



Climate Change Response (Moderated Emissions Trading) Amendment Bill

85—1

Report of the Finance and Expenditure
Committee

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Climate Change Response (Moderated Emissions Trading) Amendment Bill

Recommendation

The Finance and Expenditure Committee has examined the Climate Change Response (Moderated Emissions Trading) Amendment Bill and recommends that the House take note of its report.

Conclusions

We were unable to reach agreement on whether to recommend that the Climate Change Response (Moderated Emissions Trading) Amendment Bill be passed, because of members' differing views as to the suitability of the bill's proposed changes to the design of the New Zealand Emissions Trading Scheme (NZ ETS). We also could not agree on the kinds of amendments from which the bill might benefit if it were to be passed.

Our report sets out the process that we followed in considering the bill, the main changes proposed to the NZ ETS under the bill, and the minority views of the members from New Zealand National, New Zealand Labour, the Green Party, the Māori Party, and ACT New Zealand.

We recognise that a select committee's report on a bill usually canvasses the committee's views on the substantive policy and drafting issues that the committee confronted in the course of its consideration. However, widely divergent views on this bill amongst our members and time constraints prevented us from reaching agreement on the content of such a committee report. We concluded that it would be more appropriate for each party represented on the committee to have an opportunity to express separately its view on the proposals in the bill and the policy issues raised during our hearings of evidence.

Committee process

The bill was introduced on 24 September 2009 and was referred to us for report by 16 November 2009. By the submission closing date of 13 October 2009 we had received 379 written submissions, the majority of which were from individuals. We heard from 128 submitters over five days between 15 October and 27 October 2009.

We received advice from the Emissions Trading Group, which is made up of advisers from the Ministry for the Environment, the Ministry of Agriculture and Forestry, and the Ministry of Foreign Affairs and Trade; and from the Treasury. We also received advice from an independent specialist adviser, Dr Suzi Kerr, who commented on particular issues that were drawn to our attention by submitters. All the advice and submissions we

received, and a detailed analysis of the submissions, is available on the parliamentary website.¹

The bill as introduced

The bill would amend the Climate Change Response Act 2002 to modify the NZ ETS. The bill as introduced proposes a number of significant changes:

- Free allocations of New Zealand Units would be made to emissions-intensive, trade-exposed industries on an intensity basis. During the transition phase to 31 December 2012, emitters would be required to surrender one unit for every 2 tonnes of CO₂ equivalent emissions, and the level of assistance would be phased out at a rate of 1.3 percent per annum beginning in 2013.
- A transitional phase would operate until 2013, during which time participants in the Stationary Energy and Industrial Processes and Liquid Fossil Fuel sectors would face a progressive unit-surrender obligation, or have an option to pay \$25 per tonne of emissions in lieu of the unit-surrender obligation, from 1 July 2010.
- Entry of the agricultural sector into the scheme would be delayed until 1 January 2015. The default point of obligation for the sector would be set at the processor level, with flexibility to move to the farm level in the future.
- Free allocations to the fishing sector would be increased from 50 percent to 90 percent of 2005 emissions from 1 July 2010 until 31 December 2012. The allocations would be made to quota owners rather than vessel operators.
- A regulation-making power would be created to set a domestic emissions reduction target for New Zealand. It is proposed that this target would specify a target reduction in emissions of 50 percent of 1990 emissions levels by 2050.

New Zealand National minority view

National Party members note that the Climate Change Response (Moderated Emissions Trading) Amendment Bill reflects the principles of an emissions trading scheme that the National Party put to, and which was endorsed by, the New Zealand public at the general election in 2008. National members support changes and amendments to the existing emissions trading scheme to effect these principles.

National Party members are supportive of the bill as introduced plus amendments, both technical and material, as suggested by officials. We believe that the bill strikes a realistic balance between New Zealand's environmental and economic aspirations. The proposed changes are essential to establish a manageable timeframe for introducing the various sectors into the scheme, to ensure that the impact on the economy and therefore consumers is minimised in the first few years, to provide a level of transitional assistance to trade exposed emissions-intensive entities designed to avoid leakage in accordance with our Kyoto commitments, to encourage increased afforestation, and to reduce deforestation.

We note that analysis by the Ministry for the Environment, and peer reviewed by The Treasury, shows that both the existing scheme and the moderated scheme would have a

¹ <http://www.parliament.nz/en-NZ/PB/SC/Documents>

positive fiscal impact but that the existing scheme would extract some two billion dollars a year more from the economy than the moderated scheme. We acknowledge that it is difficult to model and predict scenarios in the long term as there are a significant number of variables, but the proposed review process will ensure that adjustments can be made to allocation phase-out levels and the like to maintain a positive fiscal position over time.

National members support including the design of the emissions trading scheme in the streams of work being undertaken across various ministries as part of the Single Economic Market discussions, with their Australian equivalent, to align or synchronise legislation, rules and regulations.

We are hopeful that New Zealand's negotiating team at the Copenhagen conference can make progress on issues that when applied to the New Zealand emissions profile place an unfair burden on our economy.

New Zealand Labour minority view

Our view

We recommend that the bill should not proceed. It is fundamentally flawed and will make New Zealanders poorer, our economy weaker, and will not curb the growth in our greenhouse gas emissions.

Process

Every part of our consideration of the Climate Change Response (Moderated Emissions Trading) Amendment Bill has been rushed and inadequate, particularly in view of the very substantial economic and environmental costs associated with this bill. This has negated the protection and value that the referral of legislation to a select committee is supposed to promote, to the point where the Finance and Expenditure Committee has been unable to discharge properly its obligations to Parliament in this regard.

Hearing of evidence

The report of the committee correctly records that the bill was introduced on 24 September 2009 and referred to us for report by 16 November 2009, with 379 written submissions having been received when submissions closed on 13 October 2009. After an initial attempt by the chair of the committee to limit the number of oral submissions to be heard to 30 and the hearing of evidence to a single day, Labour, the Greens, the Māori Party, and the ACT Party stipulated that we should hear from any submitter who had dealt with the substance of the bill and who wished to appear before the committee to speak to their submission.

As a result of that stipulation, we heard in total from 128 submitters over 23 hours 35 minutes, spread over five days between 15 October and 27 October 2009. Many submitters were given only a few hours' notice of their invitation to appear before the committee. Other submitters simply declined to appear at such short notice. Those who were heard were allocated a very short time to make their oral submissions. Many submitters expressed dismay that they were called on at such short notice and with such little time to speak on issues of such complexity and importance.

Further amendments to come without committee scrutiny

The evening before the introduction under urgency of the bill, the Minister for Climate Change Issues held a briefing in his office. He foreshadowed a number of further amendments, including a Treaty of Waitangi clause, that were not included in the bill as introduced, and that he said would not be made available until the committee of the whole House. The Minister said that those amendments resulted from an agreement between the National and Māori parties for Māori Party support for the bill. We understand that at the time of agreeing to these amendments, the Government took little or no official advice on the substance and effect of many of these proposed amendments. The Minister made it clear that these amendments would not receive scrutiny from a parliamentary committee nor be the subject of expert evidence or public submission.

Unavailability of supporting information

On Friday 9 October, as the statutory deadlines for responding to a number of requests under the Official Information Act 1982 concerning the rationale for the contents of the bill fell due, the Minister released a series of documents. This release failed to include a number of key documents, including The Treasury analysis of the long term fiscal costs of the proposed amendments, and the detail of the agreement reached between the National and Māori parties over support for the amendments contained in the bill. A number of complaints to the Ombudsman arising out of the release remain outstanding. The Minister's obstructive approach to the release of background information has seriously hampered our scrutiny of the changes proposed in the bill.

Late receipt of official and expert advice

Departmental advice: We received a number of departmental reports at our two final meetings, including reports presented during those meetings. This is extremely poor practice and in its extent and impact is unique in our parliamentary experience.

