, such as the level of incentives this provides and treatment of liabilities arising from retaining a proportion of sinks – such as forest fires. These liabilities may have fiscal implications.

57 In addition, allocation of sink credits to those undertaking sink activities may result in significant tax revenue, depending on the proportion of sink credits allocated and their tax treatment. A proportion of this value would be subject to taxation and would be available as revenue to the government. The amount of tax revenue generated will be highly dependent on issues of tax treatment, such as: the timing of realisation of income; the ability of credit holders to offset revenue from credits against other losses; and the availability of taxation offsets when forests are harvested.

58 Taking into account the discussion above, it is very unlikely that the Crown will suffer any net fiscal liability from this legislation.

## Recommendations

59 It is recommended that the committee:

- a) **direct** officials to report to POL by 7 November with a proposal inviting the Minister of Energy to issue drafting instructions to Parliamentary Counsel Office for an 'Act I' Climate Protection Bill for Kyoto Protocol ratification;
- b) **agree** to the content of the proposed legislation which will include provision for:
  - i. Crown powers to issue New Zealand's initial assigned amount, sink credits, and any other type of emission unit into the Crown account, and to acquire and transfer emission units;
  - ii. Establishment of a registry, in accordance with international requirements, to account for changes in New Zealand's holdings of emission units;
  - iii. Provision for legal entities other than the Crown to hold emission units in the registry, and for the acquisition and transfer of emission units by those entities;
  - iv. Establishment of an inventory to record New Zealand's greenhouse gas emissions by sources and their removals by sinks;
  - v. Sufficient inventory and registry agency powers to perform their functions, including data collection, monitoring, verification and search and seizure powers;
  - vi. Creation of offences and penalties for non-compliance with inventory and registry agency powers;
  - vii. Limited disclosure of private or confidential individual information held in the inventory or registry including for the purpose of complying with international requirements;
  - viii. Reporting to the UNFCCC by the responsible Minister, in consultation with other relevant Ministers, on inventory, registry and other information;
  - ix. Creation of necessary regulation making powers.
- c) **agree** to the proposed timeline and process for development of Act I legislation;
- d) **note** that the Act I Bill will be approximately 55 clauses and will be narrower in scope than the approved bid on the Government's legislative programme for a 120 clause Climate Protection Bill;
- e) **note** that when officials report back to POL by 7 November approval will be sought for any further policy decisions required for drafting instructions to be issued to Parliamentary Counsel Office;
- f) **note** that officials will report back to POL by 7 November seeking approval for the institutional arrangements for the registry and inventory agency/agencies;
- g) **note** the risks of the legislative timeline, namely:
  - i. criticisms of the ratification legislation and ratification process leading to delays in the select committee process; and
  - ii. Regulations Review Committee scrutiny.

- h) **note** the Government has signalled that it does not intend to rely on Act I only to meet Kyoto Protocol compliance requirements and that it will put in place policy measures to manage emissions, which will be implemented using Act II legislation. Paper II of this series “Climate Change : Domestic Policy Options” discusses these possible measures further [POL (01) 260 refers];
- i) **note** that, although most of the policy options under discussion involve some level of cost recovery, there are scenarios where the policy measures alone might not be sufficient to meet the Crown's obligation to ensure that the quantity of emission units corresponded to the quantity of emissions. In addition, there is also the possibility that lack of compliance with the policy measures could lead to a residual fiscal liability for the Crown;
- j) **note** that where the policy measures are not sufficient, or where there is a lack of compliance with the measures, any residual cost could be met through retained sink credits generated from Kyoto forests and potential tax revenues from sink credits;
- k) **agree** that the Crown's Kyoto Protocol Compliance requirements will need to be considered as a factor when a decision is made on what proportion of sink credits are allocated to those undertaking sink activities.
- l) **note** that the issues relating to the proportion of sink credits that are allocated or retained in the Crown account will be addressed as part of the policy options discussion and decisions over the next year.
- m) **agree** that the purpose of the legislation will be to give effect to New Zealand's international obligations under the United Nations framework Convention on Climate Change and the Kyoto Protocol to that convention.

