

The Chair
CABINET POLICY COMMITTEE

**CLIMATE CHANGE: SETTING THE DIRECTION FOR FUTURE DOMESTIC
POLICY OPTIONS AND RATIFICATION OF THE KYOTO PROTOCOL**

Executive Summary

1 The Kyoto Protocol marks the beginning of a long-term shift in the way that countries view the emissions of greenhouse gases generated by human induced activity. This will involve both the sources of emissions, including the use of fossil fuels, livestock and agricultural activity, as well as the removal of greenhouse gases from the atmosphere by “sinks” including forest areas. It will be important for New Zealand to be prepared for changes in the world economy and the possibility that subsequent commitment periods under the Protocol may be more demanding.

2 This paper seeks Cabinet approval in principle to ratify the Kyoto Protocol by August 2002, including approval to table the National Interest Analysis in Parliament. It also reports on messages from climate change consultations, provides a goal and principles for future policy development and implementation and sets out the timetable for future work.

Consultation

3 Consultation on the question of ratification and the different policy options for meeting New Zealand’s obligations was undertaken between 15 October and 21 December 2001. There was a wide range of views expressed during consultation. Some strongly opposed ratification on economic grounds; others strongly supported it on environmental grounds. Most argued, however, that the Government should take more time.

4 With regard to the wider public, survey results indicate that 47% of those surveyed favour the Government “signing up”, although many people “need to know more”.

Economic effects

5 The Government commissioned economic modelling on ratification of the Kyoto Protocol which indicates that, overall, the effect on the economy would not be significant - small net reductions in gross domestic product (GDP) but small increases in gross national income (GNI, which is GDP plus net transfers from abroad) as a result of income from sale of sink credits. On a sectoral basis, the results are more varied. For instance, some of the high emitting industries will be heavily affected if they are required to pay a high price for emissions and/or face increased input costs, to the point that they may become unviable in New Zealand. Reduced production or shutdowns would have an adverse economic effect on New Zealand and could cause an increase in global greenhouse gas emissions. This situation is referred to as ‘leakage’. Greenhouse policy needs to address competitiveness issues.

Goal and Principles

6 It is proposed that New Zealand's climate change response be guided by the following goal:

NZ should have made significant greenhouse gas reductions on business as usual and be set towards a permanent downward path for total gross emissions by 2012.

This sets the context for policy development and implementation and signals that the Government is serious about aiming for real reductions and is not going to simply buy its way out.

7 A range of principles is suggested in the paper that give body to the five criteria set out in earlier cabinet papers. It is proposed that these will guide the selection of a preferred policy response:

- Policies must result in permanent reductions in emissions over the long term;
- Policies need to be responsive to the changing international context;
- Policies need to be consistent with a growing and sustainable economy;
- Policies will not disadvantage the vulnerable in our society.

Reasons for Ratification

8 It is strongly in New Zealand's interests to ratify the Kyoto Protocol. The reasons for ratification can be summarised as follows:

- Increased climate change is predicted if global emissions of greenhouse gases continue to grow without constraint, with significant long-term adverse effects on the global economy, societies and ecosystems.
- More than any other developed nation, New Zealand depends for its prosperity on a stable climate. For New Zealand, threats to human health, land and water quality, infrastructure, biosecurity and native ecosystems are also significant.
- Climate change is a global problem and effective action to counter it is beyond the ability of any single country. The Kyoto Protocol is the only viable international response. The Protocol provides a means by which, over the long term, the risks to New Zealand can be mitigated.
- Abandoning the Protocol would damage New Zealand's credibility and its reputation as a global citizen – not only in climate change forums but also over a wide range of international issues.
- New Zealand's effectiveness in climate change negotiations means it is one of the few developed countries that stands to make a small net economic gain from the first Kyoto Protocol commitment period. Economic benefits are also likely to include technology and energy efficiency improvements.

9 The Government should now decide, in principle, to ratify the Kyoto Protocol ("the Protocol"). The decision would be subject to the further steps required to achieve ratification, including Select Committee consideration of the National Interest Analysis, enactment of the necessary legislation for ratification and final policy decisions on the preferred policy approach.