The main departmental report on the bill was divided into two parts. Part 1 provided a high level overview without supporting analysis. Part 2 purported to provide more detailed advice but omitted, because of time constraints, the usual clause-by-clause analysis of submissions. In a number of key respects it cross-referenced the Stage 1 report rather than providing its own supporting analysis. Because there was little or no analytical base to the Stage 1 report, the committee was left without adequate analytical frameworks or supporting quantitative data to allow it to assess official advice. We also found supplementary reports containing some of the underlying risk and sensitivity analysis to be opaque, lacking in clear data sources and unclear in their juxtaposition of volume and value estimates.

On the last day of our meeting, immediately before deliberating, we experienced probably the worst example of how rushed process contributes to serious error. Officials advised us on the morning of deliberation that The Treasury now estimated the fiscal effect of the vastly higher level of free emission rights for large emitters would be to increase Government debt by an astounding 13–17 percent of GDP by 2050, rather than the already very high

6–8 percent of GDP previously advised to Cabinet. In dollar terms, that is \$110 billion of extra debt.

The Treasury Regulatory Impact Analysis (RIA) was clear that the “level and quality of analysis presented is not commensurate with the significance of the proposals, which represent major design changes to the Emissions Trading Scheme”, and that “the RIS does not provide an adequate basis for informed decision-making”.²

We were told that the official from the RIA Unit responsible for that analysis was not available to brief us further.

Independent expert advice: We received final key independent expert advice from Dr Suzi Kerr, Visiting Professor of Economics, Stanford University, and an international expert in emissions pricing, only on the morning on which we were required to deliberate on the bill. We stress that this was through no fault of the independent expert, but rather because of the impossibly abbreviated timeframes which have applied to this process. At our final meeting, officials told us that they had not had the opportunity to consider Dr Kerr’s final advice to us. As a result, it has been impossible to attempt to improve the bill by incorporating her findings, or other well-founded criticism, into it by way of suggested amendment. This is particularly important, as Dr Kerr’s advice would have been pivotal in allowing the committee to assess the accuracy of other key submissions and advice, especially in regard to economic incentives, costs, and fiscal risks.

Absence of revision-tracked bill: The Parliamentary Counsel Office (PCO) worked diligently under extreme pressure to prepare in advance revision-tracked amendments for the committee. However, PCO made clear that they could not do so on the basis of the usual consideration and decision-making process because of time constraints, and would be able to provide only an untested draft on the day of deliberation. This would preclude normal quality control, and any late amendments in the normal way. In light of all this, we took the extremely rare step of declining to receive a revision-tracked bill from PCO at all.

Comparison with previous climate change legislative process

The Climate Change (Emissions Trading and Renewable Preference) Bill that created New Zealand’s Emissions Trading Scheme was introduced in late 2007 and referred to the Finance and Expenditure committee of the 48th Parliament. The committee received 259 submissions. It heard in person from 161 of them in Wellington, Auckland, and Christchurch, and by telephone and video conference, over 58 hours of hearings. The committee closed submissions on 29 February and reported back to the House on 16 June, recommending extensive changes to the bill as introduced. The legislation received assent on 25 September 2008.

On that occasion, the National Party submitted a minority view that summarised its heavy criticism of the process adopted. Throughout, that criticism was carefully orchestrated with the heavy emitter lobby’s campaign against emissions trading. It is heavily ironic, in light of the grossly inadequate procedure that we have just described, to now recall that criticism, which reads as if it were written with the past two months experience in mind:

² Explanatory note, Climate Change Response (Moderated Emissions Trading) Amendment Bill, pp. 11–12.

...legislative process has been rushed and inadequate given this bill's complexity and significance. The public has not had adequate time to examine and submit on the bill, and it is evitable that serious mistakes will be made that will adversely affect New Zealanders.

Summary of process concerns

The process adopted in respect of this bill is the worst that any of us have experienced in our time in Parliament. Its hallmarks have included

- timeframes which have made it impossible to allow for sufficient public submissions, or considered official and independent advice
- withholding by the Government of essential information and analysis around the rationale for, and the fiscal cost of, the amendments
- amendments that in substance provide for the subsidisation of emitters that will mean increasing emissions at enormous fiscal cost, such that they cannot possibly be the subject of any enduring political consensus
- highly significant errors in the calculation of the fiscal outcome, discovered only on the final day of our deliberations, showing the effect of the bill if it proceeds is to increase Government debt by 13–17 percent of GDP by 2050.

Substantive criticisms

The Treasury, the Parliamentary Commissioner for the Environment, our independent expert adviser, and the vast majority of submitters are critical of the bill. We uphold their criticisms. The bill significantly dilutes the effectiveness of the ETS, and will have a significant negative impact on the New Zealand economy and environment for many years to come. The bill ought not to proceed.

Defective assumptions

Unclear policy and legislative objectives: The primary goal of climate change policy should be to achieve the reduction of greenhouse gas emissions needed to avoid global warming, in keeping with New Zealand doing its fair share, at lowest economic and social cost. It should maximise New Zealand's existing competitive advantages in clean technology and smart adaptation. There is no clear rationale from first principles evident in the bill, in the commentary, or in supporting advice, as to how the Government seeks to achieve all this. For example, allocation rules between sectors appear to lack economic (if not political) logic. There is no explicit reference to the relative contributions of emissions trading and complementary measures. It is just not clear how the Government considers its own policy proposals will achieve the goals that it has set for itself.

No property right to pollute: Business New Zealand told us that it believes that a property right to pollute has been created. This right was said to come into being by virtue of past usage. In other words, if a business has a history of polluting, it has a property right to continue to do so.

We reject this thinking out of hand, but cannot help thinking that it underlies the rationale for most of the changes contained in the present bill.

Invalidly assumed tradeoffs: The Government has argued that the bill represents a balancing of economic and environmental responsibilities. We reject this argument. The bill will make New Zealand poorer, not richer. The bill transfers emissions costs from polluters to taxpayers and reduces the incentives for emissions reductions. New Zealand taxpayers are expected to pick up the cost of the bill, with no corresponding improvement in environmental outcomes.

Inappropriate incentives: The Government has failed to consider the proper operation of economic incentives in New Zealand climate change policy. Dr Kerr demonstrates that some of the very high-emitting industries are simply not associated with large levels of employment, and so the costs of protecting each of the jobs in these industries is so high as to be unjustifiable on this basis. An example of this thinking is the assistance that would be provided to Rio Tinto under this bill. We heard that the changes to the allocation regime and phase-out of free units means the New Zealand taxpayer could be required to subsidise every worker at the Tiwai Point smelter to the value of between \$109,000 and \$225,000 per annum.³ The high costs of protecting New Zealand firms, as proposed in the bill, would also make New Zealand firms less competitive overall, thus undermining the rationale for the Government's changes to the ETS.

The bill is based on defective thinking and incorrect assumptions. The majority of submitters oppose the changes. New Zealand will not be richer as a result of this bill, nor witness improved environmental outcomes. Indeed, as the regulatory impact statement states, the changes “come at a cost to the economy as a whole, by delaying the transition of the New Zealand economy to a carbon constrained world”.⁴

Misallocation of free carbon credits

The regime for allocation and phase-out of free units contained in the bill represents a substantial and unjustified transfer of wealth from taxpayers to polluters. Submitters were almost unanimous in their view that the allocation regime set out in the bill is unduly generous to some sectors (particularly large industry and agriculture); that the two-for-one discount proposed during the first two years is inappropriate and unduly dampens adjustment incentives; that there are considerable risks in fixing the near-term carbon price at \$25 per tonne; that the phase-out rate for free allocations is too slow; that the 50 percent reduction target by 2050 is too modest; and that the combined result is environmentally irresponsible, economically inefficient, and socially inequitable.

