

28 February 2008

Sheep, Beef and Deer Industry

Submission to the Finance and Expenditure Committee

on the

**Climate Change (Emissions Trading and Renewable
Preference) Bill (The Bill)**

29 February 2008

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Executive Summary

1. This submission is provided on behalf of Meat and Wool New Zealand, The Meat industry Association and Deer Industry New Zealand (together, the Parties), who represent all of New Zealand's sheep, beef and deer farmers, the vast majority of sheep, beef and deer processors and exporters and a variety of important service providers to the industry.

Background - The sheep, beef and deer industry

2. New Zealand agriculture has been a leader in global food production. Our productivity, adoption of research, and use of sustainable pasture-based production systems are held up as a model by many. It is important that government recognises the comparative advantages New Zealand has in agriculture and that any new regulations co-exist with, and do not harm New Zealand's economic engine.
3. The sheep, beef and deer industry generates export earnings of \$6 billion (about 18% of New Zealand's merchandise trade), provides direct employment for about 40,000 people and indirectly employs many more. Most of New Zealand's regional communities are dependent on the direct and indirect economic outcomes of the sheep, beef and deer industries.
4. There are an estimated 15,000 commercial sheep, beef and deer farms through-out New Zealand. In 2007/08 sheep and beef gross farm revenue is forecast at \$3.9 billion at the farm gate. \$3.5 billion or 90% of these receipts are spent on farm operating expenditure that range from shearing to local authority rates. The remaining \$0.4 billion (10%) is farm profit before tax, which is spent on mortgage repayments, taxation, capital equipment replacement and then family living expenses.
5. The sheep, beef and deer industries currently face tough economic conditions, at the bottom of an economic cycle, with low or negative earnings being experienced by farmers and processors alike.
6. The sheep, beef and deer industry already invests substantially in GHG mitigation through the Pastoral Greenhouse Gas research Consortium (PGGRC) and processing energy reduction initiatives. The Parties are involved in a number of different representation groups involved in research and development, policy development and relationship management for different aspects of the NZETS.

Sheep, beef and deer industry position on climate change policy

7. The Parties agree with statements made within the explanatory note accompanying the Bill that the emissions trading scheme (ETS) should:
 - Support and encourage global reductions in emissions;
 - Maintain economic flexibility;
 - Provide an equitable outcome for those involved;
 - Maintain environmental integrity, at least cost, in the long term.
 - Ensure that reduction targets are aligned with technology opportunities

Key Issues with the Bill

8. The Parties are concerned that the proposal to set down in legislation the amount of assistance available within the NZETS puts competitiveness at risk, creating the likelihood of emissions leakage undermining the environmental integrity of the scheme and imposing significant damage to

New Zealand's economic and social wellbeing. The linear phase-out proposed in the Bill is arbitrary and without any logical basis. The Parties oppose the linear phase-out and propose that a set of decision criteria be established to determine what allocations are required by sub-sectors.

9. The Parties recommend that after the initial year (which is based on a whole sector allocation of 90% of 2005 emissions) the amount of assistance to trade exposed persons be determined on the basis of regular, objective analysis of requirements, as a part of the allocation plan process. Trade-exposed sub-sectors' requirement for assistance would be a function of mitigation ability, implementation of similar climate change policy in both competitor and trading countries and changes in the intensity of emissions due to productivity improvements.
10. The Parties believe that the NZETS should not, initially, drive the reallocation of capital (or land) because the economic cost of various capital uses is not yet reflected in world market prices.
11. The Parties recommend that the Bill incorporates provisions for the guaranteed availability to industry of government held carbon credits at a capped price to manage the market risks associated with the liquidity of the New Zealand carbon market.
12. The Parties believe it is imperative that the NZETS is efficacious – that it works in incentivising emission reducing behaviours – and that efficacy is unlikely in Agriculture if processors are made Participants – as is the default option. The Parties believe that to be efficacious, the Bill must specify farmers as participants in the NZETS, thereby incentivising those who can mitigate GHG emissions with the appropriate market rewards for mitigation.
13. The Parties do not accept that there should be provisions in the Bill for recovery of the costs of administering the NZETS from Participants as the NZETS is compulsory for participants and is a 'public good' initiative that has much wider environmental and social impacts than on the Participants in the NZETS.
14. The Parties believe that, due to the significance of some of the yet-to-be-determined aspects of the NZETS, decisions about those aspects should be subject to a rigorous and timely review and consultative process and redefined in legislation later if necessary.

Further comments

15. While energy and transport cost increases will affect farm businesses from 2009 onwards, on-farm livestock emissions are planned to be subject to the ETS in 2013. There are currently no practical tools available for sheep, beef and deer farmers to affect behaviour change, and great difficulties in measuring emissions, so a delay until 2013 is important to permit farmers to adjust management practices where practical.
16. The Parties recommend that the Minister allows for dual emissions reporting systems for agriculture whereby farmers can either opt to use a detailed emissions estimation methodology or opt to use a simple, default emissions calculation that carried little or no administrative cost.
17. The Parties intend to develop a process to identify an initial equitable approach to allocation within the "Agriculture" sector as defined in the Bill under the cap of 90% of 2005. A recommendation to the Minister will be forthcoming from a cross-sector pastoral group. While international competitiveness, carbon leakage and mitigation potential issues will be unique for each sub-sector (such as the sheep, beef and deer sub-sector and the dairy sub-sector), there is a desire from the pastoral sector to be responsible in the first instance for developing an initial allocation plan for sub-sectors within "Agriculture" for the consideration of the Minister.

Summarised Recommendations

18. In respect of the Bill, the Parties have the following recommendations, which are given context in the remainder of this submission.

Recommendations

- I. The Parties recommend that the aggregate credits allocated to trade exposed sectors should at no time decrease below New Zealand's allowed emissions under international agreements.
- II. The Parties recommend that paragraphs (2)(c) of sections 70 and 71 be amended such that future reductions in the amount of free allocation to sub-sectors are determined on the basis of objective and transparent analysis of need, and not arbitrarily predetermined.
- III. The Parties recommend that the Allocation Plan development process (as set out in sections 68 through 74) should be expanded such that the Minister may determine the total envelope of assistance available to any given sub-sector without legislative constraint (following the initial allocation plan for sub-sectors under the 90% of 2005 cap as presented by the cross sector pastoral group).
- IV. The Parties recommend that the Minister develop allocation plans for individual sub-sectors (such as the meat industry and the dairy industry) instead of the high-level sectors ('Agriculture', 'Forestry' and 'Industry') currently defined in the Bill.
- V. The Parties recommend that Schedule 3 of the Bill be altered such that the default 'Participants' responsible for ruminant animal emissions are farmers, not processors..
- VI. The Parties recommend that paragraphs (5), (6) and (7) of section 148 of the Bill be deleted and that the administration of the NZETS be funded through general taxation.
- VII. The Parties recommend that the Bill incorporates provisions for the guaranteed availability to industry of government held carbon credits at a capped price.
- VIII. Should (despite the Parties earlier recommendation) meat processors be made Participants in the NZETS, the Parties recommend that the Bill be modified such that meat processors are not held legally accountable for the provision of information that they do not 'own' and do not have the capability to verify.
- IX. The Parties recommend that the Bill be amended such that, in relation to agricultural emissions, free units are only allocated to persons that are Participants in the NZETS.
- X. The Parties recommend that the Bill provides that trade-exposed firms may use 2003, 2004 or 2005 as the base year from which free allocation of assistance entitlement is calculated.
- XI. The Parties recommend that section 70(1)(b) be amended such that trade exposed firms may be allocated free units in relation to higher costs resulting from liabilities associated with the use of transport fuels.
- XII. The Parties recommend that Section 70(4)(a) be amended such that industrial emitters other than the owners of 'industrial processes' are eligible for free allocation.

- XIII.** The Parties recommend that section 72(b) be amended to clarify that allocation will not be made in respect of sectors that have not yet commenced participation in the scheme, but upon entry of a sector to the scheme, relevant persons will be eligible for free allocations.
- XIV.** The Parties recommend that paragraph (1) of section 147 be amended to require that the first review of the NZETS be completed *at least 12 months prior* to the end of the first commitment period.
- XV.** The Parties recommend that paragraph (1) of section 147 be amended to require that reviews of the NZETS are undertaken biennially or annually.
- XVI.** The Parties recommend that the Bill be amended to incorporate principles to be followed when setting regulations that determine the methodologies for calculating GHG emissions for the purposes of the NZETS, and that those principles include that:
- All scientifically proven mitigation techniques are incorporated in calculations, not just those recognised within international agreements.
 - Methodologies shall be updated to incorporate newly developed and/or accepted climate science, such as new estimates of Global Warming Potentials for various GHGs.
- XVII.** The Parties recommend that in order to minimise on farm administrative costs, the Minister allows for a two-tier system for calculating on-farm emissions, whereby farmers can opt in to providing detailed emissions returns or have a return calculated for them using default assumptions.
- XVIII.** The Parties recommend that amounts received by non-Participants, in return for disposal of freely allocated units, not be considered income for the purposes of taxation.

Part I: The sheep, beef and deer sub-sector

19. This submission is provided on behalf of Meat and Wool New Zealand (M&WZN), The Meat Industry Association (MIA) and Deer Industry New Zealand (DINZ), (together, the Parties).