10 Effects of meeting obligations under the Protocol are largely dependent on the policy that Government implements to meet its obligations. New Zealand's policy will be designed to minimise the economic effects of policy options by allowing a transitional approach to

exposing the economy to the full price of carbon. If the policy principles set out above are followed when making policy, economic analysis indicates that the effects on the nation, and affected industries, should be minimal and manageable.

11 The key issue is the timing of ratification. The main objections to ratification by August 2002 relate to the uncertainty about the costs of the policy that will be implemented and a desire to ensure that New Zealand does not get too out of step with its main trading partners. These issues will be managed through the design of domestic policy measures, which will follow the principles set out above. They will also be managed by maintaining a proactive stance at international negotiations for the second and subsequent commitment periods.

Purpose

12 This paper:

- reports on messages from climate change consultations;
- states the goal and general principles for further development of a preferred policy package;
- seeks Cabinet approval in principle to ratify the Kyoto Protocol by August 2002;
- seeks Cabinet approval to table the National Interest Analysis in Parliament;
- sets out the timetable for future work.

Background

13 On 3 September 2001, following successful negotiations in Bonn on the final rules for the Kyoto Protocol, Cabinet agreed to move forward with the process for ratification of the Kyoto Protocol, with the aim of ratifying the Protocol by the time of the World Summit on Sustainable Development in September 2002 [CAB Min (01) 27/5A refers]. The World Summit has since been rescheduled to 26 August 2002.

14 On 8 October 2001, Cabinet considered a series of papers aimed at the ratification of the Kyoto Protocol. It agreed the content of “Act 1” minimum legislation necessary to enable New Zealand to meet its Protocol obligations and thus enable ratification, and to a first phase of consultation on the ratification of the Protocol and a range of domestic policy options that New Zealand could use to meet its obligations under the Protocol. Final policy decisions are to be implemented eventually in “Act 2” legislation [CAB Min (01) 31/11-14 refer].

15 On 3 December 2001 Cabinet considered the necessary institutional arrangements for Act 1 legislation [CAB Min (01) 37/5 refers]. Drafting instructions for the Act 1 legislation were issued to Parliamentary Counsel Office on 20 December 2001. The first major step in the ratification process occurs with the introduction into Parliament of the text of the Protocol and the National Interest Analysis.

16 Consultation on the question of ratification and the different options and was undertaken between 15 October and 21 December 2001. There was a wide range of views expressed during the consultation. Some strongly opposed ratification on economic grounds; others strongly supported it on environmental grounds. Most argued, however, that the Government should take more time.

Messages from climate change consultation

17 Key messages arising from the consultation were largely based on economic concerns. Although the majority of people who oppose ratification accept that there is a need to respond to climate change and, in particular, to reduce greenhouse gas emissions, there is:

- a strong message from some affected stakeholders that the Government is moving ahead with ratification too fast. Some stakeholders are questioning whether the Protocol is the appropriate framework for achieving the necessary outcomes while others are suggesting that ratification can be delayed until more information has been gathered, particularly on the likely implementation policies and the actions of our close trading partners;
- a request for more clarity about the potential costs and benefits of policies that might be put in place to meet our obligations, and the opportunities the Kyoto Protocol brings. Strong concerns were expressed about the lack of information about climate change and proposed policies prior to the consultation. Many stakeholders asked for on-going dialogue and information exchange;
- concern about the international competitiveness of many of our industry sectors when not all countries have the same requirements under the Kyoto Protocol;
- little clarity from stakeholders about what policies they preferred;
- a low level of real understanding within the wider community about what the Kyoto obligations entail. Responses in written submissions suggested that a number of smaller stakeholders, particularly in the agricultural and small business sectors as well as private individuals, were not familiar with the issues and concepts on which consultation was based.
- with regard to the wider public, preliminary results from a public survey carried out by UMR from 19-20 January 2002 show:
 - 47% of those surveyed favour the Government “signing up” to the Protocol
 - 6% are opposed
 - 42% “need to know more”
 - The number of respondents who were aware of the Kyoto Protocol has risen 15% since March 2001 (from 39% to 54%). Of these, 54% support ratification, 10% oppose it and 32% want more information.
 - The number of respondents who *were not* aware of the Kyoto Protocol had dropped since March 2001 from 60% to 43%. Of those who were unaware of the Protocol, 38% favour ratifying it, 1% oppose ratification, and 56% require more information.

