

The Chair
Cabinet Policy Committee

CLIMATE CHANGE: INSTITUTIONAL ARRANGEMENTS FOR INVENTORY, REGISTRY AND CROWN TRADING FUNCTIONS

Introduction and executive summary

1 On 3 October 2001 POL noted that officials will report back to POL by 7 November 2001 seeking approval for the institutional arrangements for the registry and inventory agency/agencies. POL also directed officials to report back by 7 November with a proposal inviting the Minister of Energy to issue drafting instructions to Parliamentary Counsel Office with a proposal for an Act I Climate Protection Bill for ratification of the Kyoto Protocol.

2 The national inventory system records and reports information on New Zealand's greenhouse gas emissions and removals. The national registry records holdings and trading of emission units. The Kyoto Protocol and accompanying guidelines require that parties to the Protocol have in place appropriate institutional arrangements for the performance of inventory and registry functions. Officials also consider it desirable to allocate to a particular institution the function of Crown trading of emission units (although this is not a requirement of the Kyoto Protocol).

3 Officials recommend that for the time being, the following institutions perform the inventory, registry and Crown trading functions for Act I. These functions may be reviewed after introduction of Act II legislation, which will set out the specific domestic policies to meet obligations of the Kyoto Protocol:

- Inventory function: Ministry for the Environment
- Registry function: Ministry of Economic Development
- Crown trading function: Treasury

4 This paper also recommends that Cabinet invite the Minister of Energy to issue drafting instructions to Parliamentary Counsel Office with a proposal for an Act I Climate Protection Bill for ratification of the Kyoto Protocol. Cabinet has agreed to the content of the proposed legislation (refer CAB(Min (01) 31/12), and decisions requested in this paper will enable drafting instructions to be completed.

Significance of institutional arrangements

5 Under the Kyoto Protocol New Zealand will have to pass an international review of its inventory and registry systems before it will be eligible to trade on the international market for emission units, and will have to pass annual reviews during the first commitment period.

There is also a requirement that New Zealand must adequately report certain required inventory information prior to the first commitment period.

6 The consequences of non-compliance with inventory and registry requirements would be substantial. Failure to fulfil international requirements would leave the Crown unable to trade on the international market meaning that the Crown could not ensure compliance by purchasing sufficient emission units to cover New Zealand's emissions. This indicates the need for well-defined institutional arrangements with clear allocation of powers, responsibilities and funding.

Guiding principles

7 In identifying the appropriate body or bodies to undertake the performance of inventory, registry and Crown trading functions, it is necessary to take into account:

- mandatory requirements of the Kyoto Protocol and guidelines;
- the need for appropriate flows of information between the inventory and registry and Crown trading agency;
- the need for flexibility to allow for possible extensions to the activities of the agencies under later Act II domestic policy measures;
- characteristics of the proposed institutions which are desirable as a matter of policy (having regard to principles regarding the design of public bodies in New Zealand developed by the State Services Commission (SSC) and Legislation Advisory Committee (LAC)).

Required institutional functions under the Kyoto Protocol

Inventory

8 Under guidelines to the Kyoto Protocol a single agency must be designated as responsible for inventory functions. The primary function of the inventory agency will be to estimate on an annual basis New Zealand's anthropogenic emissions by sources and removals by sinks of greenhouse gases not controlled by the Montreal Protocol. Inventory activities specified in Kyoto Protocol guidelines include collecting emissions data and data on industrial processes; processing the data using accepted methodologies; compiling and publishing reports; maintaining archiving and record-keeping systems; and co-operating with international review teams.

9 The inventory agency will also have a policy role in advising when regulations should be made to collect certain data (where voluntary collection, or collection via another agency, is not a viable way of collection).

10 In order to fulfil information-collection functions, the inventory agency will require powers of search and seizure, and the ability to initiate prosecutions. More specifically, the inventory agency will require powers to (refer CAB(Min (01) 31/12)):

- 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);
- seize documents and equipment;
- carry out surveys, investigations, tests or measurements, and take samples.

Registry

11 Guidelines under the Kyoto Protocol require parties to the Protocol to have a national registry. The guidelines prescribe in detail the required features of national registries, in particular for compatibility with an international trading system through features such as a standard transaction log. Under the guidelines, the main task of the registry is to record the issuance, holding, transfer, acquisition, cancellation, retirement and carry over of emission units. A record of emission units is crucial for enabling New Zealand to demonstrate, internationally, compliance with its obligations under the Protocol (ie that New Zealand's greenhouse gas emissions do not exceed emission units held in the registry). The guidelines set out minimum requirements as to the information the registry must hold about accounts and units. The registry must take the form of an electronic database and be accessible through the internet.

Crown Trading Functions

12 There is no direct Kyoto Protocol requirement to appoint a responsible institution for Crown trading of emission units. However officials consider, given the fiscal significance of this function, that it is important for legislation to name a responsible Minister and agency to carry out Crown trading.