As the Parliamentary Commissioner for the Environment told us, each credit that is given away rather than kept or sold is a real dollar loss to the taxpayer.⁵ Maintaining a high-level of protection is very costly to the taxpayer and to the economy as a whole. Free allocation

³ Oral submission from Kent Duston; Submission from the Parliamentary Commissioner for the Environment, p. 5, citing Climate Change Leadership Forum *Preliminary feedback from Climate Change Forum Leakage Case Studies*, Climate Change Leadership Forum Report Number 6, 2006.

⁴ Explanatory note, p. 36.

⁵ Submission from the Parliamentary Commissioner for the Environment, p. 5.

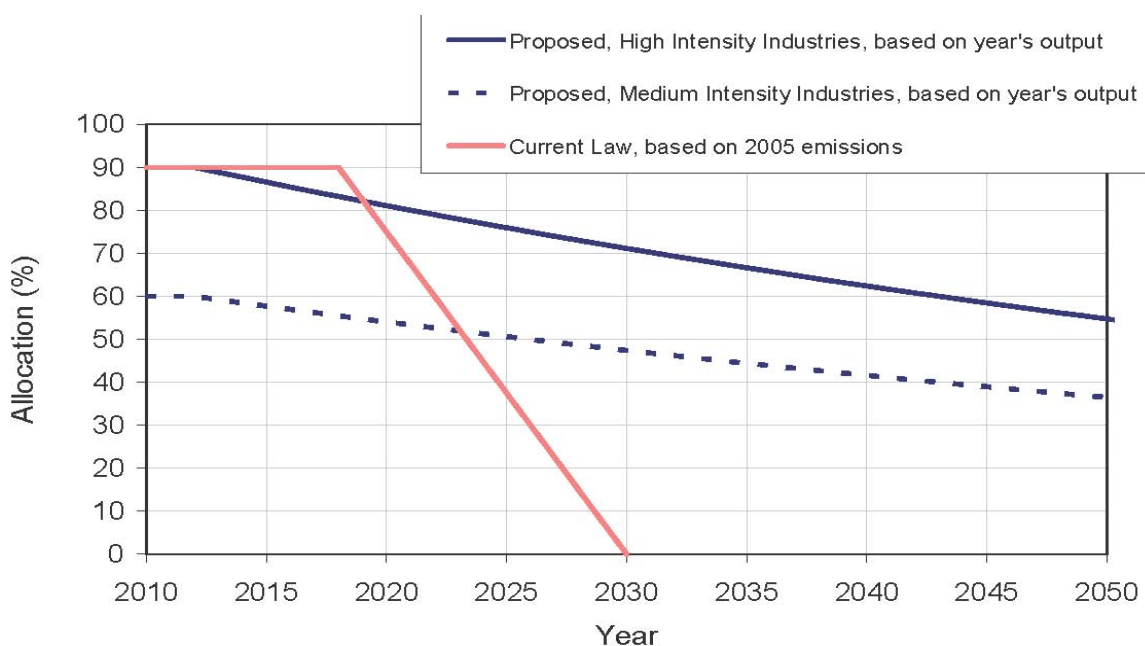
should be phased out faster. As Dr Kerr advises; “the benefits to the protected activities are vastly outweighed by the costs to the economy as a whole”.⁶

The phase-out rate for free carbon credits proposed in this bill is too slow. There is no specified date when allocation of free carbon credits will end. Under the existing scheme, free carbon credits were phased out by 2030. Under the bill, the allocation of free carbon credits could continue indefinitely. The Minister has claimed that free allocation will end eventually because it will be reviewed every five years. His colleague the Minister of Agriculture has indicated that the Government plans to provide free credits for 90 years.⁷ The latter view seems likely to be closer to the truth.

The 1.3 percent per annum phase-out rate for free carbon credits means taxpayers will still be funding over half of the emissions for high-intensive industry in 2050. According to the Parliamentary Commissioner for the Environment, the phase-out rates are incompatible with the Government’s policy of a 50 percent reduction in emissions compared to 1990 levels by 2050.

The effect of this absurdly slow phase-out of the free emission rights compared with the status quo is shown in the graph below from the Parliamentary Commissioner for the Environment. This in turn can be contrasted with the proposals in the USA shown in the second graph.

Figure 1

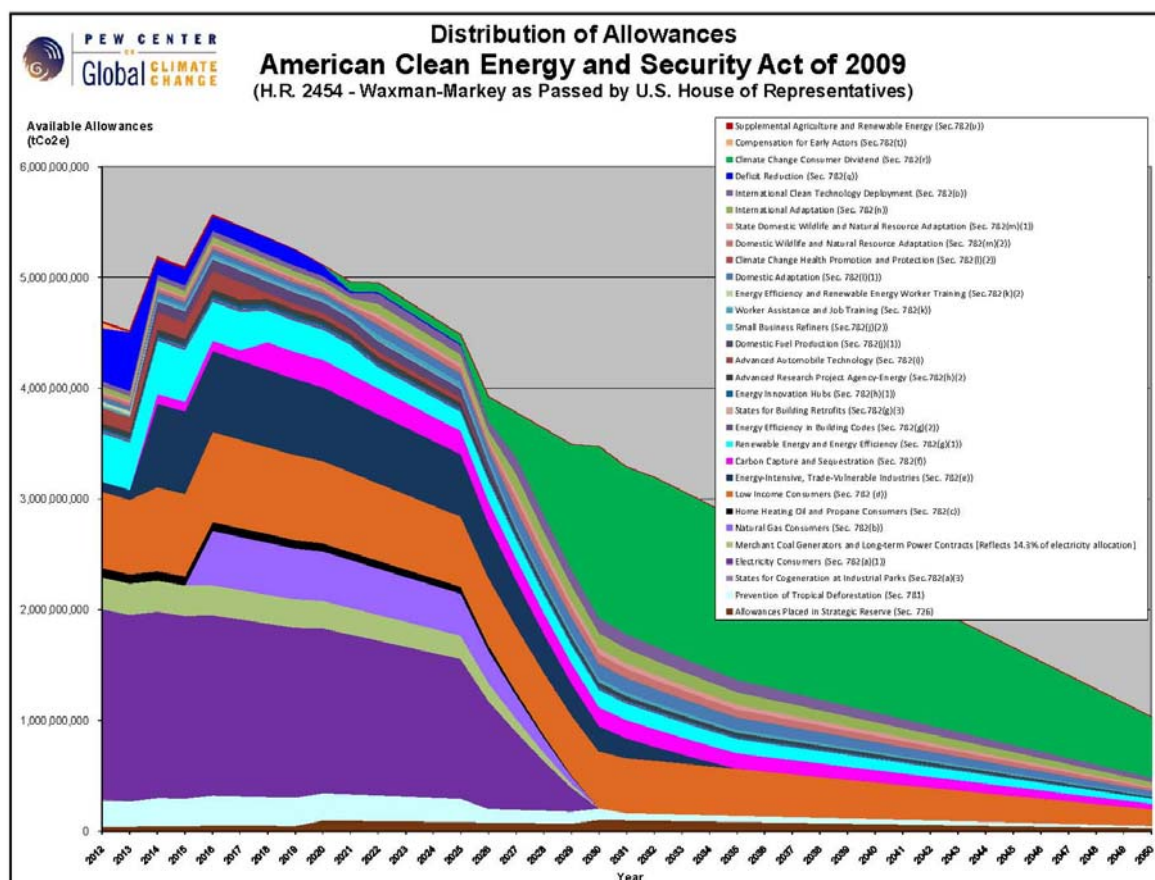


The phase-out of allocation in the proposed amendments is slower and more costly over the long-term than the current law.

⁶ Independent Specialist Adviser Dr Suzi Kerr, Response to Queries from Independent Specialist Adviser (Stage 1), 9 November 2009.

⁷ Hon David Carter, Taranaki Daily News, 18 September 2009.