18 Further details from consultation are set out in Annex I.

Proposed future policy directions

Policy options consulted on so far

19 Previously, Cabinet has noted that existing policies that result in reduced greenhouse gas emissions will not reduce emissions back to 1990 levels. New policies are needed to encourage cost-effective reductions. If those reductions are insufficient, New Zealand will

also need to obtain the revenue needed to pay for emission units to cover any greenhouse gas emissions in excess of 1990 levels. [CAB Min (01) 31/12 refers]

20 Consultation on policy so far has been based largely on a range of options for reducing and/or paying for excess emissions, including taxes, emissions trading, levy/rebate systems, projects and Negotiated Greenhouse Agreements. Options for the allocation and management of sinks have also been discussed. Until now, a key question has been the degree to which Government or emitters take responsibility for managing emissions and sinks, whether or not different emitters should be treated differently and the timing/phasing of policy instruments.

21 Cabinet has endorsed five dimensions for decision-making on climate change policy. These are:

- environmental integrity;
- competitiveness;
- economic efficiency;
- feasibility; and
- equity.

However, no guidance was given on the relative priorities of these dimensions.

Economic analysis on some policy scenarios

22 In addition to the consultation, the Government commissioned economic modelling from the Australian Bureau of Agricultural and Resource Economics (ABARE) on the effects of certain policy scenarios on the economy. The scenarios examined are set out in the National Interest Analysis provided in Annex IV.

23 ABARE's modelling indicated that, overall, the effect on the economy would be small. Most scenarios showed small net reductions in gross domestic product (GDP) but small increases in gross national income (GNI, which is GDP plus net transfers from abroad) as a result of income from sale of sink credits.

24 However, under ABARE's analysis, some of the high emitting industries will be heavily affected if they are required to pay a high price for emissions and/or face increased costs as a result of a high emissions price on key inputs, to the point that they may become unviable in New Zealand. The modelling by ABARE shows that the industries whose output is most sensitive to a high emissions price are iron and steel, aluminium, coal, gas, electricity, meat, dairy (including dairy processing) and wool. Work undertaken by PA Consulting has also identified that the cement, petroleum refining and, possibly, wood processing industries are also sensitive to a high emissions price.

25 For these industries there is a risk that the principle of environmental integrity would be breached if a high emissions price were applied to emissions in New Zealand. This is because these industries are all subject to competition in either export markets or from imports in the domestic market. Any reduction or cessation of supply from these New Zealand industries would be made up by increases in supply from the developed countries that do not ratify the Protocol or developing countries that do not have targets under the Protocol. This would have an adverse economic effect on New Zealand and an increase in global greenhouse gas emissions. This situation is referred to as 'leakage'.

Overall goals for future climate change policy

26 The Kyoto Protocol is a first binding step in international action to limit greenhouse gas emissions. It aims for an overall worldwide reduction in greenhouse gas levels of 5% over the first commitment period, even though global reductions of up to 60% are likely to be needed in the long term. It is expected that future commitment periods will be negotiated that set deeper obligations for emissions reductions and involve a wider range of countries, including some of the more advanced developing countries. The Kyoto Protocol therefore marks the beginning of a long-term shift in the way that countries view the emissions of greenhouse gases generated by human induced activity. This will involve both the sources of emissions, including the use of fossil fuels, livestock and agricultural activity, as well as the removal of greenhouse gases from the atmosphere by “sinks” including forest areas. It will be important for New Zealand to be prepared for changes in the world economy and the likelihood that subsequent commitment periods will be more demanding.

27 It is proposed that New Zealand’s climate change response be guided by the following goal:

New Zealand should have made significant greenhouse gas reductions on business as usual and be set towards a permanent downward path for total gross emissions by 2012.

This sets the context for policy development and implementation and signals that the Government is serious about aiming for real reductions and is not going to simply buy its way out.