13 Emissions trading will take place in both "primary" and "secondary" markets (using both emission units and derivative instruments such as emission unit futures). Trades can take place either "over the counter" (bilateral trades of emission units between institutions) or through an organised exchange, and must be notified to the registry.

Desirable characteristics of the inventory, registry, and body entrusted with Crown trading functions

14 Ideally both the inventory and registry would:

- have operational independence from the Minister, at least in the performance of core functions (i.e. the day to day functions of the inventory and registry would not be influenced by the Minister);
- be subject to normal public accountability mechanisms such as the Auditor-General, Ombudsmen, Official Information Act 1982 and annual reporting to Parliament;
- enjoy the confidence of the public and businesses with whom each organisation interacted;

- operate efficiently and at a minimum cost on general taxation (and thus be able to recover costs where possible).

15 In the performance of the inventory and registry functions, the government is acting in a regulatory capacity. By contrast the performance of the Crown's trading function is subject to slightly different considerations. Ideally the body carrying out this function would be:

- experienced in managing fiscal and trading risk to the Crown (e.g. through experience in forecasting and in trading in markets analogous to the international market for emission units or derivatives markets);
- experienced in forecasting and assessing the risks and benefits of keeping reserves or managing the banking of any emission units over several commitment periods.

16 The inventory, registry, and Crown trading functions are clearly functions of executive government. Guidance on whether a public function is best performed by a department of state, Crown entity, state owned enterprise or office of Parliament is provided by SSC and LAC guidelines. Officials have applied those guidelines and narrowed the possible options for the functions to a Crown entity or a government department.

17 This government has previously made some decisions on Crown entity reform that were predicated on using departments to perform the functions of executive government unless there was a compelling case to use a Crown entity. Those decisions were put on hold pending the resolution of other issues, but it was agreed that proposals for establishing new entities would be referred to the Minister of State Services and that his officials would review proposals in light of the on-hold decisions. The advice of SSC officials is that, in this case, none of the grounds for using a Crown entity applies. Accordingly, they recommend that the functions be assigned to one or more departments. Application of the LAC guidelines supports the conclusion that the departmental form is appropriate at this stage.

Should one department or several perform these functions?

18 A number of considerations bear on whether to co-locate the functions or to assign them to different departments. There are possible synergies and cost-savings to be gained by co-locating functions. These include the sharing of work functions and infrastructure such as electronic systems, and better information flows between the functions. These issues are discussed below in paragraphs 20-23.

19 Officials have concluded that assigning the 3 separate functions to separate organisations would allow better advantage to be taken of existing capabilities. As no existing department currently performs the complete range of inventory, registry and trading functions, co-locating functions would involve conferring a new type of function or functions on an existing department, or creating a new department performing all three functions. Both these options would involve significant set-up costs.

Sharing work functions/ infrastructure

20 The inventory, registry and Crown trading functions are fundamentally separate functions. The degree of direct overlap possible between the functions is limited by the different skills required for the performance of each function. Any cost savings that can be gained through work sharing between the functions are likely to be limited. There may be opportunities to

make savings, however, through sharing necessary infrastructure, and in the development and maintenance of infrastructure such as electronic information systems. It is difficult to make an assessment of the potential for savings from co-location through shared infrastructure and development until work on the functions progresses further, and until the full extent of agency functions becomes clear following decisions on Act II policy measures in July next year.

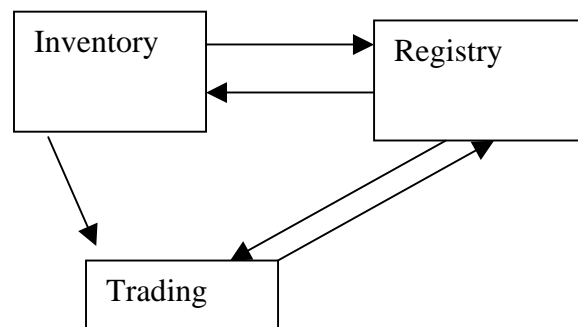
Information flows

21 There are a number of potential information flows under Act I legislation. If the functions are separated, information will have to flow between the responsible agencies for each function to be effectively performed. The primary flows of information are likely to be:

- a two-way flow between the registry and the body undertaking the Crown's trading function. The registry would inform the latter of the Crown's holdings of units on the international market, while the body undertaking the Crown trading function would advise the registry of any transactions it wished to undertake;
- a one-way flow between the inventory and the Crown trading function, to inform the latter of potential Crown liability in terms of national emissions.

22 Under a system of domestic emissions trading additional information flows would be required between:

- the inventory and the registry, the former providing the latter with information on emissions or sink activities of a particular account holder over a given period such as a year;
- the registry and the inventory as information about an entity's holding of units is passed back in the event of non-compliance to allow the inventory to take any necessary enforcement action.