Figure 2: USA proposed phase-out



Methanex is another example of where a substantial increase in taxpayer-funded free allocation occurs. The following extract from officials’ advice to the committee shows an additional allocation of at least \$15million per annum and possibly as much as \$81 million per annum:

The table below compares three possible allocations: allocation under their 2008 output (“existing”), the increased 2009 production anticipated in their submission (“2009 increase”) and the allocation if Methanex were to return to “full capacity”. Methanex stated in their submission that they would be able to return to full production if sufficient gas was available.

Hypothetical allocations to Methanex (Annual)			
	Existing	2009 increase	Full capacity
Production (000 tonnes 98% CH ₃ OH)	570	900	2410
FA Final allocation (000 NZU)	383	605	1619
Allocation cost @ \$25 (\$M NZD)	9.5	15.1	40.4
Allocation cost @ \$50 (\$M NZD)	19.1	30.2	80.9

We received no information or analysis from officials as to whether this was necessary to maintain the viability of Methanex, nor the effective subsidy per job per year. Methanex did acknowledge in their verbal submission that the company met with the then Climate

Change Minister, David Parker, before they reopened their New Zealand facility and were advised that the company would face the cost of increase in their emissions. It is a matter of fact that they proceeded to invest with that knowledge.

Uncapped intensity-based approach

We uphold the strong criticism that we heard of the approach manifest in the bill to combine an intensity-based allocation with no effective cap on total (or sectoral) emissions and a very slow phase-out of free allocations. The Parliamentary Commissioner for the Environment told us that this will likely lead to a significant increase in emissions, thus increasing the number of carbon credits the Government, and therefore taxpayers, will have to purchase. Moreover Dr Kerr advises of the possibility that banking and trading free allocated credits, taken with price caps, could result in a positive incentive to increase emissions, or windfall gains to polluters.

We recognise that there are some arguments both in favour of and against intensity-based allocation. Arguably it can provide an incentive for firms within an industry sector to approach international good practice in terms of emission efficiency, and in so doing act to prevent the transfer offshore of industries (“leakage”) to less regulated and more polluting locations.

However, even if intensity-based allocation can be argued for in some sectors, the overly generous levels of free allocation and very slow levels of abatement cannot be justified. Moreover, intensity-based allocation with sector-based caps can risk arbitrary competitive shifts, especially in industry sectors with a small number of players. Dr Kerr advises that there are more economically efficient means of preventing leakage, such as import taxes on substitutes.

An alternative favoured by many submitters is an overall cap on emissions. The lack of a cap on the allocation of free carbon credits would significantly increase both the fiscal risk for the Government and policy uncertainty for business. We heard that a global cap is vital for the creation of the right incentives to reduce emissions. We concur that the absence of some form of cap weakens the incentive for emitters to move to being less carbon-intensive. No coherent analysis was provided by officials of the cost-benefit analysis of various types of caps (global v sectoral, “hard” v “soft”), and this contributed to the lack of proper and transparent options testing, sensitivity testing, and regulatory impact analysis in advice provided to us. The Government appears to have chosen a highly distortive, environmentally unreliable, and economically inefficient mechanism to control emissions, for which there is no apparent rationale nor supporting evidence.

Fiscal costs and risks

The bill will load enormous costs onto future generations of taxpayers. The insistence by the Minister that the fiscal costs of the provisions of the bill reduce the cost of the NZ ETS until 2018 is misleading and irresponsible.

We were advised that when Government borrowing costs are included, the total additional cost to taxpayers of the higher allocation to major emitters to 2050 is \$100 billion. As noted earlier, on the final day of our deliberations the Treasury advised us that the effect of

the bill is to increase Government debt by 13–17 percent of GDP by 2050, rather than by the 6–8 percent which had been their previous estimate to Cabinet.

A table contained in the regulatory impact statement indicates that by 2030 the proposed changes would cost taxpayers between \$1.99 and \$2.17 billion per annum, and from 2030 a cost of approximately \$411–586 million per annum.

According to evidence presented by Dr Christina Hood, as well as preliminary advice from the Sustainability Council, the fiscal costs and risks are very significant. Dr Hood estimates that the compound fiscal subsidy to emitters could total up to \$130 billion by 2050. Dr Kerr advised that these estimates were a valuable contribution to the debate. It was not possible for us to develop our own financial models based on the data provided by officials in the time available for consideration of the bill. We consider it a gross breach of parliamentary practice on a bill of this importance that we did not have sufficient time or resources to test fully the underlying and conflicting estimates of officials and submitters.

The more fundamental question is of course whether it is economically prudent or sustainable to spend such significant amounts of scarce public money on free emissions rights to polluters, relative to the value of other energy efficiency, mitigation, or economic investments. For example, how many houses could be insulated, how many clean cars could be incentivised, how many clean jobs could be created, how rapidly could New Zealand be selling new clean technology overseas, how many trees could be planted, how many farms could be cleaned up, and how much cleaner and richer could we be, if even some of these funds were directed into complementary measures? Alternatively, how much better off could we be if some of these funds were directed into other spending, or into tax reduction or repayment of Government debt?

Agriculture

There should be no change to the current entry date into the ETS for the agriculture sector of 1 January 2012. The agriculture sector contributes nearly 50 percent of all New Zealand emissions. However, under this bill the agriculture sector is required to be responsible for only 4 percent of the total costs of meeting our international obligations. We can see no policy justification for delaying the entry of agriculture given that New Zealand already accounts for, and is liable for the costs of, increases in those emissions under the Kyoto Protocol. We believe that sound economic theory requires that those real costs to the New Zealand economy be passed on to the sector so that they may factor them into business decisions.

Concerns about leakage of agricultural production are unfounded. Dr Kerr advises that there “is likely to be very little production leakage from the agricultural sector”.⁸ This calls into question whether an intensity-based allocation is appropriate for the agriculture sector. Opponents of the NZ ETS within the sector often point out the lack of mitigation options available to the sector as a justification for greater assistance. However, the committee received advice from a number of submitters that there was the potential for easily accessible emissions mitigation within the sector.

⁸ Independent Specialist Adviser Dr Suzi Kerr, Response to Queries from Independent Specialist Adviser (Stage 1), 9 November 2009.

Dr Kerr informed us that there are opportunities for emissions reductions in the sector that are not being encouraged. She advises that it would be administratively straightforward to establish a system to reduce nitrous oxide emissions. Some of the revenue collected through this process could be used to fund the use of nitrification inhibitors. The increased deployment of nitrification inhibitors could provide a significant reduction in agricultural emissions. The Sustainability Council told the committee that they could, along with several other measures, enable emissions reductions close to 5 million tonnes a year, all at a profit to the farmer.

It is important for the agricultural sector to be responsible for its emissions through its inclusion in the NZ ETS at the earliest possible stage. The sector is the single largest contributor to New Zealand's total emissions. But it is responsible for only a small proportion of the costs of its emissions. Delaying its entry will only delay the introduction of economic incentives for the sector move towards reducing emissions. Without a significant reduction in emissions from the largest contributor to New Zealand's emission profile, the taxpayer will be required to cover the costs of those emissions. The bill's provisions that delay agriculture's entry into the NZ ETS and provide a greater level of free carbon credits are unjustified and unfairly burden New Zealand taxpayers.

Transparency

Most submitters recognise the need for some allocation of free carbon credits to provide assistance to firms that may face competitiveness risks. However, many submitters were concerned that protection was misallocated or too generous. To ensure an equitable allocation across the economy, the process for the allocation of free carbon units needs to be transparent and open. The motivations behind the allocation of free credits to a particular sector should be publicly available. There is an enormous level of taxpayer expense involved in the provision of free carbon credits. Taxpayers should be provided with a justification for providing free credits to a particular sector. The detail of emissions trading is not readily understood by the public. Increasing the level of transparency and openness around the support provided to emitters should increase public trust and confidence in the scheme.