28 The goal means that:

- New Zealand will be on a path to reshaping its energy use;
- there will be an increased rate of technology uptake on renewables, energy efficiency, lower emissions production;
- all sectors will be addressing emissions and positioning themselves greenhouse-wise on world markets;
- research findings will have been transferred to agricultural practice;
- new buildings, dwellings, plant, vehicles and machinery will be at the optimal edge of efficiency;
- there will be a population knowledgeable about greenhouse gases and taking responsibility for them.

29 Policies that drive New Zealand to a lower emissions future need to be balanced with the need to minimise the negative impact they may have on the country’s economic development, including ensuring that the transition to the future is done in a way that maximises net benefits. The information from consultation and from the economic modelling of different policy scenarios indicates the need for caution when devising policies that require emitters to pay a high price for their emissions or that exposes them to such mechanisms in advance of our major competitors. As discussed in paragraphs 22 to 25 above, this is because policy options that impose a high cost on emissions have the potential to significantly affect certain sectors of the economy with no real gain in terms of overall global reductions in greenhouse gas emissions. Policy also needs to take into account the evolving international policy context for such reductions.

Key principles for future policy development

30 How should this balance be achieved? A range of principles is suggested below that give body to the five criteria set out in earlier cabinet papers. It is proposed that these will guide work on, and the selection of, a preferred policy response. The goal and principles are reproduced in Annex II.

31 *Policies must result in permanent reductions in emissions over the long term*

- Policies must achieve real and sustainable reductions in emissions across all commitment periods – both to protect New Zealand’s international credibility and to ensure that we are prepared for future commitment periods.
- Policies should avoid carbon leakage. This will protect the objectives of the Protocol pending the creation of a truly global emissions regime.
- Policies will aim for long-term permanent changes in behaviour.

32 *Policies need to be responsive to the changing international context*

- The policy approach needs to recognise the uncertainty about future changes up to 2012, including changes in our emissions profile, in technology, and the international environment.
- Policy development will be incremental, building from low cost policies now to policies that expose emitters to the full emissions price as factors such as knowledge and certainty increase and as countries currently without emissions targets take on targets and expose their economies to the international price of carbon.
- Policies therefore will be adaptable and flexible, recognising the need for businesses and other stakeholders to be able to accept and respond to policy changes. They should allow for a transitional, staged approach to give affected emitters time to adjust.
- Policies must be simple and comprehensible in order to effect the necessary behavioural changes.
- Policies will be increasingly globally focused as targets under the Kyoto Protocol become increasingly globally based.
- Policies will be developed in close consultation with stakeholders, and will include processes for partnership and cooperation with key affected stakeholders.
- The policy package will include regular reviews of progress with emission reductions and effectiveness of policies, and criteria or milestones for when policy changes or new policy might need to be set in place. This includes periodic review of the goal, having regard to our domestic actions and the evolving international market situation.

33 *Policies need to be consistent with a growing and sustainable economy*

- Policies will recognise that competitiveness now and tomorrow is important for all our industries (including new entrants).
- Policies will move progressively to a full cost on emissions when competitiveness issues have been addressed by a full global targets regime.
- Policies should avoid inappropriate distortionary effects on investment.
- Policies will promote economic opportunities in climate change.

34 *Policies will not disadvantage the vulnerable in our society*

- Policies should aim to ensure that lower socioeconomic groups are not disadvantaged as a result of Kyoto commitments.

35 Provided the preferred policy approach follows this goal and principles, the competitiveness and economic issues discussed in paragraph 27 will be addressed. In particular, the work to be undertaken by officials will provide the opportunity to further assess the costs and benefits as well as the potential risks and opportunities of ratification and the extent to which the principles can be met.

Ratification and the National Interest Analysis

36 The Government is now in a position to decide, in principle, whether to ratify the Kyoto Protocol. The decision would be an in-principle one subject to the further steps required to achieve ratification, including select committee consideration of the National Interest Analysis, enactment of the necessary legislation for ratification and final policy decisions on the preferred policy approach. A further Cabinet decision will therefore be required before ratification can take place.