23 The key issue is ensuring the effective flow of information between the 3 functions. There is no *a priori* reason to believe that co-location itself would address this issue. Even if inventory, registry and Crown trading functions were co-located in one department, boundaries would need to be established between the functions to ensure public confidence in the fairness and impartiality of the registry and inventory agencies. This means that, even for co-location of functions, systems would need to be put in place for effective information flows.

Choice of Agencies for institutional arrangements

24 Officials have assessed a range of different agencies and concluded that, pending any reconsideration by officials of institutional arrangements which might be necessitated by Act II policy measures:

- The Ministry of Economic Development should take the registry function,
- The Ministry for the Environment should take the inventory function,
- Treasury should have the crown trading function.

A discussion of the best agencies for the different functions is provided below.

Registry – Ministry of Economic Development

25 Agencies assessed for the registry function included:

- Land Information New Zealand (LINZ)
- The Land transport Safety Authority (LTSA)
- Ministry for the Environment (MfE)
- Department of Conservation (DoC)
- Ministry of Economic Development (MED)

26 Although the first two have experience in registry services, these are specialist registries. It would seem incongruous for such tightly focused agencies to "tack on" a registry function unrelated to its existing business areas. Although MfE and DoC are experienced in inventories, they have no experience running registries.

27 Of the Departments surveyed for the registry function MED has the deepest and broadest experience in the provision of registries, which could be harnessed if the emission units registry were to be located within this ministry. An additional registry is compatible with the Ministry's core functions, which now include the specialist provision of registry services. Accordingly, officials recommend that for the time being MED be named as the agency responsible for the registry function.

28 The inventory agency must be named in Act I legislation for constitutional reasons as it has significant powers of enforcement and compliance. Agencies assessed for the inventory function include:

- Department of Conservation (DoC),
- Statistics New Zealand
- Ministry of Agriculture and Forestry (MAF)
- Ministry of Economic Development (MED)
- Ministry for the Environment (MfE)

29 In the first four cases, although each has experience in one type of inventory, they would all require additional institutional adjustments and experience to accommodate the range of information that needs to be collected for the climate change inventory.

30 Officials recommend that for the time being MfE be named in the Act I legislation as the agency responsible for the inventory, and that provision be made in the Act I legislation for MfE to carry out enforcement and compliance functions.

31 The Ministry for the Environment has established expertise in the international reporting aspect of the inventory function that is not available in other departments. In addition, it has gained an insight into the collection of sectoral emissions data while collating this material from MAF and MED. As an environmental agency the preparation of inventory figures is broadly within the scope of MfE's activities, and there are policy synergies from MfE's involvement in the New Zealand Climate Change Programme. Naming MfE as the Inventory agency for the time being will minimise disruption to inventory collection and the possibility that this would lead to extra cost for business.

32 MfE, as the inventory agency, will be given the ability to collect inventory data under regulations to the Act I legislation. The legislation will enable MfE to continue to use MED, MAF and other agencies to provide inventory information and expertise to MfE, and for MfE to pass information about individual companies and persons to other named Government departments for analysis.

33 Enforcement of information-collection regulations will involve powers of inspection, search and seizure¹, and the ability to initiate prosecutions where correct information is not provided. The maximum penalty for offences has been proposed as \$2,000 for a person and \$12,000 for a company (refer CAB Min (01) 31/12). Officials from the Ministry of Justice have advised that it would be inappropriate to have any continuing daily penalties (for every day that information is not provided). Following this advice, the maximum level of penalties may need to be in the region of \$5,000 for a person and \$30,000 for a company to provide sufficient deterrence and reflect severity of consequences where information is not obtained (final levels are being discussed with the Ministry of Justice).

34 There are limitations in the present ability of MfE to carry out these enforcement functions. Currently the Ministry for the Environment is not set up to exercise such responsibilities. Officials have considered whether MfE could be named as the inventory agency with *other* agencies being given responsibility for the enforcement. However it is considered that MfE should be the agency responsible for enforcement of regulations. MfE as the inventory agency will have statutory responsibility for compiling the inventory, and will be accountable for any failures in information collection. The responsibility for enforcement should lie with the agency that is ultimately responsible for compiling the inventory. That agency will have the direct incentive to carry out proper enforcement activities. .

35 Conferring the enforcement function on the Ministry for the Environment may require amendments to the Environment Act 1986. The existing functions in the Environment Act 1986 are probably too narrow to cover the enforcement of the proposed regulations.