Hon Pete Hodgson  
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## **ANNEX 1 – THE NATIONAL REGISTRY**

### **Appointment of the Registrar**

1 A Registrar of Emission Units will be appointed to maintain in New Zealand a register to be called the Register of Emission Units.

### **Form of the Register**

#### *Structure*

2 The register will be in the form of an electronic database. The structure and data formats of the register will conform to technical standards adopted under the Kyoto Protocol for the purpose of ensuring the accurate, transparent, efficient and secure exchange of data between national and other registries and the transaction log maintained by the UNFCCC Secretariat.

#### *Accounts*

3 The registry will have at least one holding account for the Crown, and one cancellation account and one retirement account for each commitment period. Each account will have a unique account number comprising the two-letter country code identifier for New Zealand and an account number unique to the New Zealand registry which will be assigned by the Registrar.

4 The registry will also have one holding account for each legal entity authorised by the Crown to hold units. The legislation will provide for such authorisation for entities either individually or as a class. The detail of any application procedure and the criteria for acceptance will be set out in regulation. Amongst other details, applicants will be required to provide contact details including their name, address, telephone number, fax number and email address.

#### *Units*

5 The register will record the holding in accounts of units created pursuant to the Kyoto Protocol. The legislation will define the ERU, CER and AAU. The legislation will provide that ERUs, CERs and AAUs are transferable and define the meaning of issuance, cancellation, retirement and carry-over and the procedure for each.

6 Each ERU, CER or AAU will be held in only one account in one registry at a given time. Once transferred to a retirement or cancellation account, an ERU, CER or AAU cannot be further transferred. ERUs, CERs or AAUs that have not been cancelled or retired may be carried over to a subsequent commitment period, provided that New Zealand is in compliance (i.e., has retired enough emission units to cover its emissions). Each AAU will have a unique serial number comprising a code for the commitment period, the two-letter country code identifier of the Party of origin, the type of the unit (i.e. AAU) and a number unique to the AAU for the commitment period and Party of origin which will be assigned by the Registrar, consistent with international requirements.

## **DUTIES, POWERS AND PROCEDURE OF THE REGISTRAR**

### **Transactions**

7 The Registrar will effect issues, transfers, acquisitions, cancellations, retirements, carry-overs and other transactions in accordance with the procedure for

the registration of transactions. The procedure and documentation for the registration of transactions by account holders and others will be prescribed by regulation where it is not otherwise dealt with under the primary legislation.

8 The Registrar will act on the direction of the Minister in certain circumstances in accordance with the international rules. For example, the Registrar must act on the Minister's directions to:

- record the issue of assigned amount into the registry as AAUs in accordance with international rules;
- record the issue of any additions to its assigned amount as a result of eligible sink activities in accordance with international rules;
- convert AAUs held by the Crown into ERUs (by adding a project identifier to the serial number and changing the type indicator to indicate an ERU) in accordance with international rules;
- cancel AAUs equivalent to any subtraction from its assigned amount, as a result of activities related to sinks in accordance with international rules, by transferring AAUs to its cancellation account;
- retire, by the compliance deadline, ERUs, CERs and AAUs for the purpose of contributing to its retirement amount in fulfilment of its commitment by transferring ERUs, CERs and AAUs.
- carry over ERUs, CERs and AAUs not held in the retirement account for their use in the second or subsequent commitment periods.

9 Where legal entities are authorised to hold accounts, the Registrar would act on the direction of an account holder to transfer units.

10 The transaction registration procedure will involve the following. The Registrar will create a unique transaction number for each transaction that originates from the New Zealand registry and must send a record of the proposed transaction to the independent transaction log operated by the UNFCCC Secretariat. The Registrar must terminate the transaction if the transaction log indicates a discrepancy according to the Protocol rules (for example, if the transaction results in a breach of New Zealand's commitment reserve).