37 As discussed in paragraph 26, the Protocol is an international agreement that will mark the beginning of a long term change in the way that the world views the emissions of greenhouse gases generated by human induced activity. A description of New Zealand's obligations under the Protocol is provided within the National Interest Analysis, which is attached in Annex IV.

Reasons for ratification

38 There are a range of reasons why New Zealand should ratify the Kyoto Protocol and these are set out in detail in the National Interest Analysis. A summary of the key reasons is set out below:

- Increased climate change is predicted if global emissions of greenhouse gases continue to grow without constraint. The resulting climate change threatens to have significant long-term adverse effects on the global economy, societies and ecosystems.
- More than any other developed nation, New Zealand depends for its prosperity on an equable and stable climate. The New Zealand economy is grounded in primary production. The strength of the primary sector is due in large part to New Zealand's excellent climate for pastoral farming.

- Threats to human health, land and water quality, infrastructure, biosecurity and native ecosystems are also significant. New Zealand has a clear and direct interest in supporting efforts to minimise climate change.
- Climate change is a global problem and effective action to counter it is beyond the ability of any single country. The Kyoto Protocol has been the international community's response. No viable alternative international approaches to the Kyoto Protocol have been developed or proposed, and any alternative would likely involve many more years of delay in reducing greenhouse gas emissions.
- New Zealand has taken an active and constructive role in more than ten years of international negotiations leading to the formulation of the Kyoto Protocol. Abandoning the Protocol would damage New Zealand's credibility and its reputation as a global citizen – not only in climate change forums but also over a wide range of international issues.
- New Zealand's effectiveness in climate change negotiations means it is one of the few developed countries that stands to make a small net economic gain from the first Kyoto Protocol commitment period. This gain arises because the carbon sink credits New Zealand which should more than offset the emissions reductions required to meet New Zealand's emissions target.
- Economic benefits of the Kyoto Protocol are also likely to include improvements in technology energy efficiency, and improvements in animal yield. Rejection of the Protocol would carry the contrary risk of falling further behind competing nations in energy and animal efficiency and trailing a significant shift in energy and agricultural technology rather than helping to lead it.

Effects on New Zealand of ratifying the Protocol

39 The National Interest Analysis discusses the effects of ratifying the Protocol, focusing particularly on the economic effects. There are some costs related to ensuring that the mechanistic elements of the Protocol are properly undertaken, such as monitoring levels of greenhouse gases and maintaining a registry of trading of emission units. These have been assessed in CAB Min (01) 37/5.

40 Effects of meeting obligations under the Protocol are largely dependent on the policy that Government implements to meet its obligations. The Kyoto Protocol provides virtually unlimited flexibility to countries in terms of their national policies. New Zealand's policy will be designed to minimise the economic effects of policy options by allowing a transitional approach to exposing the economy to the full price of carbon. The National Interest Analysis indicates that, provided the policy principles set out in paragraphs 31 to 34 of this paper are followed when making policy, the effects on the nation, and affected industries should be minimal and manageable.

Overall Assessment

41 Overall, I consider that it is strongly in New Zealand's interests to ratify the Kyoto Protocol. Climate change has long-term implications and potentially substantial costs for New Zealand. As a climate-dependent, primary producing country with significant concentrations of population and infrastructure in coastal areas, climate change presents a significant risk to our way of life. The Kyoto Protocol provides a means by which, over the long term, those risks can be mitigated. On balance, most submitters and the general public agree that there

needs to be international action on climate change and that the Kyoto Protocol is the best means to achieve this.

42 In my view, therefore, ratification offers genuine benefits, albeit benefits that are difficult to quantify at this time. This raises the question, which arose during the consultation process, of the appropriate policy response to the uncertainties about costs and benefits we face at this early stage of policy development and at this early stage of the Protocol's life. Some stakeholders expressed concern about the possible costs of ratification, and many respondents expressed the view that a decision on ratification should be deferred pending more information on the costs and benefits of implementation policies and the actions of trading partners.

43 While these concerns can and should inform policy development, they do not constitute compelling reasons for the Government not to decide in principle to ratify. The Government's preferred policy package will be designed with the policy principles set out in paragraphs 31 to 34 in mind. This paper recommends therefore a decision in principle to ratify, which can be implemented only in light of that policy analysis. In this manner, the concerns raised during consultations will be addressed through the measures the Government adopts to fulfil its obligations.