36 MfE will be able to take advantage of enforcement capabilities of other Government agencies by appointment of enforcement officers from other Government agencies. Enforcement officers will be appointed by MfE; have the prescribed qualifications to carry out the powers of inspection, search and seizure; and will be issued by MfE with a warrant to exercise those powers. MfE will be given the ability to appoint the following as enforcement officers:

¹ Powers of search and seizure will also be the primary method of collecting information about vegetation and soil compositions (rather than self-reporting with search and seizure powers if the information is not provided).

- Employees of the Ministry for the Environment.
- Employees of other Government Departments, and officers exercising functions under other legislation (eg. officers of local authorities, officers of the Department of Conservation, officers exercising powers under the Forests Act 1949).
- Employees of a Crown Research Institute within the meaning of the Crown Research Institutes Act 1992 (such as Forest Research)

37 MfE and officers from other agencies will be required to comply with the provisions of the New Zealand Bill of Rights Act 1990 concerning law enforcement. Officials will work with the Ministry of Justice to ensure that provisions of the Bill are consistent with that Act.

Crown Trading – The Treasury

38 As the Government retains responsibility for ensuring New Zealand compliance under Act I legislation, officials recommend that for the time being, the Minister of Finance should be named as the Minister responsible for Crown trading. It is proposed that the legislation include an ability for the Minister of Finance to delegate the trading function within Treasury, or to contract out the trading function. However the *responsibility* for the function will remain with the Minister.

39 The trading role may vary significantly when policy measures for Act II have been decided upon. Treasury will conduct further work on which Crown institution(s) should be given trading functions under the various policy options being considered for Act II legislation.

Fiscal implications of institutional arrangements

40 Initial estimations of the costs of the different functions are discussed below. In all cases, no funding will be needed this financial year for these functions (it is possible that, depending the timing of domestic policies, no additional funding will be needed for a few years). Once the legislation is enacted, responsible departments will make budget bids as necessary as part of the normal budget rounds. The discussion below indicates that these functions may need an additional \$2-3 million in future years.

41 Further work is being undertaken on the cost recovery options for these functions, taking into account the international requirements under the Kyoto Protocol regarding availability of inventory and registry information, and New Zealand guidelines for cost recovery. Officials will report back on this as part of the work on domestic policy options.

42 This will ensure that the proposals and their costings are adequately reviewed and considered in light of actual Act II policy decisions, and that any funding bids are subject to normal budget process scrutiny and prioritisation.

Registry

43 Establishment costs are difficult to estimate until further work is completed on, in particular, information systems required for institutional arrangements, and pending further work internationally on Registry information systems. Initial set up costs are likely to be in the order of \$1 million, based on the cost of setting up similar registries, such as the Personal Properties Registry. After this, an annual budget of approximately \$70,000- \$100,000 is

likely to be required to run the registry per annum. Only 1-2 staff, including the Registrar, would be required initially.

44 If emission units were devolved and an emissions trading regime established, the operational budget would need to increase to allow an extra 2-3 staff. Additional funding would be sought for the performance of registry functions by MED, although under an emissions trading regime it would be possible to partially fund operations through user charges on transactions and searches of the Register. Further work on cost recovery options is being undertaken based on an assessment of international requirements and national guidelines for cost recovery.

Inventory

45 As it is recommended that MfE retains responsibility for compiling the national inventory for the time being, there are no increases in costs that are related to the allocation of inventory arrangements per se. A table setting out the initial estimates for costs for running this inventory is set out in the table below:

Greenhouse gas inventory costings 20 November 2001			
	Current annual	Future annual	Future periodic
Staff hours per year (MfE, MAF, MED)	>1000	>1500	
Carbon monitoring system ¹	\$700,000	1,500,000	
Improvements to new forest planting data		200,000	
Energy sector data	24,000	24,000	
Waste sector updates (every 5 years)			20,000
Solvents		10,000	
HFCs, PFCs, SF ₆		10,000	
Agricultural statistics ²	2,100,000	2,100,000	
Inventory peer review	10,000	30,000	
Agriculture sector improvements ³	500,000	750,000	
Transport sector improvements ⁴	See note 4	See note 4	
Other costs e.g. refining 1990 baseline ⁵	See note 5	See note 5	
	\$3,334,000	4,624,000	20,000

Notes:

1. Full implementation costs currently unknown. Estimated to be \$1.2 to 1.5 million
2. Greenhouse gas inventory only one of the purposes for collection. Expected to cost \$1.3 to \$2.1 million annually.
3. Four year programme started in FY01/02 totalling \$2.75 million
4. Transport sector inventory improvements are at a preliminary stage.
5. Unable to provide costings until further work undertaken.

46 The table above shows that future additional funding of approximately \$1.3 million may be required in future years for greenhouse gas inventory. An additional amount may also be needed for transport sector improvements. More work may also be needed to assess the adequacy of information collection networks, develop international requirements for good practice in inventory data collection, and expand inventory reporting requirements under the Kyoto Protocol. This may increase data collection and processing requirements and result in expanded institutional arrangements, with an associated need for future funding. Finally, should any existing programmes be discontinued for any reason it would be necessary to secure funding through the climate change programme for their maintenance.