## **Technical Matters**

11 A number of the technical requirements common to other domestic registries will also be included. For example:

- the Registrar will be empowered to delegate its functions, duties and powers to employees, or contract out the functions;
- the Registrar will be empowered to suspend the operation of the register if necessary;
- the register will be evidence of the ownership of emission units;
- provisions relating to the right of personal representatives and assignees in bankruptcy;
- transactions have no effect until registered;
- there will be a procedure relating to refusal by the Registrar to register non-complying documents;
- there will be a procedure allowing for the correction of the register, for example as a consequence of international review;
- provisions relating to dealing with the mistakes or abuses of the system by the Registrar;

## **Provision of Information**

12 The registry will record all information required by the Kyoto Protocol (and certain other information that may be required domestically). Subject to final decisions on the institutional design of the registry, the Privacy Act 1993, the Official Information Act 1982 and Ombudsmen Act 1975 will probably apply to information in the registry. The registry will provide a publicly accessible user interface through the internet that allows interested parties to query and view it. The legislation will set out the circumstances where confidential or private information (if any) about companies and individuals may be released – for example, as required under international obligations or for the purposes of prosecution.

13 The information recorded will include for each account number: the name of the holder of the account; the type of account; the commitment period with which a cancellation or retirement account is associated; the representative of the account holder using the two-letter country code identified and a number unique to that representative; the full name, mailing address, telephone number, facsimile number and email address of the representative of the account holder.

14 For any Joint Implementation projects undertaken within New Zealand, the registry will also record information relating to projects including the unique name for the project; the country and town or region in which the project is located; the years in which units have been issued as a result of the project; a link to the downloadable electronic versions of all documentation relating to the project, including proposals, monitoring, verification and issuance of emission units where relevant, subject to confidentiality provisions contained in the Kyoto Protocol.

15 Finally, holding and transaction information relevant to the registry, by serial numbers, for each calendar year, will be recorded. A list of legal entities authorised to hold units within the New Zealand registry must also be included.

## **Offence Provisions and Penalties**

16 The Registrar (depending on final institutional arrangements) will be granted powers to enable it to perform its functions under the legislation. The legislation will provide for account holders to be liable for offences and corresponding penalty provisions for non-compliance with the registry provisions. Officials will give further consideration to the scope of offence provisions, and what coercive powers are required by the Registrar, and report back to POL on these matters by 7 November.

## **Miscellaneous**

17 Further provisions will be included in the legislation to provide for any technical or other details required to enable New Zealand to meet its international obligations. (which are expected to be finalised at the Conference of the Parties to the Protocol in November 2001). These and further technical provisions may be included in regulations.

## ANNEX 2 – THE NATIONAL INVENTORY

### Data collection and monitoring

1 It is proposed that the exact identification of the persons required to supply information, and the type of information which persons must supply, would be specified in regulations. The Bill would set out broadly the boundaries of the regulation-making power, for example using a generic list of information types. The regulation-making power will need to be broad because the inventory needs information on a number of matters and from a number of different sources. For example, information on:

- (a) direct emissions data;
- (b) volumes of fuel used;
- (c) volumes of fuel sold;
- (d) manufacturing processes, including by-products from manufacturing processes;
- (e) composition of the vehicle fleet;
- (f) the import and manufacture of products such as fridges, inhalers and solvents, and information e.g., from retailers on the end-uses of these items;
- (g) waste composition, volume, amount of landfill gas extracted and combusted;
- (h) vegetation and soil compositions;
- (i) numbers of ruminants and other farmed livestock, areas of crops and amounts produced, amount of nitrogenous fertilisers used.

2 Some information on greenhouse gas emissions and removals by sinks is already collected under other legislation such as the Resource Management Act 1991, the Forests Act 1949, the Customs and Excise Act 1996. It is not desirable to require persons to submit information twice. To avoid overlap, it is proposed that before making regulations the Minister must consider the following:

- whether the information is reasonably available to the inventory by other means, such as by voluntary collection, or by co-operation with another agency that already collects the information (e.g. local authorities holding emissions data under the Resource Management Act 1991)<sup>6</sup>;
- deficiencies with collecting the information using those other means, such as deficiencies in obtaining the required quality information and lack of certainty that the information will be provided.

3 It is proposed that the categories of persons who could be required to provide information to the inventory under regulations would include local authorities.

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<sup>6</sup> Before obtaining information from other agencies, the Inventory would need to be satisfied that the transfer of information from that other agency would not breach Privacy Act and confidentiality principles.