Industry overview

20. In 1990/91 the total agricultural sector, including on-farm, the input supply sectors and the downstream processing, transport and marketing sectors, contributed 13.5% to GDP. From 1990/91 to 2004/05, GDP for the whole economy grew by 57% – from \$79.6 billion to \$125.3 billion. During this period total agriculture grew at almost twice the rate of the rest of the economy and increased its contribution to 17% of GDP in 2004/05.
21. Rather than agriculture becoming less important following deregulation of the '80s and '90s it grew at a faster rate than the rest of the economy in terms of net added value. In part this was through improvement in downstream processing, particularly since 1986/87 when around 72% of lamb was exported as carcass meat whereas today this has fallen to 4%. Today, nearly all sheep meat (95%) is exported as further processed added value product.
22. Similarly there have been land use changes from sheep and beef to higher value dairy production on some land plus significantly improved levels of animal productivity. An example of the productivity improvement is that from 1990/91 sheep numbers have decreased 32% but total lamb production has increased 12%.
23. Exports of sheepmeat, beef and venison, along with wool, hides and many related products generate \$6 billion of foreign exchange earnings annually – 18% of total merchandise exports. The sub-sector also generates \$1 billion per annum in local market sales.
24. The earnings are returned to New Zealand's rural economies by way of payments to producers and wages earned in meat and wool processing. The sub-sector is also a major driver of economic activity in the packaging, transport and logistics sectors supporting rural New Zealand's towns and communities.
25. In 2007/08 sheep and beef gross farm revenue is forecast at \$3.9 billion at the farm gate. \$3.5 billion or 90% of these receipts are spent on farm operating expenditure that range from shearing to local authority rates. The remaining \$0.4 billion (10%) is farm profit before tax which is spent on mortgage repayments, taxation, capital equipment replacement and then the farm family living expenses.
26. In 2007/08 there are 39.1m sheep, 4.4m beef cattle and 1.6m deer in New Zealand. Of New Zealand's total agricultural land area, the sheep, beef and deer sector occupies 62% and of the total pastoral area 83% or 9.59m hectares.
27. The meat processing industry directly employs about 22,000 people, while a significant proportion of New Zealand's 15,000 sheep, beef and deer farmers also provide direct employment to others on-farm. Indirectly, sheep, beef and deer farmer businesses employ a large number of other professionals such as vets, bank managers, contractors etc underpinning New Zealand's employment market.

28. Based on 2005 National Inventory¹ figures, it is estimated that the sheep, beef and deer farming generated about 22m tonne CO₂-E of GHGs in 2005 (29% of total New Zealand emissions in 2005), mostly in the form of methane and nitrous oxide (and excluding on-farm fuel and electricity usage). In addition, it is estimated that meat processing is directly responsible for about 750,000 tonne of CO₂ per annum, as a result of energy usage. This does not include emissions from contracted services such as livestock and product transport or storage.

Meat and Wool New Zealand

29. Meat and Wool New Zealand (M&WNZ) is a New Zealand farmer owned and levy funded organisation mandated under the Commodities Levies Act (1990) with the key objective of ensuring the best possible returns for New Zealand sheep, beef and goat producers.
30. M&WNZ aims to improve farm returns by increasing preference for New Zealand wool and red meat internationally and domestically; maintaining and extending trade access for New Zealand wool and red meat; funding research and development to provide solutions that will help improve New Zealand farm returns and providing wool technical advice.
31. M&WNZ is required to consult with farmers prior to setting the levy rates each year. Additionally the Commodity Levies Act requires Meat & Wool New Zealand to show that payment of levies is supported by a majority of levy payers by conducting a referendum at least every 6 years. The last referendum was conducted in 2003.

The Meat Industry Association

32. The Meat Industry Association of New Zealand Incorporated ('MIA') is a voluntary trade association representing New Zealand meat processors, marketers and exporters. It is an Incorporated Society (owned by members) that represents companies supplying virtually all of New Zealand sheepmeat exports and all beef exports.
33. MIA member companies operate approximately 80 processing plants dispersed throughout the country. The plants slaughter and process approximately 24 million lambs, 4.4 million sheep and 4.2 million cattle and calves each year. Ninety percent of this production is processed into value-added products. Approximately 840,000 tonnes or 85% of the production is exported to overseas destinations. Our affiliate members add to the depth of expertise available from the membership, with representation throughout the meat supply chain, including road and rail transport, shipping lines, ports, packaging firms, specialist product exporters, research and technology.
34. The MIA advocates on behalf of its members and provides advice on economic, trade policy, market access, employment relations, business compliance cost and technical and regulatory issues facing the industry, with a particular focus on:
- Food safety trends and developments in importing countries
 - Economic and trade aspects of market access to key overseas markets
 - Major public policy proposals that could impact on industry operations
35. The MIA is also the interface between the meat industry and government (i.e., it is the consultative body referred to in various New Zealand statutes, such as the Meat Board Act 2004, Meat Act 1981 and the Animal Products Act 1999).

¹ MfE: New Zealand's Greenhouse Gas Inventory 1990–2005; THE NATIONAL INVENTORY REPORT AND COMMON REPORTING FORMAT, July 2005

36. The Association's mission is to:
- Provide a forum for consideration of industry-wide commercial, human resource, marketing, and sanitary and zoonosanitary issues; and
 - Provide the means of formulating a collective view on issues of industry wide interest, and of conveying that position to government, departments of state, trade bodies, and other appropriate external agencies and organisations.
37. A list of MIA members and affiliate members is attached as Appendix 1.
38. In preparing this submission all MIA members were consulted and asked for input. MIA members may also make individual submissions reflecting concerns relating to their specific operations.

Deer Industry New Zealand

39. DINZ is the levy funded industry-good body established under the Deer Industry New Zealand Regulations (2004). One of its key functions is to promote and assist the development of the deer industry in New Zealand. Levies are collected on the products of velvet antler and venison. For venison, levies are paid on a share basis between the currently ca. 4000 active deer farmers and venison processors and marketers. For velvet, levies are paid by velvet producers.
40. In the year ending September 2007 the value of exported deer products (venison, velvet and co-products) amounted to over \$280 million in export earnings. The industry, along with other pastoral sector industries (beef, lamb, wool and dairy), relies heavily on being able to access overseas markets: Cost effectiveness in production and customer acceptance are major factors in maintaining these markets.
41. Major markets for NZ farmed-venison are countries belonging to the European Union (71% of total export value) and the USA (12%). In these markets venison tends to compete with wild game venison and other specialty meats and in the European countries there is a pronounced seasonal (winter) demand based upon traditional game meat availability. In this respect, DINZ stakeholders face less competition from farming interests in target market countries, but rather from suppliers of wild deer who have significantly lower costs of production. Price impacts are therefore extremely important as are consumer perceptions of food hygiene and clean, green, sustainable farming.
42. DINZ therefore has a significant stake in how New Zealand responds to the challenges presented by climate change.

State of the sheep, beef and deer industry

43. Expectations are that in the 2007/08 season, sheep and beef farming profitability will be at its third lowest level in the last 60 years in real terms and its lowest since 1995-96. Deer farming profitability will be improved in 2007/08 from the previous year but the previous three years were particularly difficult for deer farming because of low returns and this has led to a significant decrease in deer numbers. Alongside this, meat processors' most recent financial results have shown heavily reduced profits or significant losses.
44. The short-run outlook for 2007/08 is for tough times from 4 major factors.
- A persistently high exchange rate.
 - Extremely dry summer conditions in most regions forcing an early slaughter of stock at lighter weights. If the dry conditions continue and large numbers of capital stock are slaughtered then productive capacity will be lost for 2008/09 and will have productivity and profit flow-on effects in 2008/09.

- The rapid increase in global grain and other food prices are yet to flow through to global red meat markets and sheep and beef farm-gate returns.
- On-farm inflation for farm inputs up an estimated 4.2% has added real pressure on sheep and beef farm operational expenditure. On-farm inflation has increased 22 per cent since 2000-01 and run above the consumer price index. On-farm inflation in three out of the last four seasons has been above 4 per cent. Although there has been inflationary pressure from fuel and fertiliser increases, compliance costs from governments fiscal stimulation has also played a large part in lifting non-tradable inflation significantly such as rates and wages on-farm and shearing.

45. Year-to-date in-market prices are positive:

- Trade weighted wool market prices from July 2007 to December 2007 are up 3.7%. The exchange rate has appreciated 7.9% decreasing the NZD price 3.9%.
- In-market lamb prices for this season to date are up 7.6% on the same period last year. In NZD the lamb price is down 0.3%. In addition lambs skins that bottom out in February 2007 at \$2.90 per skin FOB have increase 117% to \$6.30 per skin in NZD (in-market prices increased 148%).
- In-market beef prices for North America continue to hold near historical high levels. In NZD's the North America beef price is down 10%.

46. Good profit levels in early 2000 were underpinned by a lower NZD and low inflation. If a similar NZD and lower inflation prevailed in 2007/08, then Sheep and Beef Farm profit before tax would be a lot higher than in early 2000. This shows that there has been a real lift in offshore prices and both on-farm productivity and export processing. The high NZD and inflation completely masks this advance to the detriment of New Zealand's economy.

47. The challenges currently being experienced in the sheep, beef and deer sub-sector are exacerbated by the current high returns available from dairy farming and the knock-on effects into dairy support options and crop prices. The comparative returns from dairy farming, dairy support and cash crops are much higher, at this time, than those available in the sheep and beef and deer sub-sector and this has three knock-on effects:

- Those sheep, beef and deer farmers who are able to convert their land to dairy farming are, in many cases, doing so. This reduces the long-term supply of sheep, beef cattle and deer available for processing and leads to underutilisation of processing assets and people.
- Those sheep, beef and deer farmers who are not able or do not want to convert their land to dairy farming are looking at other farming options such as cash cropping and dairy support. This reduces the long-term supply of sheep, beef cattle and deer available for processing and leads to underutilisation of processing assets and people.
- The land use change leads to short-term distortion of store markets by decreasing demand, which impacts on prices and margins for sheep, beef and deer farmers.
- Farm land values are pushed higher, increasing the capital and interest costs incurred by producers and further impacting on profitability.

Part II: Background

48. This section sets out the sheep, beef and deer industry's broad perspectives on climate change and policy in relation to GHG emissions and mitigation.