47 Finally, some funding may need to be made available in the future to enable MfE to undertake its enforcement function, once collection of information becomes mandatory.

48 These figures are estimates only and have not yet been reviewed by Treasury. It is likely that a budget bid for next financial year will be made as part of the normal budget bid process, as this function is ongoing with or without the new legislation.

Crown trading of emission units and sink credits

49 The fiscal implications of institutional arrangements for the Crown trading functions will be dependent on the final nature of the Crown trading function, and this function's scope may vary significantly depending on any policy measures implemented through Act II legislation. In a situation where the Crown has to purchase or sell a significant amount of emission units, which may be the case if the Government takes responsibility for meeting New Zealand's compliance equation without allowing the use of sink credits, the Crown trading function has the potential to be significant.

60 This is because the risk management, risk mitigation and any forecasting requirements may add a significant function to Treasury's work, and would represent an ownership issues for The Treasury. On the other hand, should Ministers prefer, for example domestic emissions trading, the Crown trading function will be close to insignificant, as the Government would only need to take responsibility for its own, most likely small, direct emissions. As a result of these significant uncertainties, Treasury will consider potential fiscal implications when it conducts further work on the functions of the Crown trading body, in light of decisions regarding any domestic policy measures as part of the Act II legislation.

Regulatory impact statement for the Act I Climate Protection Bill

61 A regulatory impact statement (RIS) has been prepared in accordance with Cabinet Office guidelines and is attached as Annex 1.

Departments consulted

62 The following departments were consulted in the preparation of this paper: Economic Development; Foreign Affairs and Trade, Environment, Treasury, Conservation, Statistics New Zealand, Fisheries, Land Information New Zealand, Agriculture and Forestry, Research Science and Technology and Justice. The Department of Prime Minister and Cabinet and the State Services Commission were also consulted in the preparation of this paper.

Recommendations

63 It is recommended that the committee:

- a note the attached regulatory impact statement that has been prepared for the Climate Protection Bill in annex 1
- b invite the Minister of Energy to issue drafting instructions to Parliamentary Counsel Office with a proposal for an Act I Climate Protection Bill for ratification of the Kyoto Protocol.
- c note that New Zealand compliance with the international requirements for inventory and registry functions is a requirement for trading on the international market in emission units;

inventory function

- d note that MfE currently has responsibility for New Zealand's inventory obligations under the UNFCCC;
- e agree to the Ministry for the Environment for the time being acting as the inventory agency, pending any reconsideration by officials of institutional arrangements which might be necessitated by Act II policy measures;
- f note that the Act I legislation will provide for the appointment by the Prime Minister of a Minister responsible for inventory functions;
- g agree that the Ministry for the Environment would be responsible for the enforcement of the regulations made under the Climate Protection legislation that require information to be provided to the inventory agency;
- h note that the Environment Act 1986 may need to be amended to allow for the Ministry for the Environment to undertake enforcement of regulations made under the Climate Protection legislation;
- i agree that in carrying out the enforcement functions, the Ministry for the Environment may appoint as enforcement officers its own employees; officers exercising powers under other legislation and employees of other Government Departments; and any other officers who are employees of a Crown Research Institute within the meaning of the Crown Research Institutes Act 1992.

Registry function

- j note that the Act I legislation will provide for the appointment by the Prime Minister of a Minister responsible for registry functions;
- k note that there are synergies to be gained by locating the registry within the Ministry of Economic Development, given its experience in the provision of registries and the development of electronic and internet based registers such as the personal properties securities register;

- l agree to the Ministry of Economic Development being the department responsible for the operation of the registry for the time being, pending any reconsideration by officials of institutional arrangements which might be necessitated by Act II policy measures;

Trading function

- m note that the nature of the trading function and its overall importance will vary, from being relatively unimportant to being critically important, depending on which Act II policy measures are chosen;
- n agree in principle that, for the time being, the Minister of Finance be the responsible Minister for carrying out any Crown trading function, pending any reconsideration by officials of institutional arrangements which might be necessitated by Act II policy measures;

Future arrangements and funding

- o note that institutional arrangements for inventory, registry and Crown trading functions will need to be re-examined in the context of the development of Act II legislation.
- p note that depending on the policies implemented for Act II legislation, funding requirements for these institutional arrangements may change. In the case of the trading function, fiscal implications could be significant depending on the level of trading the Government expects to undertake.
- q note that there is no immediate need for funding of these institutional arrangements. Departments will seek any additional funding required to perform these functions as part of the appropriate budget process to ensure the proposals and their costings are adequately reviewed and considered in light of actual Act II policy decisions.
- r note that further work on cost recovery options will be undertaken as part of the policy development process for Act II legislation.