## **Powers of the inventory agency (search and limited powers of seizure)**

4 It is proposed that self-reporting under the regulations would be supplemented by powers of search and seizure, and corresponding offence provisions, if the correct information is not provided.

5 Powers of search and a limited power of seizure are needed to ensure compliance with statutory requirements regarding the provision of information. These powers would be needed, for example, to take samples of direct emissions, in order to check whether a company has correctly reported their emissions to the inventory. It is envisaged that officers of the inventory agency will need powers to:

- enter land or premises;
- inspect the land or premises, including inspecting documents and business records (and to require production of such documents and records);
- copy written information and electronically stored data (with an additional provision to seize electronic data storage media to recover erased data, under tightly specified circumstances);
- carry out surveys, investigations, tests or measurements, and take samples.

6 There will be the usual safeguards on the exercise of these powers, such as carefully prescribing the purpose for which the powers can be exercised (for reporting under the UNFCCC and the Kyoto Protocol), reasonable notice to be given to landowners, entry at reasonable times, and the need to produce authorisation for entry if requested (the exercise of the more invasive powers would require warrants issued under judicial authority).

## **Offence Provisions and Penalties**

7 Offences would include failure to provide information, providing incorrect information, and any obstruction or failure to provide documents or property for inspection when required. The person would have a defence if they had taken reasonable steps to provide the correct information.

8 Penalties would be monetary fines up to a maximum amount specified in the legislation. The maximum penalty would be \$2,000 for a person and \$12,000 for a company.

9 It is proposed that the enforcement functions would be undertaken under the auspices of the inventory agency (perhaps using enforcement officers from another agency, depending on the final institutional arrangements). The legislation would provide for prosecutions to be adjudicated at the District Court, with appeal to the High Court.

## **Privacy and the confidentiality of Information**

10 The legislation will set out the circumstances where individual information (information about individual companies and persons) may be released. This is important because some information may be commercially sensitive. Generally only the employees of the inventory will be permitted to see individual information. In any publication, information must be arranged in such a way that *individual* information will not be able to be identified. However these principles will be overridden in certain situations:

- Information can be published in such a way that individual information is identifiable where international obligations require publication in that way (this

may occur in sectors with a small number of firms), or where use of this information is necessary for the purposes of continuing international negotiations under the UNFCCC or Kyoto Protocol;

- Individual information can be made available to members of any international expert review team acting under Article 8 of the Kyoto Protocol; and
- Individual information can be disclosed for the purposes of a prosecution or proposed prosecution.

## ANNEX 3 – TIMELINE FOR DEVELOPMENT OF ACT I LEGISLATION

Ratification/legislation (stage I)	Time allowed	Deadline
Cabinet papers on: the ratification legislation, including authority to prepare drafting instructions and consultation document	2 months	15 Aug – 12 Oct 2001
<b>Consultation</b> on ratification	2 months	15 Oct – 15 Dec 2001
Officials prepare drafting instructions	1 month	15 Oct - 15 Nov 2001
Reports back to POL on: institutional arrangements for the registry and inventory; and on further decisions required for drafting instructions	3 weeks	15 Oct - 7 Nov 2001
PCO drafting of ratification legislation	3 months	15 Nov - 15 Feb 2001
Submissions analysis, completion of NIA and development of Cab paper	1.5 months	15 Dec 2001 – 15 Feb 2002
Cabinet approval of draft legislation for introduction/approval of NIA and <b>decision on whether to ratify,</b>	1 month	15 Feb – 15 Mar 2002
<b>Introduction of NIA</b> and examination by Select Committee	2 months	15 March - 15 May
Caucus/ <b>introduction of legislation</b> into house/1 <sup>st</sup> reading and referral to Select Committee	-	By 15 May 2002 (15 sitting days after presentation of NIA or report back from select committee)
Select Committee - (submissions, hearings, deliberation report back)	2.5 months (+)	By 15 May – 1 Aug 2002
Second reading	1 week	8 Aug 2002
Committee of the whole/Third reading	1 week	14 Aug 2002
Enact	-	Late Aug 2002
Prepare and transmit instrument of ratification to depositary	1 week	Late Aug 2002
World Summit on Sustainable Development	-	2 Sep – 11 Sep 2002