The importance of climate change to the sheep, beef and deer industry

49. The Parties recognise that the science suggesting that human induced GHG emissions cause or contribute to climate change is strengthening.
50. As well as possible humanitarian impacts, climate change is likely to have a number of commercial impacts of economic relevance to the sheep, beef and deer industry, including more frequent extreme weather events and a heightened risk of biosecurity incursion.
51. The Parties recognise that if changes in human behaviour can lead to the slowing or reversal of climate change then efforts should be made to achieve such changes.
52. As well as taking action in order to address the physical risks of climate change, the Parties recognise that it may become increasingly important that, in the eyes of some of our overseas customers, we as a nation are seen to be taking positive action in respect of climate change.
53. The Parties are involved in a number of different representation groups involved in research and development, policy development and relationship management for different aspects of the NZETS, including:
- Sustainable Food Exports Group
 - Greenhouse gas foot printing working group
 - Pastoral Stakeholders Group
 - Technical Advisory Group (TAG) for ETS Agriculture
 - Emissions trading group Stationary Energy & Industrial Process (TAG)
 - MFAT Post 2012 International Policy Consultation
 - Adoption environment/research mentor group
 - MAF Peak Group
 - Adaptation Working Group on Climate Change
 - Business Opportunities Working Group
 - Climate Change Leadership Forum
 - Climate Change Leadership Forum Clusters
 - Dairy Environment Leadership Group
 - Dairy Environment Advisory Group
 - Pastoral Sector Leadership Group
 - PGGRC

Climate change related activities in the sheep, beef and deer industry

54. Through its use of ruminant animals, the sheep, beef and deer industry is a major contributor to New Zealand's GHG inventory (29% of NZ's total emissions in 2005). Ruminant animals produce large volumes of methane from enteric fermentation, and farms, through animal excrement and fertiliser usage, produce nitrous oxide. Individual farms also create GHG emissions through energy usage for operational activities such as shearing and paddock cultivation etc. Meat and meat co-product processing also creates a much smaller, but still significant amount of GHG emissions through energy usage for industrial heat and refrigeration.

55. Since its establishment in 2002, the sheep, beef and deer industry has contributed to the funding of the Pastoral Greenhouse Gas Research Consortium (PGGRC), with the objective of mitigating the GHG emissions associated with the farming of ruminant animals. Pastoral industries contribute \$2.5 million per annum to this consortium.
56. Mainly through on-farm productivity gains, GHG emissions per unit of sheepmeat output have decreased by an estimated 17% since 1990². This improvement is thought to be the result of a number of factors including better feed and farm management, genetic selection and capital investment in water and fence systems. Future productivity gains through these mechanisms are unlikely to be as rapid or dramatic.
57. While production has increased, emissions from the sheep, beef and deer sub-sector sector now are lower than they were in 1990 – the benchmark for New Zealand reductions in the first Kyoto commitment period.
58. Most meat processors participated in the Voluntary Agreement with government in the late 1990s that focussed on reducing energy (electricity and fuels) use during processing. Subsequently individual companies have continued energy efficiency programmes by conduction energy audits, changing product forms, building new energy efficient facilities and converting to shift work operations. Significant gains have been achieved by some companies.
59. In meat processing, the imperative to reduce energy consumption needs to be carefully balanced against the requirement to ensure that temperatures and regimes for cleaning and sterilisation and for product storage are effective in maintaining the highest standards of food safety. This consideration means that energy reduction measures need careful research and often require the approval of local and overseas food safety regulators.
60. Higher environmental expectations may also work counter to the objective of reducing energy usage. An example of this would be the requirement for more intensive pre-treatment of wastewater before it is discharged from processing sites.
61. Despite these constraints, energy efficiency improvements have been, and will continue to be achieved in the sector.
62. The meat industry is a major source of feed material for New Zealand's developing biofuels industry. Two New Zealand based, commercial scale biodiesel manufacturing operations have recently been announced that will use tallow from meat processing as feedstock. The meat processing industry has huge potential to contribute to the growth of non-fossil transportation fuels.

The sheep, beef and deer industry's attitude to GHG emissions policy

63. The Parties believe that to be effective, New Zealand Climate Change policy must:
 - Not be constrained by the failings of the Kyoto Protocol;
 - Consider the long-term sustainability of the Agricultural Sector, no matter what part of the commodity price cycle it may be experiencing;
 - Be transparent to those required to change their behaviour;
 - Preserve flexibility for land use change and sustainable management;
 - Retain alignment to global emissions targets and consider international competitiveness;

² Barber, A. and Pellow, G. 2007, The Total Resource Use and Carbon Footprint of New Zealand Sheep and Beef Farms, Woollen Fabric and Processed Meat (Unpublished).

- Ensure reduction targets are aligned with technology opportunities.
64. The Parties agree with statements made within the explanatory document accompanying the Bill that the ETS should:
- Support and encourage global reductions in emissions;
 - Maintain economic flexibility;
 - Provide an equitable outcome for those involved;
 - Maintain environmental integrity, at least cost, in the long term.
65. The Parties believe that during times of full employment and a relatively comfortable standard of living, New Zealanders put climate change high on their list of priorities. If climate change policy results in job losses, pay cuts and mortgage foreclosures, motivation for climate change action and popular support for climate change policy will very quickly diminish.
66. It is crucial that action on GHG emissions does not come at the expense of jobs and exports in sectors such as the sheep, beef and deer industry, which directly employs about 2% of New Zealand's workforce and earns about 18% of the country's foreign exchange.
67. The Parties believe that the requirement to mitigate GHG emissions must be carefully balanced against the requirement to preserve the economic and social wellbeing of New Zealanders.
68. To achieve this balance requires assessment and acknowledgement of the true costs and benefits of the proposed policies, with an emphasis on the:
- Potential for emissions leakage offshore.
 - Impacts on New Zealand's competitive advantage.
 - Additional costs on producers both direct and in-direct, without guarantees that this will be accompanied by increased commodity prices.
 - Potentially difficult adjustments to regional land prices and effects on rural community viability.
 - General effect on the economic position of New Zealand's pastoral industries and the wider New Zealand economy they underpin.
69. The Parties would note that some key modifications are required in order to ensure that the NZETS is effective and that it retains the flexibility to assist, as necessary, those sectors and sub-sectors that may face irreparable damage as a result of carbon liabilities creating international competitive disadvantage and carbon leakage.
70. Under the proposed NZETS, the sheep, beef and deer sub-sector will need to learn, in a progressive manner, how to manage different carbon assets and liabilities. These include:
- The introduction of forestry to the scheme in 2008, which will affect some farmers.
 - The introduction of transport fuels in 2009, which will have a significant impact in respect of both livestock and end product transport.
 - The introduction of stationary energy in 2010, of which processors are major consumers.
 - The introduction of livestock emissions in 2013.
71. The Parties agree with the phased approach to introducing new sources into the scheme. This will allow market managers and participants to learn lessons from earlier phases and minimise the impact of teething problems.

Scope of this submission

72. This submission addresses those sections of the Bill that deal with “*A proposed New Zealand emissions trading scheme*” (as described in pages 20 to 52 of the explanatory note, primarily detailed in amendments to the Climate Change Response Act 2002). The Parties do not wish to submit on issues related to the “*Limit on new thermal capacity*” (dealt with in amendments to the Electricity Act 1992) except to comment that a reliable supply of reasonably priced electricity is essential for the operation of plants and the viability of the sheep, beef and deer sector.

Part III: The Sheep, Beef and Deer Industry's Key Concerns with the Bill

73. This section describes four key areas where the Parties consider that the Bill is fundamentally deficient and requires substantive change. Further detail on these, and other less fundamental issues, is set-out in the later parts of this submission.

Competitiveness at risk

Problem definition

74. As has been stated earlier, the Parties believe strongly that in order to:

- Preserve New Zealanders' standard of living relative to other nations, and;
- Maintain popular support for climate change efforts and climate change policy, and;
- Prevent leakage of production and emissions to competitor countries,

it is imperative that the NZETS does not result in damage to the economic and social wellbeing of New Zealanders.

75. The Parties acknowledge that government has a difficult task to develop policy that balances the requirements to place impetus on individuals and firms to modify their emissions behaviour, but does not do significant harm to the economy or the environment.

76. There is a clear risk that the NZETS could place exporting agricultural and industrial sectors at competitive disadvantage because New Zealand businesses are compelled to purchase carbon credits to offset emissions whereas overseas competitors (currently) are not. In other words, the competitiveness of New Zealand exporters is at risk.

77. The competitiveness at risk issue has two likely negative outcomes:

- a. Returns from New Zealand's agricultural and industrial export sectors are reduced, resulting in flight of firms, investment redirected offshore, land transferred to inherently lower-value uses, jobs lost or not created and wages lowered.
- b. In the case of exported food products, global demand is highly unlikely to reduce in response to higher costs in New Zealand, that demand will simply be met by other producing countries. In the case of meat, there is evidence to show that production in New Zealand is highly efficient in terms of GHG emissions³. Leakage of that production to other countries is therefore likely to result in a loss of income for New Zealanders, an increase in GHG emissions per unit of output and a rise in total global emissions.

78. Reduced competitiveness of New Zealand food exporters is therefore likely to result not only in damage to New Zealand's economic and social wellbeing, but also (perversely) a rise in global GHG emissions.

79. To damage the New Zealand economy by exposing firms to the full costs of GHG emissions whilst their competitors face no such costs is economic masochism and would deliver no climate change benefits.

³ Saunders, C.M., Barber, A. and Taylor, G (2006) Food Miles – Comparative Energy/Emissions Performance of New Zealand's Agriculture Industry. AERU Research Report No. 285 July 2006.

NZETS design implications

80. For the reasons described above, the Parties believe it is vital that the NZETS includes provisions that *ensure* that the international competitiveness of New Zealand industries is not significantly adversely affected by an uneven international playing field in respect of GHG liabilities.
81. While the majority of New Zealand's internationally competitive industries could be protected through the omission of agriculture from the NZETS, the Parties understand the argument for an 'all gasses, all sectors' approach for economic efficiency. The rationale for all sectors and all gasses is about enabling all possible opportunities for mitigation, not punishing emitters.
82. If agriculture is to be included in the NZETS, the Parties believe that the best mechanism for protecting agricultural subsectors from an uneven international playing field is through the allocation of carbon credits free of charge.
83. The Parties do not support the provision of assistance by the Progressive Obligation method.