Hon Pete Hodgson

CONVENOR, MINISTERIAL GROUP ON CLIMATE CHANGE

Annex 1 – Regulatory Impact Statement for the Climate Protection Bill

Nature and magnitude of problem and need for government action

1 The Intergovernmental Panel on Climate Change (IPCC) has predicted possible increases in global average temperatures ranging from 1.4 to 5.8 degrees Celsius in this century as a result of human activities that increase concentrations of greenhouse gases in the atmosphere. It is anticipated that projected temperature increases will cause changes in climate systems that could have significant adverse environmental, economic and social impacts both globally and in New Zealand.

2 As a small emitter of greenhouse gases New Zealand can only meaningfully influence the rate of climate change through participation in international action. The Kyoto Protocol to the United Nations Framework Convention on Climate Change (UNFCCC) and the UNFCCC embody the international response to climate change. The Protocol creates obligations for industrialised states to manage their greenhouse gas emissions and provides for international mechanisms to facilitate this.

3 The Government has stated its intention to ratify the Kyoto Protocol in September 2002 and is consulting on this at the moment. To ratify the Protocol the Government will need to put in place domestic legal mechanisms to meet the Protocol's obligations. In particular, to meet its obligations the Crown will be required to put in place a national inventory to record and report New Zealand's greenhouse gas emissions; a national registry to record holdings and international trading in 'emission units' that represent allocations of emissions to nations with targets under the Protocol; and Crown trading capabilities to allow New Zealand to buy and sell emission units on an international market.

4 Failure to ratify the Protocol could: reduce New Zealand's ability to influence and contribute to international efforts to reduce climate change; hinder New Zealand's development of capacity to manage greenhouse gas emissions and prepare for later more stringent targets that are likely as part of future international action on climate change; and damage New Zealand's international reputation as an environmentally responsible nation and contributor to international initiatives.

Public policy objective

5 To enact minimum legislation (the Climate Protection Bill) to allow New Zealand to ratify the Kyoto Protocol.

Feasible options for achieving desired policy objective

6 There are no non-regulatory options to achieve the objective. Regulatory options include the use of existing legislation or developing new legislation.

Status Quo – existing legislation

7 Technically many of the requirements of the Kyoto Protocol could be met through existing legislation or through non-legislative means. However, this would require the use of a wide range of legal powers from different sources, and would be likely to result in:

- Lack of certainty in the availability of institutions and powers to meet Protocol requirements;
- Lack of transparency in the specification and performance of functions; and
- Difficulty of co-ordination between different functions.

Preferred Option – new legislation

8 The only effective way to meet the policy objective, to enable ratification of the Kyoto Protocol, is to provide for the following minimum requirements in new domestic legislation:

- A national inventory system to record and report New Zealand's emissions of greenhouse gases as required by the UNFCCC and the Kyoto Protocol;
- A national registry to record holdings and transfers of emission units; and
- Powers for the Crown to trade in the international market for emission units to ensure New Zealand's compliance with Protocol.

Net benefit of the proposal

Benefits

9 The benefits of the legislative proposal arise from Kyoto Protocol ratification. These benefits mostly fall into the province of high Government policy and are not readily quantifiable. The benefits of ratification include:

- contributing to a reduction in climate change through demonstrating international leadership and committing at a national level to manage emissions;
- protecting and enhancing New Zealand's reputation as a responsible international actor;
- maintaining New Zealand's influence over the development of international policy in relation to climate change;
- maintaining New Zealand's environmental image and corresponding trade and tourism benefits;
- signalling the Government's intention to manage greenhouse gas emissions to encourage early adoption of emission reduction measures;
- through early engagement in the Kyoto Protocol process, encouraging the development of capacity to meet more demanding international measures to reduce climate change likely to be implemented in future;

Costs

10 The cost of implementing institutional arrangements will not be fully quantified until domestic policies for meeting the obligations of the Kyoto Protocol are decided. These will be set out in a second piece of legislation to be introduced after the Climate Protection Act. Further work is also needed on these institutional functions, particularly on the nature of electronic systems needed for storage and transfer of data between the registry, inventory and any Crown trading function.

11 Initial estimations of the costs of the different functions are discussed below. In all cases, no funding will be needed this financial year for these functions (it is possible that, depending the timing of domestic policies, no additional funding will be needed for a few years). Once the legislation is enacted, responsible departments will make budget bids as necessary as part of the normal budget rounds.

Registry

12 Registry set up costs, apart from the development of information systems, are likely to be in the order of \$1 million, based on set up costs for similar registries such as the personal properties registry run by MED. Running costs are likely be approximately \$70,000-\$100,000 as only 1-2 staff, and corresponding office and other facilities, will be required to implement Act I legislation.