We agree with the recommendation from the Parliamentary Commissioner for the Environment that the Controller and Auditor-General be required to publish annually all allocations of free carbon credits. This idea was widely supported by submitters. Ensuring that public allocation information is available each year will ensure that allocation is based on an equitable approach and help build trust in the system.

The process of free allocation also needs to be supported by additional complementary measures. The public needs to know that the Government is working on the promotion of investment in low-carbon technologies, investing for a low-carbon economy, and providing support for workers in firms that are affected by measures to reduce emissions. As the New Zealand Council of Trade Unions described it, the movement towards a low carbon economy needs to be a "just transition". The Government needs to be proactive rather than just protective of existing interests.

We also believe there is a need for independent advice on climate change policy. We have already explained that the process for amending the NZ ETS has been completely

unsatisfactory, given the lack of sound analysis and official advice. A climate change committee should be established as an independent crown entity. The role of the committee would be to provide independent advice to Ministers and to promote informed public debate on the public policy response to climate change. There also need to be independent and settled carbon accounting standards. The confusion in the past over the extent of New Zealand's carbon liabilities needs to be put to an end.

Harmonisation with Australia not in New Zealand's economic interests

We question the Government's unreasoned focus on harmonisation with the Australian Carbon Pollution Reduction Scheme (CPRS), which has not yet been passed by the Commonwealth Parliament, and whose final shape therefore remains unclear.

As we observed earlier, the RIA Unit at the Treasury has identified a number of risks with the approach to harmonisation with Australia. There appears to have been no consideration of New Zealand's unique emissions profile and industrial structures, and a *carte blanche* acceptance by the Government of relevant aspects of the proposed CPRS. The RIA makes it clear that there is no clear analytical basis for the proposal to align some of the design elements of the ETS with the proposed CPRS, and that the Government has not considered the risks of harmonising with a scheme that has not been approved and may be subject to extensive revision.

The differences between New Zealand and Australia are highlighted by the exclusion of agriculture from the CPRS. Currently, the agriculture sector is not included in the CPRS and the Australian Government has indicated it will review in 2013 whether agriculture will be included in the CPRS in 2015. Nearly 50 percent of New Zealand's emissions come from the agriculture sector, in contrast to approximately 15 percent in Australia. Australia has considerably higher emissions from the energy sector because of its reliance on coal-fired power stations, while New Zealand generates approximately 70 percent of our electricity from renewable sources. Harmonisation with Australia needs to be thoroughly considered. We have simply not had sufficient time or advice to allow us to properly consider the benefits or costs of the level of alignment envisaged by the bill.

The Parliamentary Commissioner for the Environment told us that harmonisation with Australia also runs the risk of limiting New Zealand's ability to align with schemes in other countries. The Institute of Policy Studies and the New Zealand Climate Change Research Institute, Victoria University of Wellington, also notes that intensity-based allocation would be incompatible with the US and EU policy regimes. The adoption of an intensity-based approach without a cap, as contained in the CPRS, might prevent New Zealand credits being sold in the United States. The Kerry-Boxer Bill contains the provisions that credits from countries "not subject to [...] mandatory absolute tonnage limits" do not qualify under the scheme.⁹

Harmonisation should occur only where it is demonstrably in New Zealand's interests. Climate change policy in other countries is continually undergoing refinement as international circumstances change. Ill-considered and hasty harmonisation with Australia

⁹ Submission from the Parliamentary Commissioner for the Environment.

runs the risk of imbedding inflexible provisions in New Zealand's climate change legislation. This is most unwise

Forestry issues

We agree with the bill's proposed amendments relating to wilding pines, but have been unable to assist in progressing those amendments because of the procedural issues that we have detailed elsewhere.

Treaty issues

This is a very important point of principle. As officials advised us:

The fundamental underlying question facing the Government with regard to the impact of the emissions trading scheme on the Ngāi Tahu Claims Settlement Act 1998 is whether the Crown considers that it has an obligation to protect the value of commercial assets distributed as part of the Treaty settlement process and, if so, to what degree and for how long after the settlement has passed. The Government's treatment of this settlement in relation to the emissions trading scheme is likely to create an implicit precedent for the treatment of other settlement in similar situations in the future.

This is an important and difficult question. On the one hand, it can be argued that it will never be practical for any government to attempt to shield the private assets held by particular groups from the effect of all future policy changes, regardless of whether or not those assets were originally transferred under a Treaty settlement. On the other hand, Māori groups have argued that it would undermine the intent of Treaty settlements if the Government took actions that significantly reduced the value of the assets transferred before Māori had had an opportunity to grow and develop them. They therefore argue that it is reasonable to provide preferential treatment to settlement assets for a number of years after settlement.

Officials have sympathy with the argument that the Crown has an obligation to avoid taking steps that lead to a significant reduction in the value of Treaty assets in the years immediately after settlement. However, it is not clear that, given a time delay of approximately 10 years since settlement and the particular circumstances around this situation, further assistance is warranted.

Cancellation of Household Fund

We believe complementary measures to reduce greenhouse gas emissions have a crucial role to play. We do not support the removal of the Household Fund from the legislation. The fund was a legislative requirement for \$1 billion to be allocated by Parliament by 2024. The fund was to promote reductions in non-transport household greenhouse gas emissions through the promotion of household energy efficiency and conservation and household renewable energy technologies. The rationale behind the fund was to assist households in adjusting to increased energy costs from the inclusion of the electricity sector in the NZ ETS, in part by increasing the energy efficiency of their homes. We are concerned about the provision of assistance to households after the end of the transitional phase proposed in this bill.

The transitional phase to be established by this bill would reduce the increase in electricity prices under the NZ ETS, but the Government has made no announcements about assistance after this period. The Household Fund would have continued to provide assistance for household energy efficiency improvements. Improving household energy efficiency will become an increasingly important part of reducing emissions and minimising household costs once electricity enters the NZ ETS. Once again, it appears the Government's primary interest is providing support to emitters while ignoring the effects of the ETS on New Zealand households.

An alternative approach

The tragedy is that parliament could instead be debating a politically and fiscally sustainable scheme. It is a matter of public record that early this year, Labour offered to talk to National on what amendments might be needed to reach enduring certainty over climate change policy. When National collapsed those negotiations in favour of advancing the amendments contained in the bill, three main issues were outstanding:

Date of entry for sectors: The Government proposed delaying the entry of stationary energy until June 2010, bringing forward the entry of transport fuels to June 2010, and delaying the entry of agricultural emissions from 2012 until 2015. We said we could not see the policy justification for delaying the entry of agriculture, given that New Zealand already accounts for, and is liable for the costs of, increases in those emissions under the Kyoto Protocol. As we have noted, we believe that sound economic theory requires that those real costs to the New Zealand economy be passed on to the agriculture sector so that it factors them into business decisions.

Nevertheless, we indicated that if agreement could be reached on the other two issues we might be able to compromise on the proposed dates of entry, given the political aim of the Government to ease entry for the agriculture industry. We indicated that we thought that the entry dates for stationary energy and transport could be harmonised, with the date for agriculture being delayed by up to one year. Indeed, we note that the Minister took such a "meet in the middle" proposal to Cabinet, and was rebuffed.

Price cap: We think price caps are undesirable, because they distort the response to the ETS. The Kyoto-compliant market is already large. Participants in the ETS (mainly companies worth billions of dollars) can already hedge their risk against substantial rises in the cost of carbon until at least 2012 by buying units on that market.

The transitional measure requiring only one emissions unit to be remitted for every two tonnes of emissions in the electricity sector would not necessarily reduce the impact on electricity prices. The European experience demonstrates that the long-run marginal cost of new generation does not change, so electricity generators will charge consumers the same amount and effectively pocket the value of the emission units they do not have to remit (at costs to the taxpayer).

