



Cabinet Legislation Committee

Minute of Decision

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Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Bill - Approval for Introduction

Portfolios **Forestry / Climate Change**

On 24 November 2022, the Cabinet Legislation Committee:

- 1 **noted** that the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Bill (the Bill) will amend industrial allocation policy in the New Zealand Emissions Trading Scheme (NZ ETS);
- 2 **noted** that in June 2022, the Cabinet Economic Development Committee (DEV) agreed to update and increase the accuracy of the way the government allocates free units under the NZ ETS to emissions intensive and trade exposed firms [DEV-22-MIN-0159];
- 3 **noted** that based on the policy decisions made by DEV in June, the Bill:
 - 3.1 enables a review and update of allocative baselines using new base years, and the framework for potential updates in the future;
 - 3.2 enables a reassessment of the eligibility for industrial allocation using new base years, and updated emissions intensity thresholds;
 - 3.3 updates some technical areas of industrial allocation policy, including the modelling framework for the electricity allocation factor, amending the eligibility process for new activities, simplifying the process for updating allocative baselines, and enabling easy access to information submitted to the Environmental Protection Agency;

Additional policy decision for new activities' eligibility process

- 4 **noted** that policy decisions taken by DEV in June allow new activities existing after the financial year 2020/21 to seek eligibility via the assessment of criteria under section 84C(3) of the Climate Change Response Act 2002 (the Act);
- 5 **noted** that the intent of using these criteria is to provide a more rigorous test for prospective activities to ensure eligibility for industrial allocation is weighed against both the risk of emissions leakage and meeting New Zealand's broader climate goals;
- 6 **noted** that a level of assistance (percentage of emissions costs covered by industrial allocation) and a new activity's allocative baseline are both required for calculating the industrial allocation to a firm undertaking a new activity;

- 7 **noted** that criteria in section 84C(3) of the Act cannot be used to calculate an activity's level of assistance or allocative baseline because new activities will not have actual emissions, production, or revenue data needed to determine them;
- 8 **agreed** to retain the emissions intensity and trade exposure test for the purpose of new activities seeking eligibility;
- 9 **agreed** that the Minister of Climate Change will still be required to assess the criteria of section 84C(3) of the Act in addition to the emissions intensity and trade exposure test for determining the eligibility of a new activity;
- 10 **agreed** that any new applicant must provide projections of its expected annual emissions costs, production, and revenue, to enable a tentative calculation of both their emissions intensity for the purpose of eligibility and its allocative baseline(s)
- 11 **agreed** that if a new activity is found to be eligible, the initial level of assistance will be set at the moderately emissions intensive level, subject to the relevant phase-out rate;
- 12 **noted** that applicants carrying out a new eligible activity are entitled to receive a final allocation for the relevant year and a provisional allocation for the following year;
- 13 **agreed** that for any new activity, a specified amount of actual financial-year data must be provided before a specific period of operation is complete (amounts and periods to be specified by the Minister) to:
- 13.1 inform a reassessment of emissions intensity against the emissions intensity thresholds; and
- 13.2 recalculate the allocative baselines as appropriate;
- 14 **agreed** that the activity's eligibility (and therefore the appropriate level of assistance), and its allocative baseline(s) will be updated using actual data;
- 15 **agreed** that if the new activity was found to be ineligible based on actual data – any firm undertaking the activity would be liable to repay the units received to the Crown;
- 16 **agreed** that if the new activity is found to remain eligible but has been under or over-allocated, a wash-up will occur which requires firms undertaking the new activity to either repay units received to the Crown, or the Crown to allocate more units;
- 17 **noted** that subject to your agreement, the Bill enables this process for assessing eligibility for new activities;
- 18 **noted** that the Bill will introduce a new penalty that will apply to forestry participants in the NZ ETS with low volume liabilities of less than 25,000 units on average per year (small forestry participants) who fail to surrender or repay units by the due date for liabilities occurring from 1 January 2025, and that the new penalty is:
- 18.1 a strict liability penalty that may be waived by the EPA where 'total absence of fault' applies;
- 18.2 set at half the price of carbon (as set in regulations) for each unpaid unit.
- 18.3 halved for small forestry participants who deforest pre-1990 forest land;