Side-note on free allocation of units

The Parties note that, in theory, providing a rational market-participant with additional assets does not reduce that participant's economic incentive to procure more units, as any 'excess' can still be redeemed for monetary gain. One important proviso to this theory is that the total volume of free units allocated is not so great that the market value of units collapses. The risk of market value collapse in the NZETS is remote given that there will be no provision of free units to Participants that are not 'trade exposed'.

Following this theory, it is unlikely that the level of free allocation would have any effect on the efficacy of the NZETS in driving behaviour that minimises GHG emissions.

Issue 1

It might be argued, however, that confronting market participants with the probability of financial loss (as opposed to potential financial gain), for non-rational reasons, will be more effective in promoting desired action by those participants. Indeed, the NZETS (as drafted) seems to adopt this premise by electing an initial allocation of free units to trade exposed Participants (90% of 2005) that will place them in a net deficit market position.

The notion that poor financial performance is a better motivator than financial over-performance may have some merit. It should be noted, however, that for NZETS Participants, tension about possible poor financial performance will be driven by much more than liabilities created by the NZETS. In the case of the meat industry for instance, due to their difficult economic circumstances, farmers would have ample motivation to capture any available financial benefits from GHG mitigation, regardless of whether they have a net deficit or surplus of units in the NZETS.

Issue 2

It has also been proposed, within the explanatory note of the Bill and elsewhere, that the NZETS should be driving reallocation of capital to more GHG-favourable industries. In New Zealand this might be primarily around the reallocation of land from pastoral farming to forestry. While in the long term this could potentially make economic sense, in the short term, whilst international competitors face no emission costs, it does not.

In order to optimise capital usage, and particularly in the New Zealand context – land usage, the full cost and benefit of that usage should be considered. The NZETS will introduce to New Zealand industries, one component of cost – GHGs – which has previously been an externality. When the emission costs of ruminant farming and the sequestration benefits of forestry are apparent to all global producers, we can expect an adjustment in world prices for ruminant and forestry products. Presumably, meat prices would rise and wood prices would fall. The increased cost of ruminant farming and the benefit of foresting will likely be offset, to some extent, by changes in the market values of those industries' outputs

The Parties believe that the NZETS should not, initially, drive the reallocation of capital (or land) because the economic cost of various capital uses is not yet reflected in world market prices.

84. The Parties believe that sufficient free credits should be allocated to trade exposed sectors to ensure that the NZETS does not risk trade exposed sectors international competitiveness and drive the reallocation of capital (or land) leading to carbon leakage.
85. The Parties recognise that any free credits allocated by government to industry come at the expense of the taxpayer (notwithstanding that the taxpayer has been allocated a significant quantity of free credits under international agreements). Balanced against the requirement to prevent carbon leakage and harm to the economy, is the concern that the taxpayer should not provide more assistance to at-risk sectors than they need.
86. The Parties believe that in order to maintain the balance between ensuring that no economic and social harm is done to at-risk sectors by the NZETS (causing carbon leakage) and prudence in the disbursement of a public asset, the requirement of sectors for free allocations needs to be regularly and thoroughly analysed. Such analysis should assess a range of factors, but most importantly:
- a. The exposure, or otherwise, of major trading partners and competitors to the costs of GHG emissions, through emissions trading schemes, carbon taxes or otherwise.
 - b. The availability, or otherwise, of cost effective methods to mitigate GHG emissions.
 - c. Changes in the intensity of emissions per unit of output from New Zealand sectors due to productivity or other improvements.
 - d. The stock of free emission units that New Zealand has secured within any international agreements that might exist and that the government has entered into.
87. The Bill provides for no such analysis of circumstances surrounding the requirement for and availability of units to be freely allocated to at-risk sectors. Instead the Bill sets out that there will be an initial amount of freely allocated units available and that that amount will reduce to zero, in a linear fashion, over 12 years. There is no mechanism set out in the Bill to modify the availability of freely allocated units. Any modification in the amount of freely available units would require a legislative amendment to be enacted.
88. The Parties oppose the proposed linear phase out because it is entirely arbitrary, divorced from the economic and social realities and technical advances over the relevant time period. As such, it will not provide an appropriate level of assistance. It will provide either too much free assistance (in the case, for instance of a technological breakthrough to eliminate emissions) or too little (in the case of little technological progress and inaction by international competitors). We can be sure that the phase-out, as drafted will be wrong because it is simply not possible to predict future circumstances with accuracy. Further, the Parties do not consider it prudent to rely upon legislative amendment as a design component to deal with future uncertainty.
89. The Parties note that the proposed linear phase out of assistance would produce a situation where agriculture and industry were required to take responsibility for 100% of their emissions by 2025. New Zealand as a whole is highly unlikely to be required, under international agreements, to reduce emissions by anywhere near 100% by 2025. This would mean that government received units under international agreements significantly in excess of what it was passing out to at-risk sectors by way of assistance. In other words government would receive a windfall gain at the expense of industry and agriculture, which would be required to shoulder more of the burden for emissions than New Zealand as a whole was. The Parties consider such a transfer of wealth from firms to government to be completely inappropriate.

Recommendation 1

90. **The Parties recommend that the aggregate credits allocated to trade exposed sectors should at no time decrease below New Zealand's allowed emissions under international agreements.**

Recommendation 2

91. **The Parties recommend that paragraphs (2)(c) of sections 70 and 71 be amended such that future reductions in the amount of free allocation to sub-sectors are determined on the basis of objective and transparent analysis of need, and not arbitrarily predetermined.**
92. The Parties recommend that the amount of assistance available to trade exposed persons (subsequent to the initial 90% of 2005 allocation) be determined on the basis of regular, objective analysis of requirements and be built in to the Bill's proposed process for developing allocation Plans for each reporting period. Trade-exposed sub-sectors' requirement for assistance would be a function of mitigation ability, changes in the GHG intensity of production and the implementation of similar climate change policy in both competitor and trading countries. Using the allocation plan process would expose analysis to public scrutiny and consultation (as would be desirable).
93. A proposed model for determining sub-sectors' future requirement for free allocation assistance (as a component of the development of allocation plans) is set-out at Appendix 2.
94. The Parties consider that the circumstances of different sub-sectors within the sectors currently defined in the Bill ('Agriculture', 'Forestry' and 'Industry') may vary considerably, and therefore that a lower level of definition is required when developing on going allocation plans (including the requirement for assistance).
95. The Parties believe that a lower-level definition of sector groups is appropriate because competitiveness at risk circumstances may be quite different for different industries. For instance, technologies might appear that drastically reduce emissions from smelting, but that have no application in cement manufacture. This would reduce the smelting sub-sector's requirement for free allocation.
96. There are also substantial differences between agricultural sub-sectors in terms of their ability to mitigate emissions. Many of the mitigation technologies currently being developed, like nitrification inhibitors, herd homes or feed pads have clear potential in the dairy sub-sector but not for sheep, beef and deer.
97. Not only are there likely to be differences in the ability of the sub-sectors to use mitigation technologies but there are also likely to be difference in the ability of sub-sectors to apply current known methods of increasing productivity. For example, the sheep flock has been reduced significantly since 1990 and this rapid reduction has been the basis for increased selection pressure for genetics relating to improving productivity. This has resulted in the increased productivity per animal, which is reflected in the overall reduction in GHG emissions in this sector per tonne of product. Now that the flock has been substantially reduced and has reached a new steady state, the genetic pressure that can be applied will be much lower and so the rate of reduction in GHG emissions by this means will become much slower. The Parties believe that different sub-sectors, as listed in the arguments above, will have different requirements for assistance – a situation that the Bill, as currently drafted cannot deal with.

Recommendation 3

98. The Parties recommend that the Allocation Plan development process (as set out in sections 68 through 74) should be expanded such that the Minister may determine the total envelope of assistance available to any given sub-sector without legislative constraint (following the initial allocation plan for sub-sectors under the 90% of 2005 cap as presented by the cross sector pastoral group).

Recommendation 4

99. The Parties recommend that the Minister develop allocation plans for individual sub-sectors (such as the meat industry and the dairy industry) instead of the high-level sectors ('Agriculture', 'Forestry' and 'Industry') currently defined in the Bill.

Efficacy of the NZETS

100. The Parties are concerned that the default provisions set out in the Bill, with respect to Participants in the Agriculture sector mean that the Bill will not be efficacious in reducing the GHG emissions of the pastoral based industries.

101. The Parties believe, that to be efficacious – to work – the Bill must create an emission trading scheme that:

- a. Is not unacceptably costly in terms of economic damage or administrative burden.
- b. Results in actions from Participants that produce significant reductions in GHG emissions below business as usual levels.

102. The Parties believe it is vital that the NZETS is efficacious because the consequences of it not working are unacceptable. The unacceptable consequences of an NZETS that does not work include that:

- a. Instead of providing the 'good example' of domestic climate change policy that other larger countries might follow, the NZETS would provide a case study for why emissions trading does not work – potentially doing irreparable damage to global emission reduction efforts.
- b. Government, being committed to reducing GHG emissions would be compelled to supplement or replace the NZETS with alternative climate change policy – potentially regulated emission limits or a tax – which the Parties consider highly undesirable.
- c. Countries that import New Zealand products may be unimpressed by our emission reduction efforts and more inclined to impose trade measures that penalise GHG emission inaction.
- d. The considerable expense of designing, implementing and participating in the NZETS will have been a total waste of resources.

103. The Parties' key concern is that, should processors be made the 'Participants' in the NZETS, farmers, who own the livestock and processes that create the vast majority of the sector's GHG emissions, will not be directly exposed to the relevant market forces and therefore not incentivised to take action that reduces net GHG emissions.

104. The Parties understand that a Technical Advisory Group (TAG) has been established and tasked with investigating and setting out options for how the scheme could work with the participant at various points throughout the sector. The Parties are unclear, however, how one of these options will be selected and, if necessary, enacted through order in council.

105. The Parties submit that while there is a need to consider all options and also a desire for administrative ease, the pre-eminent consideration should be that the scheme achieves the objective of incentivising farmers to take GHG reducing action.

106. The Parties believe that it should be precondition for those options investigated by the TAG, that the NZETS would be efficacious under that given option.