13 If emission units were devolved and an emissions trading regime established under Act II, the registry function would change. Operational budget would need to increase to allow an extra 2-3 staff. Additional funding would be sought for the performance of registry functions by MED, although under an emissions trading regime it would be possible to partially fund operations through user charges on transactions and searches of the Register. Further work on cost recovery options is being undertaken based on an assessment of international requirements and national guidelines for cost recovery.

14 The Ministry of Economic Development has been given responsibility for the registry function under Act I legislation and would require additional vote funding to perform this function.

Inventory

15 Estimated costs of the inventory are set out below:

Greenhouse gas inventory costings 20 November 2001			
	Current annual	Future annual	Future periodic
Staff hours per year (MfE, MAF, MED)	>1000	>1500	
Carbon monitoring system ¹	\$700,000	1,500,000	
Improvements to new forest planting data		200,000	
Energy sector data	24,000	24,000	
Waste sector updates (every 5 years)			20,000
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1. Full implementation costs currently unknown. Estimated to be \$1.2 to 1.5 million
2. Greenhouse gas inventory only one of the purposes for collection. Expected to cost \$1.3 to \$2.1 million annually.
3. Four year programme started in FY01/02 totalling \$2.75 million
4. Transport sector inventory improvements are at a preliminary stage.
5. Unable to provide costings until further work undertaken.

16 The table above shows that future additional funding of approximately \$1.3 million and 500 additional staff hours may be required in future years for greenhouse gas inventory. An additional amount may also be needed for transport sector improvements. More work may also be needed to assess the adequacy of information collection networks, develop international requirements for good practice in inventory data collection, and expand inventory reporting requirements under the Kyoto

Protocol. This may increase data collection and processing requirements and result in expanded institutional arrangements, with an associated need for future funding. Should any existing programmes be discontinued for any reason it would be necessary to secure funding through the climate change programme for their maintenance.

Crown trading

17 The fiscal implications of institutional arrangements for the Crown trading functions will be dependent on the final nature of the Crown trading function, and this function's scope may vary significantly depending on any policy measures implemented through Act II legislation. In a situation where the Crown has to purchase or sell a significant amount of emission units, which may be the case if the Government takes responsibility for meeting New Zealand's compliance equation without allowing the use of sink credits, the Crown trading function has the potential to be significant.

18 This is because the risk management, risk mitigation and any forecasting requirements may add a significant function to Treasury's work, and would represent an ownership issue for The Treasury. On the other hand, should Ministers prefer, for example domestic emissions trading, the Crown trading function will be close to insignificant, as the Government would only need to take responsibility for its own, most likely small, direct emissions. As a result of these significant uncertainties, Treasury will consider potential fiscal implications when it conducts further work on the functions of the Crown trading body, in light of decisions regarding any domestic policy measures as part of the Act II legislation.

Consultation undertaken

19 Consultation on Act I legislation has occurred with the following Departments: Economic Development (including the Business Compliance Cost Unit), Treasury, Environment, Justice, Agriculture and Forestry, Foreign Affairs and Trade, the State Services Commission and the Department of Prime Minister and Cabinet. MoRST, Transport, MFAT?

20 There have been a number of preliminary dialogue meetings on Kyoto Protocol issues with sector groups and with Maori in 2000 and 2001. A round of formal consultation was conducted from October to December 2001 and included consultation on the Act I legislation and on the question of whether to ratify the Kyoto Protocol. The results of consultation were considered when Government made a decision on whether to ratify the Kyoto Protocol, and will be available during select committee consideration of the Climate Protection Bill.

21 Widespread public consultation on this legislation is currently underway – with submissions due by 21 December 2001. Any issues arising from this consultation will be reported back to Cabinet early in 2002, when the legislation is provided to Cabinet for approval for introduction.

Business Compliance Cost Statement

Sources of compliance costs

22 It is important to note that the Climate Protection Bill is the first of two proposed climate change bills. The Part I Climate Protection Bill implements measures to allow New Zealand to ratify the Kyoto Protocol, and provides for Crown management of the costs and benefits of the Protocol. As this legislation deals primarily with Crown assumption of liability the costs of compliance for business are limited. It is intended that a later Part II Climate Protection Bill will be introduced as an amendment to the Part I legislation to provide policy measures to manage emissions, including possible devolution of responsibilities and benefits to business. Consequently the full compliance cost implications of climate protection measures will not become apparent until later decisions are taken on Part II policy measures.

23 There should be no compliance costs for business relating to the crown trading function.

Registry Costs

24 The Part I legislation provides for the creation of accounts for individuals and businesses in the registry to allow them to participate in international emission unit trading. Further work is being undertaken on the cost recovery options for these functions, taking into account the international requirements under the Kyoto Protocol regarding availability of inventory and registry information, and New Zealand guidelines for cost recovery. Officials will report back on this as part of development of domestic policy options. It is likely that any fees incurred will be small (International requirements suggest that information should be freely available on the internet, and fees for requesting copies of searches in similar registries are small – approximately \$10).

