



November 2008

Climate Change update

Agriculture and the Emissions Trading Scheme

Having become law in September 2008 the Emissions Trading Scheme is now reality for New Zealand. The agricultural sector will enter New Zealand's Emissions Trading Scheme (**ETS**) from 1 January 2013. Those importing or manufacturing nitrogen-containing synthetic fertiliser, certain persons slaughtering ruminant animals, pigs, horses, or poultry and all persons undertaking dairy processing of milk or colostrum will all be mandatory participants. The result will be increased costs to the agricultural sector and those that rely on it. *Are you ready?*

Developments

- The Climate Change Response (Emissions Trading) Amendment Act 2008 received Royal assent on 25 September 2008. It introduces the ETS and amends the **Climate Change Response Act 2002** (the **Act**).
- On 8 November 2008 New Zealand elected a new government. The National party-led government has promised to change the ETS, but the scale of the proposed changes is currently unknown. Lobbying from the agriculture sector to the National party is expected to be significant.

The Emissions Trading Scheme

The ETS assists New Zealand in meeting its international climate change commitments. New Zealand has committed under the Kyoto Protocol to reducing its climate change emissions to 1990 levels and to otherwise take responsibility for emissions above that level.

The ETS is a market-based mechanism. The ETS currency is the New Zealand Unit (**NZU**) which can be traded in New Zealand. The NZU is linked to the international Kyoto Protocol market and can generally be interchanged with Kyoto Protocol Assigned Amount Units (**AAUs**) as well as other Kyoto Units. The ETS has mandatory and voluntary participants for various sectors. There is no cap on a participant's level of emissions; rather participants are incentivised to avoid the cost of NZUs by reducing their level of emissions.

What it covers

There has been a debate about who is appropriate to impose this sector's obligations upon: farmers or processors. The outcome remains open. The Act provides that unless the government decides before 30 June 2010 to make the point of obligation at the farmer level, the obligations will be imposed on processors. Regardless of the approach taken the ETS will enable the other group to volunteer to be involved.

Agricultural activities that the ETS focuses upon are in two areas: fertiliser and animals. Liability for these two areas remains regardless of the point of obligation.

Assuming the **processor level** of obligation remains, **mandatory participants** will be involved in:

- Importing or manufacturing synthetic fertilisers containing nitrogen.
- Slaughtering ruminant animals, pigs, horses or poultry by certain persons
- Dairy processing of milk or colostrum.

Assuming in 2010 the **farmer level** of obligation is chosen to be imposed, **mandatory participants** will be involved in:

- Purchasing, other than for on-selling, synthetic fertilisers containing nitrogen
- Farming, raising, growing or keeping ruminant animals for reward or the purpose of trade.

Regardless of the point of obligations, **voluntary participation** can occur in the following activities:

- Purchasing, other than for on-selling, synthetic fertilisers containing nitrogen, where the total synthetic fertiliser purchased exceeds a prescribed amount
- Farming, raising, growing or keeping ruminant animals for reward or the purpose of trade and where the total number of animals or emissions from those animals exceeds the prescribed amount.

Other sectors included in the ETS are forestry, stationary energy and industrial processes. Waste and agriculture will be the last sectors to enter the ETS in 2013.

Free Allocation – Allocation Plans

The expectation is that participants will pass through the supply chain costs of satisfying ETS obligations. For some this will reduce competitiveness. To ease the pain and to provide a "transition" while businesses adjust to these extra costs, some NZUs will be freely allocated to people who apply. The amount of NZUs will not cover a participant's entire liability to surrender NZUs.

Free allocations are available to the agricultural sector.

However, the scope of these allocations has not been confirmed. These allocations will only be issued up to 90% of 2005 emissions and will be gradually phased out by 2030. Consequently agriculture will not bear the total brunt of its emission costs until this date. Given its importance to the New Zealand economy, it remains to be seen whether this level of allocations will be sufficient to avoid driving up the cost of dairy product exports while still incentivising reductions in emissions.

In due course detailed eligibility criteria will be provided in a draft allocation plan. There will be an opportunity to comment on that plan before it becomes law.

There are also free units available in an Innovation Fund to facilitate deployment of innovative technology that has the potential to significantly reduce greenhouse gas emissions.

General Tax Treatment

If you will be trading and surrendering NZUs, you need to make sure you are able to pay the necessary costs. You are liable for tax obligations and need to ensure you are aware of those obligations. Generally:

- Tax payers are allowed a deduction for their accrued emissions liability.
- Any gain on the sale of emissions units will generally be taxable with a deduction for the cost of the units.
- There will be no tax consequences when an emissions unit is received from the government and surrendered in the same income year.
- Emissions units held by a person over an income year will be taxed under modified trading stock rules.
- Emission units will be zero rated for GST purposes.

For specific tax advice on climate change matters please contact the [Minter Ellison Tax team](#).

Penalties for Non compliance

There are civil penalties for non-compliance with the scheme aimed at supporting the obligations under the ETS of calculating emissions and surrendering equivalent NZUs.

Criminal offences apply when a person without good reason, knowingly or with intent to deceive, fails to collect information, register as a participant, submit an emissions return or keep information in relation to an activity.

This advice is general in nature. We recommend you obtain specific advice on how you may be affected by the ETS. We would be happy to assist you to understand further how to comply with your obligations under the ETS, and make the most of the scheme. Please [contact us](#).

Participant Obligations – Are you ready?

Commencement dates

Reporting is voluntary from 1 January 2011 and mandatory from 1 January 2012. Obligations commence 1 January 2013.

Are you registered?

Participants are not required to register until their sector enters the trading scheme, although they can choose to register earlier. Participants have 20 working days to give notice to the chief executive of the Ministry of Economic Development (MED) once they become a participant. Voluntary participants may apply to the chief executive to register as a participant.

Do you have a holding account?

At the time of registration participants must apply to open a holding account, if they don't have one already. Participants must have a holding account to receive and surrender units under the scheme. A holding account can be obtained from the [New Zealand Emissions Register](#).

Do you know how to monitor and calculate emissions and removals?

Participants must, for each year they carry out relevant activities, collect described data or information, calculate the emissions and the removals activity in accordance with the relevant regulations (see below) and if required, have calculations verified by a recognised person.

Are you aware of the record keeping requirements?

Participants must keep records of the data, information and calculations. Participants must also retain records for seven years after the end of the period to which they relate.

Do you know how to file annual emissions returns?

For the agriculture sector, voluntary and mandatory reporting periods exist. Agriculture may voluntarily collect data from 1 January 2011, with mandatory reporting obligations commencing on 1 January 2012. Participants will have to file emissions returns before 31 March 2014.

Are you aware of the liability to surrender units to cover emissions?

Obligations to account for emissions commence on 1 January 2013 for agricultural participants. A participant is liable to surrender 1 NZU for each whole tonne of emissions covered by the scheme. After submitting their return by 31 March participants are required to surrender NZUs by 30 April of the same calendar year. The participant must make an application to transfer the required number of NZUs from the participants holding account to a surrender account designated by the chief executive of MED.

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