107. The Parties believe that a prima facie examination of the 'processors as Participants' option suggests that the precondition of efficacy for the NZETS would not be met.

Side-note on upstream versus down stream point of obligation

The Parties understand that in the case, for instance, of petrol sales, it makes sense for the fuel wholesaler to be the participant because wholesalers can easily add a cost of carbon to each unit of product sold and consumers will rightly bear this expense. In the case of fuel there is a reasonably fixed relationship between the amount of fuel consumed in a motor vehicle and the amount of carbon dioxide released into the atmosphere. There is very little motorists can do to reduce their CO₂ emissions except to use less fuel – either through efficiency or reduced activity.

There is no need to audit or verify that a motorist has emitted a given amount of carbon dioxide; if they have bought and used fuel, they have emitted a known amount.

In contrast, the relationship between the number or weight of animals delivered to a meat processor and the emissions produced on the farms where those animals were raised is by no means fixed. There may be, in future, a variety of techniques that a farmer can adopt in order to improve his or her farm's emissions performance.

It will be a complex task to assess what a given farm's emissions have been in a given year. Farmers may, for instance:

- a. Be more or less efficient in terms of outputs per input (demonstrated for example in higher lambing percentages).
- b. Use new technologies like nitrification inhibitors or feed pads where those are applicable.
- c. Be more or less responsible in fertiliser practices.
- d. Use animal phenotypes that produce more or less methane.
- e. Use livestock feeds or feed regimes that produce more or less methane.

If domestic policy intends to encourage emissions reducing practices among farmers then it must recognise, measure (or estimate) their effect and reward those practices accordingly.

If policy makers expect the NZETS to be efficacious and also expect meat processors to be 'Participants', then they must also expect processors to undertake recognition, measurement and reward activities. This is an unreasonable and unrealistic expectation.

Aside from issues of fairness and equity, processors are unlikely to be able to derive commercial benefit from establishing mechanisms to pass on the rewards of emissions reducing behaviour. Instead, emissions liabilities would likely be considered a tax, and passed through to all farmers in equal measure.

Even if some of the larger processors elected to implement systems whereby suppliers could be rewarded for good emissions practice, the Parties consider that from a cost-benefit perspective, the idea of multiple processors designing and implementing separate systems does not make sense.

Recognising, assessing and rewarding good emissions practice is most sensible undertaken by a single agency on a consistent basis.

108. The Parties believe that, in respect of Agriculture, an NZETS in which processors were Participants would be highly inefficient, and most likely wouldn't work. Processors in the meat industry are unlikely to take on the responsibility of passing through GHG mitigation price signals, and will instead treat any GHG liabilities as a tax, the costs of which would be spread evenly among

suppliers. Without direct exposure to the carbon market, farmers will have no incentive to improve their GHG emission performance.

109. The key argument for an 'all sectors, all gasses' scheme is that the lowest cost opportunity to mitigate emissions can be identified and utilised by the whole economy. If the agricultural sector is not effectively exposed to drivers to identify mitigation opportunities, then the economic argument for an 'all sectors, all gases' scheme does not hold and there is no point in including this sector in the scheme.

110. To ensure that farmers are motivated to take action to mitigate, such as the investment in and adoption of new technology, the NZETS agency must deal directly with those farmers as Participants – just as the Bill proposes it should deal directly with foresters.

Recommendation 5

111. The Parties recommend that Schedule 3 of the Bill be altered such that the default 'Participants' responsible for ruminant animal emissions are farmers, not processors.

Cost recovery

112. Paragraphs (5), (6) and (7) of section 148 of the Bill set out that regulations may be created by Order in Council that prescribe fees for the recovery of costs incurred in government's administration of the NZETS. The Parties are strongly opposed to the administration costs of the NZETS being recovered from Participants, or any other member of industry.

113. The Parties note that participation in the NZETS will be compulsory and expect that the costs of participation are going to be significant on their own. Adding to those participation costs, the government's costs of administering the scheme may cause economic damage, even before GHG emissions liabilities are taken into account.

114. The Treasury's guidelines on cost recovery⁴, state that *"There is a good case for recovering the costs of a public good from the community as a whole, either by general taxation, or (where the benefits are localised) from local government revenue"*.

115. The Parties consider the NZETS, and climate change policy in general, to be a perfect example of a 'public good'. The ultimate intent of the NZETS is the mitigation of climate change, and this would clearly have beneficiaries much wider than the Participants in the NZETS.

116. The only other major consideration highlighted in The Treasury's guidelines is the role of 'risk exacerbators' in creating the need for government intervention. The Parties would argue strongly that the risk exacerbators, in the case of the NZETS, are the world's consumers of products that contribute to GHG emissions – primarily fossil fuels.

Side-note on agriculture's contribution to climate change

It is generally accepted that methane and nitrous oxide, which are produced by agricultural and other processes⁵, are powerful greenhouse gasses; i.e.: they have the effect of absorbing energy radiated from the earth's surface thereby trapping heat in the atmosphere.

In agriculture, relatively innocuous forms of carbon and nitrogen are converted to methane and nitrous oxide through farm processes. For instance, in New Zealand, atmospheric carbon dioxide is converted by grasses and clover into complex carbohydrates that are eaten by ruminant animals. Bacteria in the gut of the ruminants

⁴ The Treasury; Guidelines for Setting Charges in the Public Sector, December 2002

⁵ Ruminant emissions are estimated to make up about 28% of global methane emissions (US EPA)

convert those complex carbohydrates partly into sugars absorbable by the animal, and partly into methane. The methane released into the atmosphere has a finite lifespan (a 7-year half-life) – at some point it will degrade back to its constituent carbon dioxide (and water).

Similar processes have been at work for as long as there have been ruminants eating grass or natural fermentation sources such as wetlands.

So, the average carbon atom has always spent a portion of its time in the atmosphere in the more potent greenhouse gas form of methane, and the majority of its life as carbon dioxide or trapped in solid form. Agricultural and similar biological processes do not add to the total balance of carbon in the atmosphere (in fact some have suggested that pastures can gradually accumulate soil carbon, thereby reducing atmospheric carbon).

Fossil fuel users add to the greenhouse gas effect every time they start their engine, because this process takes carbon from underground stores and injects it into the atmosphere. In contrast, New Zealand farmers only add to the greenhouse gas effect when they increase the rate at which they convert carbon dioxide to methane – by the marginal change in ruminant animal numbers – a tiny change compared to the rate at which people burn fossil fuels.

Notwithstanding the fact that fossil fuel use is the cause of the climate change issue, it is clear that ruminant animal farmers have the potential to positively influence global GHG levels if they can reduce the amount of methane and nitrous oxide that is produced by agricultural processes.

117. While it is agreed that New Zealand Agriculture has the ability to contribute small reductions in global atmospheric GHG levels, it is unfair to argue that New Zealand agriculture has created the need for the NZETS. The primary cause of GHG emissions growth and consequentially the need for the NZETS (and all other emissions trading schemes) is the extraction and combustion of fossil fuels. The Parties do not believe that New Zealand sectors' contribution to the requirement for the NZETS justifies the costs of the NZETS being recovered from those sectors.

Recommendation 6

118. The Parties recommend that paragraphs (5), (6) and (7) of section 148 of the Bill be deleted and that the administration of the NZETS be funded through general taxation.

Detail yet to be determined

119. The Parties note that there are a large number of aspects of the operation of the NZETS that have not yet been determined and are not expected to be determined through future legislative process. Important aspects that are not finalised in the Bill include:

- a. The determination of Participants in agriculture.
- b. The allocation of free units between members of sectors.
- c. Thresholds of emission activity for application of aspects of the NZETS.
- d. Methodologies for the calculation of emission liabilities.
- e. Recognition (for the purposes of calculating emissions liabilities) of mitigation measures or technologies.

120. Many of these yet-to-be-determined policy details have major ramifications for the overall efficacy of the NZETS and for the livelihoods of prospective Participants. It is vital that those prospective Participants and the broader community are thoroughly consulted before Orders in Council are made.

121. Whilst the Bill sets out that those yet-to be determined details will be determined by Order in Council and not by new or amended legislation, the Parties would urge government to adopt a consultative approach to determining these details as if it were undertaking a legislative drafting process.

122. The Parties note that the Bill could easily be amended to determine a process by which key future decisions were publicly debated prior to final determination, as is set-out currently in the allocation plan development process.

Part IV: Comments on the Explanatory Note accompanying the Bill

Objective of the Bill

123. The stated objective for the NZETS is as follows:

"That a New Zealand Emissions Trading Scheme support and encourage global efforts to reduce global greenhouse gas emissions by:

- Reducing New Zealand's net emissions below business-as-usual levels; and*
- Complying with our international obligations, including our Kyoto protocol obligations; while maintaining economic flexibility, equity and environmental integrity at least cost in the long term."*

124. The Parties approve broadly of this stated intent but would note that; (1) reducing New Zealand's net emissions and; (2) complying with Kyoto, will not achieve the overall objective of lower global emissions if there is 'leakage' of New Zealand's emissions to other countries not participating in international protocols. If carbon leakage occurs this would undermine the environmental integrity of the scheme.

125. Further, the Parties would make the following comments in relation to the stated objective:

- New Zealand's GHG emissions are insignificant on a global scale, and any reductions made by New Zealand, on its own, will have negligible impact on the global prevalence of atmospheric GHGs.
- The New Zealand Government's best hope of contributing to global GHG reduction is to set a good example for others.
- Setting a good example may provide confidence for other countries to act, and may convince other countries and their consumers that NZ products are produced in a manner that is responsible in respect of GHG emissions.
- In order to provide a good example and confidence to other countries, it is imperative that the NZETS actually works – that is, that it:
 - Has the effect of reducing global GHG emissions below the 'business as usual' levels that would otherwise have occurred.
 - Is not prohibitively costly either in terms of administrative burden or economic and social impact.

Regulatory Impact Statement

Staged entry of sectors into the NZETS

126. Under the terms of the Bill, the sheep, beef and deer sector will be exposed to substantial new costs with the introduction of liquid fuels in 2009, stationary energy in 2010 and livestock emissions in 2013.

