

emissions trading

August 2001



Bell Gully

Vantage point

An emissions trading market is becoming a reality. Despite the US withdrawing its support for a global market, domestic markets are emerging in Europe and Canada. New Zealand is moving in the same direction, and business can expect steps to be taken in the next year towards the possible establishment of a domestic market in New Zealand. This is the first in a series of commentaries on key features of an emissions trading market.

Emissions Trading Market Issue 1: The Point of Obligation

Introduction

At the recent climate change conference in Bonn, the international community progressed agreement on measures to meet targets for the reduction of greenhouse gases, undeterred by the United States' opposition to the Kyoto Protocol. Although a number of uncertainties remain, it appears likely that signatory countries will take steps towards implementing measures associated with ratification of the Kyoto Protocol. Central to these is the development of international and domestic trading markets to achieve reductions in greenhouse gas emissions. The framework for a potential New Zealand market is emerging and is likely to operate as follows:

- total national greenhouse gas emissions would be capped at 1990 levels;
- emission units (each representing one tonne of carbon dioxide equivalent) would be allocated to scheme participants;
- emission units could be traded; and
- for each reporting period, participants would be required to monitor and report their emissions and to reconcile actual emissions with units held. Penalties would be imposed if emissions exceeded units held.

"Scheme participants" have yet to be decided. The various points in the economy where entities will be required to participate in the scheme will be called "points of obligation". These are points where sufficient emission units needed to offset emissions.

Points of obligation

It is unlikely that only those who actually emit greenhouse gases will be participants in the scheme. For some sorts of emissions it may



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not be practical to require actual emitters to comply with the scheme. Vehicle emissions are an example. Requiring all motorists to purchase emission units in order to operate a car would be impractical. To get around this difficulty, obligations could, for example, be placed on petrol stations or oil companies.

Therefore, an entity which does not emit greenhouse gases, but provides products which ultimately produce greenhouse gases, may be subject to the scheme (this is called placing the point of obligation "upstream"). Rather than offsetting emissions against units, units would be offset against the total product distributed in the reporting period.

Similarly, if an entity uses a product which requires the emission of greenhouse gases to have occurred in its production, it may become subject to the scheme (by placing the point of obligation "downstream"). For instance, the

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creation of magnesium or aluminium involves the discharge of greenhouse gases from the smelter. An entity that uses the magnesium or aluminium may be made the point of obligation over the smelter that actually emitted the greenhouse gas. Emission units would be offset against the product purchased.

When determining where points of obligation will be placed, the government is considering a number of factors including administration, transaction and compliance costs and the ability to monitor an entity's activities. Ideally, maximum coverage of emissions with minimal impact on the economy will result.

Other participants

It is likely that anyone, whether designated as a point of obligation or not, may be allowed to participate by holding emissions units and trading them on the market.

Obligations

If chosen as a point of obligation, an entity's most important requirement will be to reconcile actual emissions (or product distributed or purchased) with emission units held.

To do this, the point of obligation would need to:

- hold an account at the emission unit registry which will record the number of units held and transferred ; and
- report sufficient data to enable emissions, or the movement of product, to be calculated.

Many of the potential scheme's components are dependent on international agreement, which has yet to be reached. What is clear, however, is that information received from points of obligation will be used to demonstrate compliance internationally.

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