44 It is therefore recommended that Cabinet agree in principle to ratification, subject to Select Committee consideration of the National Interest Analysis, the passing of ratification legislation and final agreement on a policy approach that is consistent with the policy principles set out in paragraphs 31 to 34. Final decisions on ratification will occur after the final decisions on the policy approach in July 2002.

Next Steps

45 A proposed timetable for the next steps for the policy and ratification programme is set out in Annex III. A preferred policy package will be presented to Cabinet by 31 March 2002, with consultation on this package timed for April/May, and final policy approval by Cabinet in late July. Prior to formal ratification it is intended that there be a formal announcement setting out the policy approach.

46 This paper seeks approval for the National Interest Analysis to be presented to the House, along with the text of the Kyoto Protocol. It will then stand referred to the Foreign Affairs, Defence and Trade Select Committee. Once the Select Committee has reported back to Parliament or 15 sitting days have elapsed following presentation, the legislation necessary for ratification can be introduced.

Consultation

47 The following departments have been consulted and their comments incorporated in the paper: the Ministry for the Environment, the Ministries of Research, Science and Technology, Transport, Foreign Affairs and Trade, Economic Development, Te Puni Kokiri and Treasury.

Specific Māori /Treaty of Waitangi Issues

48 The National Interest Analysis indicates that ratification of the Kyoto Protocol does not conflict with the principles of the Treaty of Waitangi. Ratification of international treaties is an exercise of kawanatanga by the Crown. Maori have been consulted about the

ratification of the Protocol and their views, as well as the principles of the Treaty, are being taken into account in the development of policy to meet Protocol obligations.

49 There are no other Treaty implications arising from this paper.

Fiscal Implications

50 There are no fiscal implications arising from the introduction of the National Interest Analysis to Parliament. Fiscal implications arising from the introduction of legislation for ratification (which will be introduced once the Select Committee has reported back to Parliament on the National Interest Analysis or 15 sitting days have elapsed since its presentation) have been previously noted in CAB Min (01) 37/5. Fiscal implications arising from the implementation of policy to meet Kyoto Protocol obligations will be discussed in future papers on the preferred policy response in mid March.

Legislative Implications

51 There are no legislative implications arising from this paper. Legislation to enable ratification of the Kyoto Protocol has been previously set out in CAB Min (01) 31/11 and CAB Min (01) 37/5.

Recommendations

52 It is recommended that the Committee:

Consultation

- a) **note** that phase one of the consultation on the ratification of the Kyoto Protocol and options for domestic policy measures has been completed. Major messages from consultation included:
- a strong message from some affected stakeholders that the Government is moving ahead with ratification too fast. There was a desire for more clarity about the potential costs and benefits of policies that might be put in place to meet our obligations, and the opportunities that the Protocol brings.
 - concern about the international competitiveness of some of our sectors when not all countries have the same requirements under the Kyoto Protocol
 - general support for ratification from the survey of the general public, although there was low level of real understanding within the wider community about what the Kyoto obligations entail.

Directions for policy approach following consultation and analysis

- b) **note** that the Kyoto Protocol is only the first binding step in the control of greenhouse gases. It signals a long term change in the way the world will think about key resources. Because of this the Government needs to indicate that it is serious about aiming for real reductions in emissions.
- c) **note** that consultation and economic modelling indicate that policy options that impose a high cost on emissions have the potential to significantly affect certain sectors of the New Zealand economy and at the same time increase overall global greenhouse gas emissions.

- d) **note** that a goal and principles that provide direction for future policy development and implementation have been proposed in Annex II that recognise the need to move towards long term reductions in emissions while protecting the economy.
- e) **agree** that the goal and principles for policy set out in Annex II should drive the development of the preferred climate change policy response.
- f) **note** that further work is underway to develop the preferred policy response and officials will report to Cabinet on this by 31 March 2002.