127. The Parties strongly support the proposal to delay the entry of Agriculture to the NZETS until 1 January 2013. The Parties believe that, as a biological system, the techniques for quantifying and reporting agricultural GHG emissions will be highly complex and industry members and officials will need at least 5 years to properly prepare for the NZETS.

Impacts and sector specifics

128. The Parties were disappointed with the quality and quantity of quantitative analysis presented in support of the policy parameters chosen for the NZETS.

129. Analysis of the potential impact of the ETS on the agricultural sector seems to be isolated to 12 numbers setting out possible impacts on payout to agricultural producers. For example, the potential for a 42.8% reduction in the payout to venison farmers is highlighted without any further discussion or consideration of the up and down-stream effect of such an unsustainable change of circumstances.

130. Unless the intent of the Bill is that venison farmers should all go out of business, then there must be some assumption that they would be able to mitigate or offset the reduction in payout somehow, but no analysis of how this might be achieved, or at what cost, is included or mentioned. Analysis in this area is unsatisfactory.

Risk Assessment

131. The Parties consider that the risk assessment section adequately categorises most of the major categories of risk associated with the ETS, but that the proposed mitigations for each of those risks are glib, uncertain, poorly defined and do not seem to relate to the ETS as proposed in the Bill.

132. The Parties consider that the key risks associated with the ETS relate to:

- The market for carbon credits, including:
 - Volatility of prices.
 - Unexpectedly high prices.
 - Lack of liquidity (availability) in markets.
- Leakage – the potential for firms to transfer, or prefer to make new investments offshore, where no costs for GHG emissions are realised.

133. The Bill's risk assessment section addresses these risks as follows:

- Risk: - Carbon market volatility/liquidity
- Mitigations: - Play an active role in international agreements...
- Enable the development of financial instruments...
- Consider measures to reduce the initial volatility...
- Ensure as much liquidity as possible by linking to international markets...
- Consider the effects of government allocation decisions...

134. The Parties submit that these proposed mitigations provide no certainty and little confidence that serious problems with the availability of carbon credits and the stability of their prices will be adequately addressed.

Recommendation 7

135. The Parties recommend that the Bill incorporates provisions for the guaranteed availability to industry of government held carbon credits at a capped price.

- Risk: - Unexpectedly high price of credits
- Mitigation: - Government will need to make ongoing decisions about what further international agreements NZ is prepared to sign-up to...

136. The Parties submit that in the context of the Bill as set-out, NZ's signing or not signing up to international agreements has little or no bearing on the price of carbon credits.

137. The Parties submit that an excessive price of credits can only be effectively mitigated by a commitment by the government to sell at a capped price, as set out above.

Risk: - Loss of firms or production (leakage)

Mitigation: - Government will look to provide an assistance package to reduce risk of firms shifting operations offshore as a result of the ETS.

138. The Parties are not certain whether such an assistance package is the same as that detailed under Subpart 2 – Allocation of New Zealand Units but for the purposes of this submission will suppose that it is.

139. The Parties do not believe that the risk of leakage of production from New Zealand has been so carefully quantified that the government can determine that a certain level of assistance in year one, phasing out to zero by 2025 is going to be sufficient to mitigate that risk.

140. The Parties have recommended, in Part III of this submission, that the Bill incorporates provisions for the periodic determination of the level of assistance that given sub-sectors require, and the delivery of that assistance, in order to mitigate the risk of loss of firms or leakage of production from New Zealand. This determination would include such measures such as changes in the intensity of emissions per unit of output, mitigation potential and climate change policy in competitor countries.

Consultation

141. The view of the Parties is that the *Consultation* discussion within the explanatory note of the Bill takes a 'rose tinted' view of the consultation process and deals very offhandedly with some of the very relevant and important concerns raised in public fora. One area of concern, for instance, that has been raised by a number of eminent economists, is the potential for lack of liquidity in the New Zealand carbon market. The *Consultation* and following discussions give the Parties no comfort that the liquidity issues will be satisfactorily remedied.

Part V: Submission on particular clauses of the Bill

Amendments to the Climate Change Response Act 2002

"Part 4 "New Zealand greenhouse gas emissions trading scheme

Section 54 – Participants (Including Schedules 3 and 4)

142. The Bill sets out that the 'default' Participants in the NZETS who will be responsible for the emissions associated with the raising of ruminant animals are those who slaughter those animals.
143. It is the strongly held view of the Parties that the NZETS will not be efficacious in promoting changes in behaviour or technology relating to on-farm GHG emissions should meat processors be made the Participants responsible for ruminant animal emissions.
144. The Parties believe that in order to improve the GHG emissions performance of the pastoral sector, farmers must have a clear view of the market signals that are intended to be created through the NZETS.
145. The Parties believe that expecting meat processors to assume responsibility for effecting on-farm behaviour change in relation to GHG emissions is unreasonable and unrealistic.
146. The Parties believe that farmers have a right to be able to manage their own liability around GHG emissions, just as foresters (including many farm foresters) are proposed to be given the right to manage their own GHG removal assets.
147. The Parties believe that encumbering meat processors with the commercial liability for purchasing many hundreds of millions of dollars worth of carbon credits on behalf of farmers is grossly unfair and would constitute a dangerous concentration of commercial risk in firms that have no experience in managing such risk.
148. The Parties are aware that the Ministry of Agriculture and Forestry (MAF) has established a Technical Advisory Group (TAG) tasked with identifying viable options about which industry members could act as Participants. The process for then selecting one of those options is, however, opaque. The Parties believe that to reach what seems the common-sense determination – farmers as Participants – should not require trust in an opaque, non-legislative process.
149. The Parties have recommended, in Part III of this submission, that the Bill be amended such that the default Participants for ruminant animal emissions are farmers, not processors.

Section 62 – Monitoring of emissions and removals

150. The Bill sets out that Participants are required to collect information relating to GHG producing activities and from that information, calculate the emissions for which they are responsible. The Bill also sets out that Participants will be required to submit emissions information and will be held accountable for its veracity, with severe penalties for error or omission.
151. Notwithstanding that the Parties recommend that meat processors not be made Participants, the Parties are concerned that should meat processors be made Participants, they will be held accountable for GHG emissions information that can only be provided by farmers.
152. For the NZETS to be efficacious, farmers need the ability to be recognised for improved emissions behaviour (other than ceasing or reducing farming activities). To recognise such improved

behaviour, the NZETS will need to collect information relating to on-farm practices, such as the use of new management techniques, technologies or improved plant or animal varieties. The government has discussed using a tool such as Overseer for this purpose.

153. Should meat processors be made Participants, they would need to make emissions returns incorporating on-farm emissions performance data, and under the Bill as drafted would be accountable for that data, but would not own that data or have the capability to verify it. This situation would likely result in meat processors making overly conservative estimates of emissions performance improvement, to avoid legal risk, and farmers, consequentially receiving no or insufficient recognition for their mitigation efforts.
154. The Parties believe that the problem identified above further supports the recommendation above, that meat processors should not be Participants under the NZETS.

Recommendation 8

155. Should (despite the Parties earlier recommendation) meat processors be made Participants in the NZETS, the Parties recommend that the Bill be modified such that meat processors are not held legally accountable for the provision of information that they do not 'own' and do not have the capability to verify.

Section 68 – Allocation plans for allocation of New Zealand Units free of charge

(And also Section 73 – Statement of intention to prepare draft allocation plan and Section 74 – Preparation of draft allocation plan.)

156. As set-out in Part III of this submission, the Parties recommend that the process that has been set-out in the Bill for development of allocation plans be amended. In particular, the Parties recommend that the Bill provides for:
- a. Allocation plans to be redrafted on a periodic basis, and modified if necessary.
 - b. The allocation plans should determine the total envelope of assistance available to given sets of Participants (and not be subject to those caps on the availability of assistance as set-out in sections 69 to 71).
 - c. The Minister's decision making in the allocation plan development process is supported by a commission of independent experts.
 - d. Allocation plans are drafted at the level of individual sub-sectors (meat, dairy, etc) which are subsets of the broad sector groupings currently set-out in the Bill.
157. The Parties note that the wording of section 68 envisages the allocation of free units to "*persons or classes of persons*" and there is no requirement that those persons be Participants in the NZETS. This, presumably, allows for a situation where, for instance, processors are Participants but free allocations are provided to farmers.
158. The Parties consider that in the agriculture sector, allocating free units to persons other than the Participant would be highly inefficient. Problems with such an approach would include;
- a. The requirement for a vast number of small transactions for Participants to purchase the units that have been freely allocated to alleviate damage to their industry.
 - b. Participants may become distracted by focussing on the procurement of units from free allocation recipients, at the expense of their core business.
 - c. The potential for freely allocated units provided to an industry to be sold to another industry or offshore, and the Participant being unable to source sufficient units when required to surrender. An industry as a whole could thereby default on its liability (by bankrupting a Participant) whilst realising the value of freely allocated units.

- d. That there is the potential that income from the sale of freely allocated units to Participants would be taxable, thus automatically discounting the value of freely allocated units (as discussed later in this submission).

159. The Parties believe that industries in which Participants are not the recipients of free units would face greater costs, and a competitive disadvantage compared to those in which free allocations were made directly to Participants.

Recommendation 9

160. The Parties recommend that the Bill be amended such that, in relation to agricultural emissions, free units are only allocated to persons that are Participants in the NZETS.

161. The Parties consider that in certain instances, the distribution of a sub-sectors' free allocations of units would most sensibly be managed on a per-unit of output or intensity basis. This would deal with the potential problems around the treatment of new entrants and also reduce the effect of a restricted supply of units dis-incentivising marginal production increases.

Section 70 – Allocation to industry

162. While the Parties are not aware of any logical basis for the proposal of 90% of 2005 emissions levels as the initial level of free allocation of emissions units, the Parties accept that this is probably a reasonable starting point for free allocation to Industry, subject to the level of free allocation being reassessed and adjusted as necessary as part of the allocation plan process (as previously recommended).