In principle, if the market is not trusted, then the Government should have pursued a carbon tax rather than an ETS. A cap at less than the market price results in a further subsidy from the taxpayer to emitters, and reduces the incentive the ETS is meant to create to reduce emissions.

Free allocation to trade expose industry: We have always agreed that transitional assistance by way of free allocation of emission rights is needed for the industries that produce high emissions, relative to their output, while they are exposed to competition from overseas markets that are not facing a cost for their emissions.

We prefer the current allocation methodology based on historic emissions (that is 90 percent of 2005 emissions) because this preserves the clearest price signal for the next transaction by the emitter. The emitter faces the full cost of increases in emissions and gains the full benefit of decreases in emissions. The Treasury advised the previous Government that preserving the clear marginal cost was the best policy and would lead the New Zealand economy to reduce its emissions at the lowest cost to our economy. We still believe is to be true.

In an effort to find an enduring compromise for the good of New Zealand, we indicated we would consider free allocation based on intensity rather than historic emissions if it were within a cap on the total quantity of free emission units granted. We said that we would need to see the detail of the amounts of the intensity-based allocations proposed and a comparison with allocations under the existing ETS, but indicated that we were likely to agree to this if it were within a cap for the sector. We remain of that view, with the added proviso that the phase-out of free allocation would have to be at a rate considerably higher than the 1.3 percent per annum proposed in the bill.

The Minister indicated that the issue of the cap would be unlikely to be difficult in practice in stationary energy and industrial processes (because he thought the allocations on an intensity basis to industry would total less than the cap of 90 percent of 2005 emissions), but that he saw greater difficulty for agriculture in this approach.

We know that the agriculture industry claims they are already at world's best practice, and that intensity-based allocation without a cap is likely to see their emissions grow at a cost to taxpayers. Intensity-based allocation within a cap will not see New Zealand agriculture fail or move overseas. The land, stock, and existing productive assets, which are the means of production, will not move. But on an intensity basis within a cap, expansion in agriculture at the margin above 90 percent of 2005 emissions would reflect the real cost to the economy of emissions. This would encourage lower-emission practices where they were economic, and would not distort the forestry industry. It would do what an ETS is meant to do.

Intensity-based free allocation without a cap in agriculture will make New Zealand less prosperous rather than more, and will significantly reduce the environmental effectiveness of the ETS.

Summary

To achieve an enduring settled ETS for New Zealand, we were likely to have agreed

- to the dates proposed for inclusion of stationary energy and transport, with a compromise entry date for agriculture in the middle
- to accept the proposed transitional price cap and transitional two-for-one allocation rule

- to support intensity-based allocation within a cap, subject to reasonable phase-out rules.

All were less than ideal compromises, but as it was clearly desirable to have an ETS that was agreed by the major parties, we were willing to make some compromises in order to achieve that aim. We negotiated with the Government in good faith and could see no reason for the Government not to act in similar good faith, since it appeared to us that the only substantial issue that National would need to compromise on was the issue of the cap on free allocation in agriculture. If they had done so, an enduring and effective ETS could have been achieved.

Instead we have an ETS backed by the Māori Party and Peter Dunne, which does the opposite of what it should do. It is softer rather than tougher on emitters. They have served up an ETS which does not properly encourage the mix of our productive economy to change towards lower-emission goods. Overall, the NZ ETS is now to be designed as a license to increase emissions, especially in agriculture, rather than an incentive to reduce them. New Zealand will be poorer financially and our emissions will be higher as a consequence.

If Parliament passes the bill in anything like its current form, a priority for Labour will be its repeal and replacement with legislation providing for a robust ETS and a fit-for-purpose series of complementary measures.

Green Party minority view

The Green Party regrets that we have had to write such a substantial minority report. This is because many key issues in the legislation were never fully discussed by the committee.

Global climate change is the most important environmental challenge of our time. The Green Party has been calling for a price on carbon since 1993. Our preference for many years was a carbon tax because of its simplicity; the certainty it gives business on what the price will be, thus enabling investments in emissions reductions to proceed with confidence; and the opportunity for Governments to use the proceeds to reduce other taxes. We do not believe the case for an ETS instead is overwhelming, but agree that is the direction the world is going and there are some benefits in aligning with international efforts. We have therefore put our efforts since 2007 into ensuring New Zealand has the best ETS it can have.

The Hon Dr Nick Smith wrote in the National Party's minority report on last year's ETS legislation:

The importance of getting this legislation right cannot be overstated. [The development of an ETS] represents the most significant economic reform since the deregulation of the economy in the late 1980s. Getting this bill right is also important for the environment. Poor policy can also have unintended adverse environmental consequences.

Process concerns

The Hon Dr Nick Smith complained bitterly during the select committee stages of the existing ETS legislation, stating:

the legislative process has been rushed and inadequate given this bill's complexity and significance. The public has not had adequate time to examine and submit on the bill, and it is inevitable that serious mistakes will be made that will adversely affect New Zealanders.

Unfortunately, the process around this bill has been worse in every respect.

The most damning indictment of the process is The Treasury's public rejection of the legislation, which stated:

the level and quality of analysis presented is not commensurate with the significance of the proposals, which represent major design changes to the Emissions Trading Scheme, and that the Regulatory Impact Statement does not provide an adequate basis for informed decision-making.

It is ironic that after such a scathing indictment of this legislation by The Treasury, they discovered errors in their own calculations indicating that the debt-to-GDP budget blowout that this bill creates will be twice the amount they originally thought, a \$50-billion-dollar discrepancy.

An independent submitter, who was only given 10 minutes to speak, had provided the committee with more accurate cost projections than officials. The select committee only discovered this at the eleventh hour.

This is further evidence that officials are being put under intense pressure by the flawed process and are prone to serious mistakes posing enormous risks to the welfare of the nation.

With regard to the current bill, the Greens reiterate Dr Smith's earlier warning:

this process has not been conducive to getting such an important bill right nor in getting the cross-party support needed to ensure the stability and longevity of New Zealand's ETS.

This select committee report is meant to report on a select committee process. However, the rushed and deeply flawed process has meant there is little to report. The Parliamentary Counsel Office would not have been able to produce an amended bill in the time allotted even if we had wanted one.

Having failed at the select committee stage, it is clear that the Government is intending to introduce during the committee of the whole House stage a number of significant amendments, which the select committee has not seen or discussed. This is a deeply flawed, undemocratic way of developing such important legislation and will result in serious errors.

It would be better for the current framework of the NZ ETS to remain intact and for the Government to return its focus to delivering the necessary regulatory framework and not risk further exacerbating the uncertainty for business and the taxpayer.

Design of an ETS

Given that the mechanism of choice is a market trading in emissions units, it is important to allow the market to work. Interference with price or liquidity should be avoided.

This bill interferes with both price and liquidity. It would do nothing to reduce emissions, and instead promotes speculative trading only. We agree that trade-exposed firms need some protection while their competitors face no price on carbon. However, basing this protection on output creates an incentive to increase their pollution because it dilutes the price effect at the margin of their activities. A free allocation of units based on a proportion of historical emissions would greatly reduce the cost of an ETS to those firms, without reducing the incentive to reduce emissions.

The Greens strongly oppose an uncapped intensity-based allocation, which commits New Zealand to constantly rising emissions and rewards those responsible for them. It is fiscally and environmentally reckless.

Similarly we oppose a price cap. The whole purpose of an ETS is to bring the international price of carbon into decision-making by firms and individuals. A price cap denies those reducing emissions the full value of their actions and will reduce the incentives for all mitigation actions. It will have the perverse effect of rewarding those who are causing the climate change problem and punishing those who are part of the solution. It will also delay the economic transformation we so desperately need to a low-carbon economy.

Rather than cap the price, it would be better to return to a carbon tax. Jumping abruptly from \$12.50 to the international price of carbon in 2013 invites lobbying for the extension of subsidies and a further “transition period”.