- 19 **noted** that the Bill will also make minor amendments to the legislation to clarify how the penalty will apply in practice, and that these amendments are:
- 19.1 where a participant files an emissions return containing part-years, that part-years will be treated as full years for the purpose of calculating whether a liability exceeds the 25,000 unit threshold, rather than pro-rating this threshold across part-years;
 - 19.2 where an emissions return that has already received a penalty notice relating to the new penalty is amended by the regulator to correct a unit obligation, and a subsequent penalty is incurred for any additional units owing as a result of the amendment, the subsequent penalty will be based on the subsequent unit amount only for the purpose of determining whether the liability exceeds the 25,000 unit threshold;
 - 19.3 where an emissions return covers activities occurring both before and after 1 January 2025, to prevent situations arising where two different penalty regimes apply to a single emissions return, the excess emissions penalty currently in place under the transitional arrangement will apply to the entire emissions return, meaning it will effectively be extended to activities occurring up until 31 December 2025;
- 20 **noted** that policy decisions made on the new penalty (paragraph 18) and legislative clarifications (paragraph 19) were agreed by a sub-group of Ministers (Minister of Forestry, Minister of Climate Change, Minister of Finance and Minister for the Environment), given delegated authority for that purpose by ENV [ENV-22-MIN-0029];
- 21 **noted** that the transitional arrangement currently in place for small forestry participants who fail to surrender or repay units by the due date is being extended to cover liabilities from forestry activities occurring up until 31 December 2024, and that this process is underway separately via the Climate Change Response (Extension of Penalty Transition for Forestry Activities with Low Volume Emissions Liabilities) Amendment Bill 2022, which was introduced into the House on 4 October 2022;

Additional policy decision to extend legislative clarifications

- 22 **noted** that the Bill will make minor amendments to the legislation to clarify how the penalty will apply in practice, including how the 25,000-unit penalty threshold applies to forestry participants who submit emissions returns containing part-years, and incorrect emissions returns (paragraphs 19.1 and 19.2 above);
- 23 **agreed** to extend these minor and technical clarifications to apply to the provisions giving effect to the transitional arrangement, effective from the day after the Bill receives Royal assent (applicable to penalties issued from this date onwards, including penalties relating to forestry activities carried out prior to this date), these amendments are:
- 23.1 where a participant files an emissions return containing part-years, that part-years will be treated as full years for the purpose of calculating whether a liability exceeds the 25,000 unit threshold, rather than pro-rating this threshold across part-years;
 - 23.2 where an emissions return that has already received a penalty notice relating to the 'excess emissions' penalty is amended by the regulator to correct a unit obligation, and a subsequent penalty is incurred for any additional units owing as a result of the amendment, the subsequent penalty will be based on the subsequent unit amount only for the purpose of determining whether the liability exceeds the 25,000 unit threshold;

- 24 **noted** that the Ministers will seek to implement these clarifications through the Select Committee process or through a Supplementary Order Paper;
- 25 **approved** the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Bill [PCO 24947/2.0] for introduction, subject to the final approval of the Government caucus and sufficient support in the House of Representatives;
- 26 **agreed** that the Bill be introduced in early December 2022 and referred to select committee before the end of year recess;
- 27 **agreed** that the government propose that the Bill be:
- 27.1 referred to the Environment Select Committee for consideration;
 - 27.2 reported back by 2 May 2023;
 - 27.3 enacted by 1 July 2023.

Rebecca Davies
Committee Secretary

Present:

Hon Chris Hipkins (Chair)
Hon Poto Williams
Hon Dr David Clark
Hon Kieran McAnulty
Dr Duncan Webb, MP

Officials present from:

Office of the Prime Minister
Officials Committee for LEG