163. The Parties would note however, that in theory, within the NZETS framework, the level of free allocation of emissions units is not likely to affect the motivation of market Participants to reduce emissions. Even if Participants have enough, or more than enough free units to offset their liability, further emission reductions have a monetary value and rational Participants will continue to pursue any mitigation options that have a net benefit. Motivation to reduce emissions is only hampered where free allocations are so high that there is a surplus of units available and the unit price falls significantly, as per the European ETS. This seems unlikely in the NZETS as many Participants are considered to be not trade exposed and will rightly receive no free allocation.

164. As recommended in Part III of this submission, the Parties believe that paragraph (2)(c) of section 70 should be deleted and the Bill should contain no specification of 'phase-out' of freely allocated emission units to industry.

165. The Parties believe that there is merit in recognising early mitigation action on the part of industrial emitters who may have made significant reductions in emissions shortly prior to 2005. The Parties are unclear how this will be possible under the Bill given that the total envelope of free units is set at 90% of 2005, but that Participants that wish to use 90% of earlier years as the basis for free allocation will most likely have had higher emissions in those earlier years than in 2005.

Recommendation 10

166. The Parties recommend that the Bill provides that trade-exposed firms may use 2003, 2004 or 2005 as the base year from which free allocation of assistance entitlement is calculated.

167. The Parties do not understand any logical basis for allocating assistance only on the basis of trade-exposed firms' exposure to greater gas, coal, steam and electricity costs, whilst omitting any reference to costs increases related to emissions liabilities from transport fuel usage. The same principles of protecting competitiveness at risk and avoiding carbon leakage must surely apply.

Recommendation 11

168. The Parties recommend that section 70(1)(b) be amended such that trade exposed firms may be allocated free units in relation to higher costs resulting from liabilities associated with the use of transport fuels.

169. The Parties are concerned that the wording of section 70 erroneously limits allocation to industry to the owners of 'industrial processes such as smelting and cement making. 70(1)(b) requires recipients of allocations to have 'specified emissions' and 70(4)(a) defines specified emissions as coming from activities in Part 4 of Schedule 3 – 'Industrial Processes'.

Recommendation 12

170. The Parties recommend that Section 70(4)(a) be amended such that industrial emitters other than the owners of 'industrial processes' are eligible for free allocation.

Section 71 – Allocation to agriculture

171. The Parties are not aware of any logical basis for the proposal of 90% of 2005 emissions levels as the initial level of free allocation of units to Agriculture. The Parties are concerned that, in agriculture, the reference to 2005 emissions levels, as opposed to 1990 levels (upon which New Zealand's Kyoto liabilities are based) will favour some sub-sectors over others. Between 1990 and 2005, the sheep and beef sub-sector has substantially reduced both its GHG intensity (emissions per unit of output) and its total volume of emissions, whereas other sub-sectors have not. The Parties therefore accept the proposal set out in section 71(2)(a), subject to:

- a. The level of free allocation being reassessed and adjusted as necessary as part of the allocation plan process (as previously recommended).
- b. The sheep and beef sub-sector being recognised for its early action in mitigating GHG emissions by the use of 1990 as the basis for its allocation of assistance.

172. As recommended in Part III of this submission, the Parties believe that paragraph (2)(c) of section 71 should be deleted and the Bill should contain no specification of 'phase-out' of freely allocated emission units to agriculture.

173. The Parties intend to develop a process to identify an initial equitable approach to allocation within the Agriculture sector as defined in the Bill under the cap of 90% of 2005. While international competitiveness, carbon leakage and mitigation potential issues will be unique for each sub-sector (such as the sheep, beef and deer sub-sector and the dairy sub-sector), there is a desire from the pastoral sector to be responsible in the first instance to develop an initial allocation plan for sub-sectors within Agriculture for the consideration of the Minister. It is proposed that a cross-sector pastoral group provide a recommendation to the Minister regarding intra-sector allocation.

Section 72 – Persons not eligible for allocation of New Zealand units free of charge

174. The Parties note that section 72(b) sets out that free units will not be allocated to any "persons specified in sections 69 to 71 in respect of any period other than a period specified in those sections". The Parties also note that the only period specified in section 70 (Allocation to industry) is "1 January 2014 to 31 December 2024". This seems to suggest that the industrial sector would only be eligible for free allocations from 2014 – 4 years after it is proposed to enter the NZETS. The Parties did not understand this to be the intent of the Bill.

Recommendation 13

175. The Parties recommend that section 72(b) be amended to clarify that allocation will not be made in respect of sectors that have not yet commenced participation in the scheme, but upon entry of a sector to the scheme, relevant persons will be eligible for free allocations.

Section 147 – Reviews of operation of emissions trading scheme

176. The Parties approve of the requirement to comprehensively review the operation of the NZETS but consider that the timing for the proposed review, as set out in the Bill is too late, in the first instance, and too infrequent thereafter.

177. The wording of section 147 requires that review be completed “*within 9 months before the end of [...] the first commitment period [being the end of 2012]*”. The Parties interpret this to mean that the initial review’s findings could be passed to audiences the day before agricultural industries are about to commence participation in the NZETS. This outcome would clearly preclude recommended modifications being made to the design or operation of the ETS prior to the entry of agriculture into the scheme.

Recommendation 14

178. The Parties recommend that paragraph (1) of section 147 be amended to require that the first review of the NZETS be completed at least 12 months prior to the end of the first commitment period.

179. The Parties believe that circumstances relevant to the NZETS are likely to change much more rapidly than can be predicted over a 5-year review period. Technology or practices to mitigate on-farm GHG emissions for instance, may develop over a 1 or 2 year timeframe, and in order to drive the development and uptake of such technologies or practices, the NZETS must rapidly recognise their contribution. The Parties believe that the Bill should require that issues such as new technology be reviewed more frequently than 5-yearly.

Recommendation 15

180. The Parties recommend that paragraph (1) of section 147 be amended to require that reviews of the NZETS are undertaken biennially or annually.

Section 148 – Regulations – Paragraph (1)

181. The Parties note that paragraph (1)(b) of section 148 of the Bill sets out that regulations may be made, by Order in Council, that prescribe the methodology for calculating emissions for the purposes of emissions returns. While the Parties understand that such methodologies are not yet well-enough understood to describe in the Bill, they believe that the Bill should set-out the key principles that will be followed when determining emissions calculation methodologies.

182. Understanding the principles of the NZETS, with respect to emissions calculation methodologies would provide Participants with greater certainty and motivation to invest in ventures intended to mitigate emissions in a given sector.

Recommendation 16

183. The Parties recommend that the Bill be amended to incorporate principles to be followed when setting regulations that determine the methodologies for calculating GHG emissions for the purposes of the NZETS, and that those principles include that:

- **All scientifically proven mitigation techniques are incorporated in calculations, not just those recognised within international agreements.**

- **Methodologies shall be updated to incorporate newly developed and/or accepted climate science, such as new estimates of Global Warming Potentials for various GHGs.**

184. The Parties strongly believe that in the interests of the efficacy of the NZETS, all proven mitigation techniques should be recognised and incorporated into emissions calculation methodologies.

185. The consequences of not immediately recognising new mitigation techniques (and instead only recognising those accepted within international agreements) would be that:

- a. Potentially useful mitigation techniques would not achieve widespread uptake (there being no financial driver to adopt the technique) and would therefore not be widely demonstrated as effective, and would be much more difficult to get included into international agreements (i.e. to receive UNFCCC approval).
- b. For even the most robust techniques, potential developers of new mitigation techniques would expect a delay between development expenditure and income – as determined by when customers would realise a return on their own investment following international recognition of that technique.

186. The Parties believe that the consequences of not recognising all proven mitigation techniques in emission calculation methodologies would handicap investment in emission mitigation technologies and thereby impede the efficacy of the NZETS and global progress toward GHG mitigation.

187. The Parties believe that, in respect of the sheep, beef and deer subsector, until there are sufficient cost-effective mitigation technologies, compliance costs should be kept to a minimum. This could be achieved through two-tier system for calculating emissions.

188. Those producers who do not want to measure and report carbon can opt for a carbon charge system on production (possibly with industry aggregation for those whose situation doesn't suit being involved in ETS at a point in time). Those who do want to opt in can measure and submit detailed carbon returns including their specific mitigation activities. This would provide a transition phase until technology, markets and general understanding develops sufficiently and effective application of mitigation technologies are realised. The objective of this system would be to keep compliance costs to a minimum while still providing an incentive for reducing total emissions.

Recommendation 17

189. The Parties recommend that in order to minimise on farm administrative costs, the Minister allows for a two-tier system for calculating on-farm emissions, whereby farmers can opt in to providing detailed emissions returns or have a return calculated for them using default assumptions.

Section 148 – Regulations – Paragraphs (5), (6) and (7)

190. As recommended in Part III of this submission, the Parties believe that the NZETS is a pure 'public good' initiative and as such, its administration should be funded out of general taxation.

191. The Parties have recommended that paragraphs (5), (6) and (7) of section 148 of the Bill be deleted.

Part 5: Sector Specific Provisions

Section 178 – Transitional provision for penalties

192. The Parties support the adoption of a 'grace period' period in which errors in information provided to government will not be punished. This seems a common-sense approach given that

participation in the NZETS will be a learning experience for all involved and that honest mistakes will inevitably be made in the early stages.

Amendments to the Income Tax Act 2004 Page 118

Clause 47 of the Bill - CB 29 - Disposal of ETS units

193. The Parties note that Clause 47 of the Bill amends the Income tax Act 2004 to insert a new heading and section that defines amounts received from the disposal of ETS units as income, for tax purposes. Transactions to surrender units directly to the NZETS attract no tax liability.

194. The Parties further note that government has discussed during consultations, and the Bill does not preclude, the possibility that free units could be allocated to persons who are not the Participants in the NZETS. The Parties have recommended earlier that the Bill be amended to preclude this eventuality within the agriculture sector.