The Greens welcome the earlier start to the phase-out of free allocations, but at the 1.3 percent per annum rate phase-out lasts for decades and is far too long. The 2030 cut-off of allocations in the existing legislation is reasonable because most of New Zealand’s existing emission-intensive plant will have reached retirement.

The Treasury has modelled the cost of the never-ending subsidies. It estimates that, if a 1.3 percent phase out rate is maintained into the long term, the proposed policy settings for intensity-based allocation indicate a cumulative increase in Government debt of around 13–17 percent of GDP by 2050, at a cost of about \$110 billion.

Fairness in an ETS takes several forms. One has been addressed above—firms exposed to unfair trade competition from countries with no price on carbon need some protection during a transition period. However, this protection comes at the expense of taxpayers, and particularly households and small businesses, which have to pay both for their own emissions and for those of large firms. The transition subsidies should end with the life of existing plant, and should not be used to subsidise new emission-intensive plant. The uncapped transfer of risk from emitters to taxpayers is unfair and reminiscent of the Muldoon era.

We agree with the recommendations of the Parliamentary Commissioner for the Environment that there should be transparency in the massive wealth transfers that this ETS creates, and that the unit registry be required to make public the number of units

allocated for the previous year to each activity, industry, or sector. The Controller and Auditor General should report annually on allocation. It is sobering to think that donations to political parties are far from transparent and allocations of taxpayer funds to polluters in the form of free allocation will be even less transparent. This creates a perception of undue influence and a real risk of undue influence.

There is also a need to ensure fairness between sectors. Late entry for agriculture and high levels of grandfathering will impact badly on forestry. The exemption from a carbon price for farmers will tend to be capitalised in land prices, raising the value of marginal land so that it becomes unaffordable for forestry.

The Greens welcome the small steps proposed on wilding pines. However, the proposals to address the wilding pine problem are haphazard and poorly thought out. They treat some of the symptoms without addressing the underlying causes.

The Greens have long been concerned that the incentive to plant pine trees may be at the expense of natural ecosystems such as tussock land in the high country or regenerating native forest. A National Policy Statement on Biodiversity was agreed and gazetted as part of the negotiations for the existing ETS to manage the problem through district plans. However, the Minister has indicated that the Government will not be following through on this important issue. We also believe that the carbon-storage look-up tables need to be revised to account for the greater carbon stored by native forests.

Alignment with Australia's developing ETS

Linking with emissions trading schemes in other countries with which we trade, and as soon as possible with an international market, is desirable, but only where our principles are not compromised. Closely linking with the proposed Australian scheme (if it is passed) requires us to distort our market by capping the price and allocating on an intensity basis, while eliminating our ability to link with our three next largest trading partners. Linking with the EU would be less distortionary and would have the benefit of a more established and experienced market. However, we should not attempt to link with any country until there are common rules that meet the principles above.

New Zealand has an adequate ETS in law now. It covers all sectors and all gases (though more slowly than we would have liked); it preserves the full price signal at the margin even for firms that are 90 percent grandfathered; it allows mitigators to sell units at the full international price; it excludes Assigned Amount Units (AAUs) from other countries unless specific regulations allow them because their environmental integrity has been established. In our view the large wealth transfers from households and small businesses are too great, which compromises fairness; but there is a compensatory provision for households in the form of a large fund for home insulation.

We do not see any reason to change these fundamentals. The proposed changes would destroy the price signal at the margin, limit the price mitigators could get for their reductions, and uncap the large wealth transfers from households and small businesses to big emitters.

The proposed legislation is fiscally, environmentally, and morally reckless.

Māori Party minority view

Climate change is an almost unfathomable global reality. Climate change demands the highest level of concentrated commitment to collective responsibility locally, nationally, and internationally, to both carbon emissions abatement and the pursuit of environmentally sustainable human interaction with the environment.

New Zealand's emissions trading scheme, whatever its form, is inevitably only a discrete contribution toward global efforts in carbon emissions reduction and, confined by its objective of promoting carbon emissions abatement, it is an incomplete response to climate change. The Māori Party considers that the challenges of, and answers to, climate change will only be met by collective responsibility—each business, community, and nation assuming responsibility for their interactions with the environment.

The Māori Party is acutely conscious of the limitations of an emissions trading scheme, and remains concerned that market mechanisms may not be capable of promoting collective responsibility and delivering the behavioural change that is needed to ensure environmentally sustainable practice is adopted by business. Balancing the distribution of responsibilities under the scheme has also been challenging, particularly with the intensity and transitional provisions included in this bill having uncertain fiscal impacts. The importance of any scheme appropriately providing for collective responsibility, and our respective contributions to it, cannot be understated; the resources of Papatūānuku are finite, and if our national responses are not carefully enough designed, we impoverish the inheritance of future generations.

Accordingly, the Māori Party preferred a fixed price on carbon through a carbon tax, because it would provide for greater control over activity and has, in our assessment, a more incisive ability to ensure that polluters pay directly for their activities, as well as delivering greater transparency. However, the current context is that we have an emissions trading scheme in place, and through its development, enactment, review and now amendment, we have allowed a number of years to be directed more to designing a legislative scheme, rather than on acting on climate change. We can foresee that without a clear decision being taken now, the policy debate would continue to be the dominating issue of the day, and we would all witness further years of the push-me-pull-you approach to reconciling sectoral obligations, with advocates seeking to reduce their liabilities and transfer greater costs elsewhere, that has become all too familiar over recent years. For the Māori Party, the worst-case scenario is for nothing to happen. We need to move to the next stage of comprehensive responses to climate change that are innovative, principled and, above all, collectively driven.

For the amended scheme to be acceptable to the Māori Party, four objectives must be met, both through the scheme and the wider climate change policy framework:

- Whānau—ensuring that vulnerable communities do not bear an unfair burden under the scheme.
- Whenua—delivering increased environmental sustainability across a number of policy areas.

- Te Tiriti o Waitangi/Treaty of Waitangi—Te Tiriti/Treaty must be provided for in the scheme so that it is fair for our people, no matter what future changes get made along the way and so that Treaty Settlements are respected.
- Māori Economy—Our people are heavily involved in fishing, farming and forestry, all of which are affected by the scheme. It is important that our people’s businesses are not the hardest hit by the scheme, so that the outcomes are fair and our economy can grow.

The current scheme does not deliver on these objectives, nor does the bill as reported back from this committee. As noted in the committee’s report, the Māori Party is continuing to negotiate with the Government on a range of amendments and further commitments to meet these objectives.

Important to the Māori Party is a comprehensive clause that provides for recognition of Te Tiriti o Waitangi/Treaty of Waitangi in and relating to the scheme both now and into the future. This clause must provide more than simple procedural participation, and deliver substantive outcomes that accommodate the full breadth of Treaty rights and interests. An historical pattern that cannot be replicated under this scheme is the imposition of arbitrary constraints on Iwi and Māori assets and resources. The Māori Party considers it imperative that Iwi and Māori are able to express their rangatiratanga and retain flexibility over land and resource use over future generations.

Also noted in the committee’s report is the concern of Iwi forest owners over deforestation liabilities. This is another area of negotiation between the Māori Party and Government, along with amendments to facilitate large-scale afforestation. Incentivising planting, particularly indigenous species, is an important part of meeting our international obligations, as this bill does not create a framework that in and of itself sufficiently reduces our carbon emissions—creating a potentially substantial future liability on the State (and hence taxpayers). Afforestation is in our opinion imperative for the national good.

The other key strand of the Māori Party’s negotiations with the Government is a comprehensive climate change policy and sustainability framework. This policy framework must provide effective and equitable outcomes for our people and whenua, including targeted packages for householders, valuing biodiversity, promoting clean-tech innovation, and recognising that mātauranga Māori has significant contributions to make to a comprehensive and principled response to climate change.