National Interest Analysis and Ratification of the Kyoto Protocol

- g) **note** that the National Interest Analysis in support of the ratification of the Kyoto Protocol is attached in Annex IV.
- h) **note** that broad acceptance by some affected stakeholders of an in principle decision to ratify the Kyoto Protocol can not be expected before policy decisions confirm that their concerns about costs and benefits of policies will be addressed.
- i) **note** that as the preferred policy package is developed there will be further occasions to assess the cost and benefits, as well as the risks and opportunities of ratification, so as to maximise New Zealand's interests.
- j) **agree in principle** to ratify the Kyoto Protocol prior to or at the World Summit on Sustainable Development beginning 26 August 2002, subject to select committee consideration of the National Interest Analysis, passing of the necessary legislation for ratification and final decisions on the preferred policy approach consistent with the principles in Annex II.
- k) **note** that a further Cabinet decision authorising ratification will therefore be required before ratification can take place.
- l) **note** that ratification will require deposit of the ratification instrument at the United Nations in New York by August 23 2002, or at the World Summit if a depositary function is to be provided.
- m) **approve** the immediate presentation in the House of the Kyoto Protocol and the National Interest Analysis attached in Annex IV, in accordance with the international treaty examination process.
- n) **note** that drafting instructions were issued in December 2001 to Parliamentary Counsel Office for the minimum legislation required to enable ratification, in accordance with the directions in CAB Mins (01) 37/5 and 11.

Future timetable

- o) **note** the timetable for future work attached in Annex III.

Hon Pete Hodgson
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ANNEX I – Additional Points from Consultation

In addition to the overall comments set out in paragraph 15 of this Cabinet paper, there are also concerns about economic impacts of climate change policies across different industry sectors, together with areas of specific interest:

Agricultural sector

- difficulties and inaccuracies in measuring agricultural emissions.
- concern that few if any agricultural competitors will face the cost of their emissions due to the much smaller significance of agricultural emissions in all other Annex 1 (developed) countries.
- a lack of technological solutions might mean emission reduction would be achieved at the expense of production.
- charges or levies on agricultural emissions would therefore be inequitable.

Forestry sector

- long production cycle limits forest owners' ability to factor costs arising from policies into strategic business planning.
- concerns of the effect of policy decisions on future investment and expansion of forestry in New Zealand and on land use decisions.
- the 1990 baseline is arbitrary and will allow a minority of forest owners to gain a windfall benefit while the majority of forest owners would face a contingent liability for any future land conversion.
- increased production costs and consequent decrease in forest value will impact on Maori forest owners, on employment and on the legal relationship with Maori partners under joint venture arrangements.

Business and commercial sector

- focused on economic outcomes.

Local authorities

- need more information about possible impacts of policy at regional and sub-regional levels.
- clarification of the role of local authorities in implementing climate change strategies.
- need to give greater weight to the strategies for adapting to climate change which are likely to be adopted at community level.

Some Maori submitters:

- Maori have not been actively involved in the ratification process and in policy development in a manner consistent with the principles of the Treaty of Waitangi and the recognition of kaitiakitanga.
- climate change policies will have adverse economic outcomes on the primary production sector, which forms the basis of the Maori commercial asset base.
- the introduction of emissions trading does not consider the cultural practices and spiritual values of Maori.
- economic outcomes of climate change policies may erode the value of past and future Treaty Settlement assets and lead to an increase in the quantum of claims.

There was a lack of detailed discussion of policy options and preferences amongst many of the stakeholders. While the focus of the written submissions was on issues relating to ratification, some general themes in respect of policy options were:

- a need for co-ordinated policy and consistent objectives across sectors, legislation and regulations and related policy initiatives and strategies.
- general recognition policies should be sector specific and flexible.
- a need to recognise that limiting emissions would be constrained by the current state of technology and asset life cycles.
- there should be rewards, not just sanctions, for emissions reduction activities.
- supply side and demand side policies must be introduced.
- some support for Government taking full responsibility for emissions and funding any costs through general taxation, at least in the first commitment period. Some submitters also suggested a mix of responsibility, with Government assuming high level responsibility for the regime, through policies and action at international level, while management of reduction strategies would be undertaken by those best placed to implement the strategies.
- limited support for emissions charges. Most support for charges was from submitters representing environmental interests. Opponents of ratification tended not to favour charges because of the impact on production costs, prices and competitiveness.
- mixed views on whether emissions trading is the best means to manage emissions.
- a tendency amongst stakeholders to favour hybrid policy that would allow for flexibility and for appropriate policies to be determined on a sector by sector basis. Business groups in particular supported extension of the use of Negotiated Greenhouse Agreements and other voluntary arrangements.
- concern at the lack of detail on proposals to manage transport emissions. Many were looking for more information on policies to encourage use of more fuel efficient transportation modes such as public transport, rail, shipping, walking and cycling.