195. If non-Participants are allocated free units, those units must be sold, as recipients have no ability to surrender them directly to the NZETS. If the proceeds of a sale are taxable, then the utility of those freely allocated credits is immediately discounted, placing the recipient at an unjustifiable disadvantage in comparison to those free unit recipients who are also Participants in the NZETS.

Recommendation 18

196. The Parties recommend that amounts received by non-Participants, in return for disposal of freely allocated units, not be considered income for the purposes of taxation.

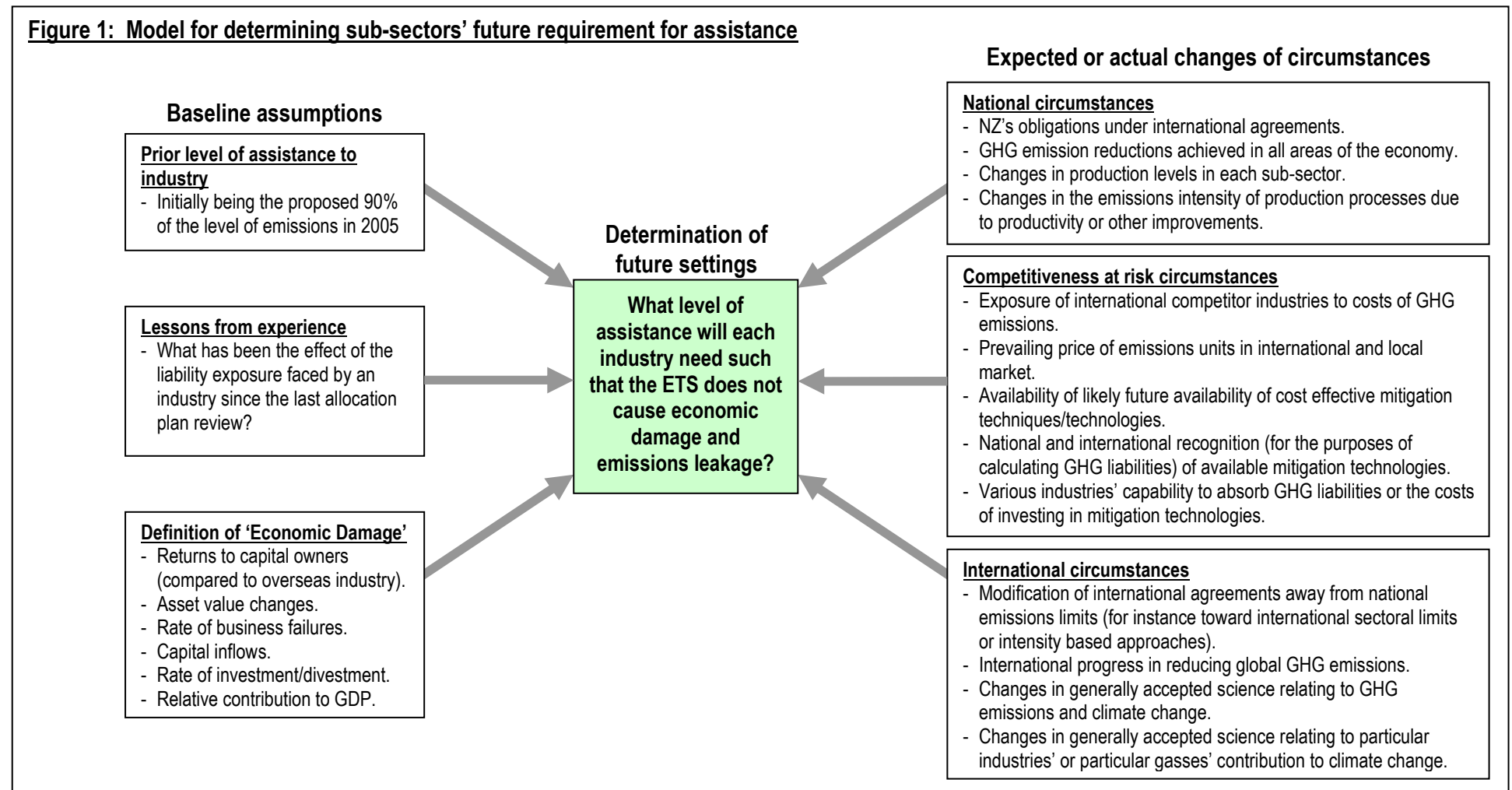
Appendix 1: Members of the Meat Industry Association

Members	Head Office Location
Advance Marketing Ltd	Auckland
AFFCO New Zealand Ltd	Hamilton
Alliance Group Ltd	Invercargill
ANZCO Foods Ltd	Christchurch
ANZCO Green Island Ltd (ANZCO group)	Dunedin
ANZPAC Foods Ltd	Auckland
APJ Meats Ltd	Mapua
Auckland Meat Processors Ltd	Auckland
Ballande New Zealand Ltd	Auckland
Bernard Matthews New Zealand Ltd	Waipukurau
Blue Sky Meats (NZ) Ltd	Invercargill
<i>Brookland (NZ) Ltd (in receivership)</i>	<i>Auckland</i>
Canterbury Meat Packers Ltd (ANZCO group)	Ashburton
Columbia Exports Ltd	Auckland
Crown Marketing Ltd (ANZCO group)	Wellington
Crusader Meats New Zealand Ltd	Benneydale
Davmet New Zealand Ltd	Napier
Fern Ridge Ltd	Napier
Frasertown Meat Company Ltd	Auckland
Garra International Ltd	Christchurch
Greenlea Premier Meats Ltd	Hamilton
Harrier Exports Ltd	Auckland
Horizon Meats New Zealand Ltd (wholly owned subsidiary of Blue Sky Meats (NZ) Ltd)	Auckland
Lamb Packers Feilding Ltd (wholly owned subsidiary of Bernard Matthews NZ Ltd)	Waipukurau
Land Meat (NZ) Ltd (AFFCO group)	Hastings
Lanexco Ltd	Tauranga
Lowe Corporation Ltd	Hastings
Mathias International (Mathias Meats NZ Ltd)	Auckland
New Zealand By-Products	Havelock North
Pilot (NZ) Ltd	Christchurch
PPCS Ltd	Dunedin
Progressive Gisborne Ltd (wholly owned subsidiary of Bernard Matthews NZ Ltd)	Waipukurau
Progressive Meats Ltd	Hastings
Riverlands Ltd (ANZCO group)	Eltham
South Pacific Meats Ltd (AFFCO group)	Invercargill
South Pacific Meats - Malvern (AFFCO group)	Malvern
Tara Exports Ltd	Auckland
Taylor Preston Ltd	Wellington
Te Kuiti Meat Processors Ltd	Te Kuiti
Towers Thompson (New Zealand) Ltd	Christchurch
Universal Beef Packers Ltd (UBP)	Te Kuiti
Wallace Corporation Ltd	Waitoa, Waikato

Affiliate Members	
AgResearch-MIRINZ Centre	Hamilton
Aon New Zealand Limited	Wellington
Axis Intermodal (Ports of Auckland Ltd)	Auckland
CentrePort Wellington	Wellington
DeLaval Cleaning Solutions	Hamilton
Energy for Industry (ex Meridian Solutions)	Wellington
GHD Ltd	Palmerston North
Hamburg-Sud New Zealand Ltd	Auckland
Hapag Lloyd (New Zealand) Ltd	Auckland
Maersk New Zealand Ltd	Auckland
Millers Mechanical NZ Ltd	Dunedin
NZI Marine	Auckland
Oceanic Navigation Ltd	Auckland
Port of Napier	Napier
Port Otago Ltd	Port Chalmers
Port Taranaki Ltd (previously Westgate Transport Ltd)	New Plymouth
Sealed Air (New Zealand), Cryovac Division	Wellington
Vero Marine Insurance	Auckland

Appendix 2: Proposed mechanism for flexible allocation of assistance

- Figure 1, below, summarises the sheep, beef and deer industry's proposed methodology for assessing the requirement of individual sub-sectors for free allocation of emission units.



Application of the proposed Model for determining free allocations

2. The Model illustrated above is a rough outline of those considerations that would need to be taken into account when determining what level of assistance each industry requires in the future.
3. The Model would need to be further developed in order to formularise the decision process as far as possible. This would involve precise specification of the quantitative indicators for each of the parameters stated and their relative contribution to the outcome. The objective would be to ensure that the determination of assistance to industries was open to as little interpretation as possible.
4. The Parties propose that as a component of the process to develop Allocation Plans (as currently drafted in sections 68 through 74) the Minister utilise the Model, and a group of independent experts, to determine what level of assistance any given sub-sector should receive in the upcoming allocation period.
5. The Parties recommend that allocation plans should be redrafted on a periodic basis.
6. The Parties recommend that the allocation plan for a given period be completed no less than 6 months before the start of that period, in order to provide sufficient lead time that firms may plan for their likely level of net liability.
7. The allocation plan might determine that an industry requires a flat rate of assistance for each of the period within an allocation period, or that the requirement for assistance will change over that period.
8. The Parties recommend that the Bill requires the Minister to enlist the advice of a group of independent experts in producing allocation plans (including determining the appropriate level of assistance to industries). That group of experts would include individuals with expertise in:
 - a. Economic impact analysis.
 - b. International climate change agreements.
 - c. GHG mitigation technology relevant to particular industries.
 - d. The domestic climate change policy of overseas trading and competitor countries.
 - e. International climate science consensus.
 - f. Administration and management of the NZETS.
9. The Parties recommend that the Minister develop allocation plans for individual 'Sub-sectors' as opposed to the high-level sectors currently defined in the Bill. 'Sub-sectors' would, for instance, separate meat and dairy from within the current 'Agriculture' sector defined in the Bill, and probably significant industrial processes such as metal smelting and cement manufacture from the 'Industry' sector currently defined.
10. The Parties believe that a lower-level definition of sub-sector groups is appropriate given that competitiveness at risk circumstances, ability to migrate and intensity based indicators may be quite different for different industries. For instance, technologies might appear that drastically reduce emissions from smelting, but which have no application in cement manufacture. This would reduce the smelting industry's requirement for free allocation. Similar examples are conceivable within the 'Agriculture' sector.