The Māori Party is committed to moving beyond deliberating over high legalism within a scheme that is inherently limited, toward an integrated package of responses to climate change that, in combination, promote and support collective responsibility for climate change. We each have an important part to play in intergenerational environmental sustainability.

ACT New Zealand minority view

General

- ACT believes scientific evidence pointing to dangerous human-induced warming is still uncertain, as is the prospect of decisive international action.

- Against the background of international recession, the Government's intentions on climate change have moderated.
- New Zealand should be a follower not a leader on policy action. The costs to both New Zealand consumers and businesses are too great to do otherwise, particularly when we know that our contribution will have no discernable impact on the climate whatsoever.
- Because Labour's existing ETS is currently on the statute books, with some sectors due to come into operation in less than two months on 1 January 2010, there is an urgent need to pass legislation to delay this commencement date. While ACT does not support this bill, ACT is prepared to support National in any legislation to delay the commencement of the existing provisions, to give the Government time to make a considered study of what changes are necessary for the long term.
- Both the existing ETS and that proposed by the modifications in this bill, would have a significant impact on the standard of living of all New Zealanders.
- ACT does not believe that most New Zealanders fully understand the costs and impositions being put on the New Zealand economy by both the existing ETS, and as proposed to be modified. A recently published survey by the New Zealand Council for Sustainable Business Development highlighted this very point.
- Because of the huge number of variables (for example what if any commitments we make after 2012; the price of carbon; the commitments of our trade competitors; and those of the developing world), any sort of modelling is largely a theoretical and academic exercise. More certainty could be provided by waiting until after the Copenhagen negotiations are concluded as a bare minimum, and better still until after Australia and the US finalise their commitments.

Copenhagen

There is no need for amended legislation to take to Copenhagen:

- an Act is already in place.
- US government officials have stated the US will not have one.
- Australia is in doubt.
- Post-2012 agreement will hinge on whether the US and China come to an agreement in due course—New Zealand's position will not be of any consequence.

Process

Has been far too rushed and repeats mistakes of earlier years:

- There is still no Regulatory Impact Statement (RIS): submitters called for one as a basis for sound, ongoing policy. The Treasury has certified that the RIS in the bill is inadequate. The Government has asked (in Government Statement on Regulation) to be held to account for poor practice—Parliament should do so.

- For example, the committee was submitted to the bizarre spectacle of having to adjourn its last meeting on Wednesday 11 November for half an hour while The Treasury officials withdrew to clarify if they had made a \$50-billion error or not. This is not a reflection on the officials but on the speedy and reckless process that National adopted to push the bill through the committee. Parliament has a job of holding the Government and the Executive to account and our ability to do so has been severely constrained by the tight timeframes given to the committee.
- The short notice (in one case less than four hours, and in most less than 24 hours, resulting in some who had requested the chance of making an oral submission being denied the chance to do so) and time given to submitters were unsatisfactory.
- The major issues for firms involved, bad for foreign investor perceptions, constitutionality questions (adjustments of allocations by regulation)
- The National Party members were not prepared to allow oral submissions to be heard over more than two days and it was only when all other members of the committee voted to hear all those who wanted to be heard oral submissions were extended.
- The committee has not had time to deal with important issues raised, for example by Fonterra.
- Making amendments by Supplementary Order Paper is a bad process: no opportunity for affected parties to comment.
- Exposed sectors not indicating that benefits in the terms of reduced “food miles” etc risks would exceed the costs imposed on them alone, let alone on the community as a whole.

Major substantive issues

- Initial impact excessive: at \$12.50 per tonne, same burden as Australia (A\$10 per tonne) yet New Zealand is 30% poorer and costs of mitigation are higher; Australian scheme starts 1 July 2011, a full 12 months after New Zealand (the concessionary rate of A\$10 per tonne extends to 1 July 2012).
- Protection being removed faster than Australia (and Australian scheme may be made even less onerous if the Government accepts some Liberal Party amendments). Relief for high-intensity emitters set at 94.5 percent (New Zealand 90 percent) and for medium emitters 66 percent (New Zealand 60 percent).
- Relationship between NZ ETS parameters and conditional 2020 commitments (10–20 percent below 1990 levels) unclear—economic costs to New Zealand could be far greater than currently suggested.
- No certainty about international trading market post-2012: NZ ETS cannot be domestic-only; post-2012 agreement (if or when it happens) may be independent, loosely coordinated commitments by Governments; and idea that New Zealand will have to pay for shortfalls may be invalid (for example Canada who has said it will not be paying anything for the first commitment period, immediately raising the issue of why New Zealand, or indeed any other signatory, should).

- Property rights in forests being expropriated: of greater economic importance to Iwi than likely economic gains from foreshore and seabed claims; and New Zealand's prosperity is based on highest and best use of land, and owners of central North Island forests (both Māori and non-Māori) are being denied the opportunity to convert their land to the highest and best use by conversion to alternative pastoral uses. Offset provided for in existing ETS, but only if this can be negotiated in a post-Kyoto treaty. Why should foresters pay for poor negotiating skills?
- Property rights in fishing being expropriated—at \$25 per tonne from 1 January 2013 on all emissions, the cost to industry will be \$15 million, or approximately 25 percent of fishing's gross margin, despite New Zealand getting a full credit for the 1990 level of fishing emissions.
- Concerns raised by mining (Solid Energy) and CFC industries (Temperzone) previously have not been addressed.
- New Zealand scheme for industrial allocations based on draft Australian legislation which may or may not be passed, and may or may not be appropriate for New Zealand, further illustrating the recklessness of rushing through legislation.
- Institutional arrangements: not satisfied that independent, arm's-length, robust arrangements are in place (in EPA) to administer a scheme starting in six months time.
- Proposed United Nations treaty has not been presented to select committee or public. Transfers to developing countries could be very costly—e.g. in relation to aid programme.
- Economy is in a weak state, which also justifies delayed action, and measures ultimately taken must be consistent with Government's aim of faster growth to match Australia's per-capita GDP income levels by 2025.

Preferred approach

- Stop, slow down, and simply change start dates of 1 July sectors to 1 January 2011 (or beyond) and no other changes to existing ETS at this stage (ACT would support National on this, guaranteeing a majority for this change).
- Leave bill in front of select committee for review post-Copenhagen and in the light of Australian and US developments.
- Do proper RIS: not clear that international relations and commercial benefits warrant costly action by New Zealand.
- Express preference for a low, revenue-neutral carbon tax as an initial measure for New Zealand, with exemptions for trade-exposed industries and subsidies for sinks. A carbon tax would facilitate statutory adjustments of contracts (for example Todd Energy). There is a growing international consensus that a carbon tax is preferable to an ETS, and a tax is much easier to dismantle than the property rights created under an ETS, should climate change concerns be ultimately unfounded.

Appendix

Committee procedure

The Climate Change Response (Moderated Emissions Trading) Amendment Bill was referred to us on 24 September 2009. The closing date for submissions was 13 October 2009. We received and considered 379 submissions from interested groups and individuals. We heard 128 submissions.

We received advice from the Emissions Trading Group made up of advisers from the Ministry for the Environment, the Ministry of Agriculture and Forestry, and the Ministry of Foreign Affairs and Trade; and from the Treasury. We also received advice from an independent specialist adviser, Dr Suzi Kerr.

Committee members

Craig Foss (Chairperson)
Amy Adams
David Bennett
John Boscawen
Brendon Burns
Charles Chauvel (from 14 October 2009)
Hon David Cunliffe
Aaron Gilmore
Raymond Huo (until 14 October 2009)
Rahui Katene
Peseta Sam Lotu-liga
Stuart Nash
Dr Russel Norman

Hon David Parker and Moana Mackey replaced Stuart Nash and Brendon Burns for this item of business.

Hekia Parata and Nicky Wagner attended all committee meetings on this item of business.