Further conclusions from consultation included:

- a number of submitters indicated support for ratification. The key point of difference was the timing of ratification. There was a view from strong supporters of ratification that urgent action is needed for environmental reasons. Many submitters also point to the need for changes to be made to individual patterns of consumption.
- no clear indication of the relative priorities stakeholders give to the five criteria for decision making endorsed by Cabinet. Stakeholders with commercial interests who opposed ratification of the Kyoto Protocol in August 2002 tended to identify Efficiency, Equity, Feasibility and Competitiveness as the dimensions that influenced their views. Supporters of ratification tended to identify Environmental Integrity as the policy dimension which influenced their views.

ANNEX II – Goal and principles for a preferred climate change policy approach

Goal: New Zealand should have made significant greenhouse gas reductions on business as usual and be set towards a permanent downward path for total gross emissions by 2012.

This goal means that:

- New Zealand will be on a path to reshaping its energy use;
- there will be an increased rate of technology uptake on renewables, energy efficiency, lower emissions production;
- all sectors will be addressing emissions and positioning themselves greenhouse-wise on world markets;
- research findings to date will have been transferred to agricultural practice;
- new buildings dwellings, plant, vehicles and machinery will be at the optimal edge of efficiency;
- there will be a population knowledgeable about greenhouse gases and taking responsibility for them.

Key principles for future policy development

Policies must result in permanent reductions in emissions over the long term

- ⇒ Policies must achieve real and sustainable reductions in emissions across all commitment periods – both to protect New Zealand’s international credibility and to ensure that we are prepared for future commitment periods.
- ⇒ Policies should avoid carbon leakage. This will protect the objectives of the Protocol pending the creation of a truly global emissions regime.
- ⇒ Policies will aim for long-term permanent changes in behaviour.

Policies need to be responsive to the changing international context

- ⇒ The policy approach needs to recognise the uncertainty about future changes up to 2012, including changes in our emissions profile, in technology, and the international environment.
- ⇒ Policy development will be incremental, building from low cost policies now to policies that expose emitters to the full emissions price as factors such as knowledge and certainty increase and as countries currently without emissions targets take on targets and expose their economies to the international price of carbon.
- ⇒ Policies therefore will be adaptable and flexible, recognising the need for businesses and other stakeholders to be able to accept and respond to policy changes. They should allow for a transitional, staged approach to give affected emitters time to adjust.
- ⇒ Policies must be simple and comprehensible in order to effect the necessary behavioural changes.

- ⇒ Policies will be increasingly globally focused as targets under the Kyoto Protocol become increasingly globally based.
- ⇒ Policies will be developed in close consultation with stakeholders, and will include processes for partnership and cooperation with key affected stakeholders.
- ⇒ The policy package will include regular reviews of progress with emission reductions and effectiveness of policies, and criteria or milestones for when policy changes or new policy might need to be set in place. This includes periodic review of the goal, having regard to our domestic actions and the evolving international market situation.

Policies need to be consistent with a growing and sustainable economy

- ⇒ Policies will recognise that competitiveness now and tomorrow is important for all our industries (including new entrants).
- ⇒ Policies will move progressively to a full cost on emissions when competitiveness issues have been addressed by a full global targets regime.
- ⇒ Policies should avoid inappropriate distortionary effects on investment.
- ⇒ Policies will promote economic opportunities in climate change.

Policies will not disadvantage the vulnerable in our society

- ⇒ Policies should aim to ensure that lower socioeconomic groups are not disadvantaged as a result of Kyoto commitments.