Inventory Costs

25 The Part I Climate Protection Bill provides for the creation of regulations to require provision of data to the inventory agency. This raises compliance cost issues to the extent that:

- regulations compel the provision of information that was previously provided voluntarily; or
- information that is already collected for other purposes is collected a second time for climate change purposes; or
- new information collection is required.

26 Much of the inventory data presently collected is through existing voluntary collection or mandatory collection under other statutes such as the Resource Management Act 1991, the Forests Act 1949, and the Customs and Excise Act 1996. To the extent that this information is already collected the Act I legislation will not create an increase in compliance costs. Whether the legislation imposes additional compliance costs will be highly dependent on whether existing programmes that collect inventory data under other statutory requirements or voluntarily are maintained.

27 Present inventory collection provides a guide to the extent of possible compliance costs under Act I legislation, given current levels of inventory reporting.

28 The present inventory reporting includes collection of data on industrial and energy emissions from approximately 110 companies in the electricity, gas, petroleum, and coal industries, and from approximately 20 major industrial emitters, and many more minor industrial emitters. Most of this information is already used by these companies for internal purposes, however varying levels of work are required to compile this information into required reporting formats, depending on the format in which individual companies currently keep this data, and whether their periods of data collection match those required for inventory purposes. A very approximate range for the amount of time taken to complete individual surveys might be from 0.5-7 FTEs each.

29 Agricultural data on livestock numbers is collected through a survey of approximately 80,000 farms, with survey forms likely taking around 1-2 hours each to complete. The survey is completed at periods of approximately 5 years. Additional information on animal productivity is collected from information made publicly available by dairy companies. Information on the costs of providing animal productivity information is not presently available.

30 Forestry data is collected from surveys of major forestry companies and nurseries, and is mostly based on data already used for projecting wood flows by the forestry industry.

31 Enforcement of information-collection regulations, should collection of information become mandatory, will involve powers of inspection, search and seizure², and the ability to initiate prosecutions where correct information is not provided. The maximum level of penalties may need to be in the region of \$5,000 for a person and \$30,000 for a company to provide sufficient deterrence and reflect severity of consequences where information is not obtained (final levels are being discussed with the Ministry of Justice).

Longer term implications of the compliance costs

32 Costs of registry compliance are likely to be in line with normal inflation. Policy measures adopted under Act II legislation may result in increased registry functions and in related increases in compliance costs.

33 Present compliance costs for inventory reporting requirements relate to time spent on collating information and supplying it to the various government agencies that collect inventory data as discussed in paragraphs 26-28 above. The longer term compliance cost implications will depend on later policy measures under Act II legislation and on whether existing programmes which collect inventory information for other purposes continue to collect required data in a sufficiently accurate and verifiable manner.

Parties likely to be affected

Registry

34 Affected parties will be limited to those wishing to trade on the international market in emission units. This could include, among others, companies and individuals that typically engage in trading on financial and commodities markets, and those that participate in emission reduction project activities in other nations under the Protocol. As noted above, there will be no requirements for individuals to hold accounts under Act I legislation.

Inventory

35 As discussed in the section above on business compliance, information used for the inventory is presently collected from a number of sources for a number of purposes.

Estimated compliance costs of the proposal

36 See the section above on business compliance costs. No further compliance costs on individuals or other parties are expected.

Level of confidence of compliance cost estimates

37 As discussed above, there is a reasonably high level of confidence that Registry compliance costs for the Act I Climate Protection Bill will be low. However further work on cost recovery is still to be undertaken.

38 As noted above Inventory compliance costs cannot be readily quantified for the Act I legislation, and will depend to a large extent on the maintenance of other data collection programmes that also provide inventory data.

² Powers of search and seizure will also be the primary method of collecting information about vegetation and soil compositions (rather than self-reporting with search and seizure powers if the information is not provided).

Key compliance cost issues identified in consultation

39 Consultation to date has not identified inventory and registry compliance cost issues.

Overlapping compliance requirements

40 Registry compliance requirements under Act I legislation will not overlap with compliance requirements of other legislation or regulation.

41 There is potential for overlap in inventory data collection where a data collection power is created in regulations for data collection carried out for other purposes that no longer reaches required inventory standards. Potential overlaps will be limited by restrictions on the regulation making power noted in paragraph 33 below.

Steps taken to minimise compliance costs

42 To minimise compliance costs and costs of data collection the Act I legislation requires that before making regulations the Minister responsible for the inventory must consider:

- 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)³;
- 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.

43 Further, the inventory system will be subject to ongoing review of efficiency and adequacy of data collection that will include consideration of compliance cost issues.

³ 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.