

Principles of Incentive Scheme

A background paper prepared by Bay of Plenty Regional Council staff for Council and the Lake Rotorua Catchment Stakeholders Advisory Group (StAG), dated May 2013

Background

The proposed Regional Policy Statement (RPS) requires that the amount of nitrogen entering Lake Rotorua does not exceed 435 tonnes per year by 2032. This equates to a nutrient reduction of 320 tonnes per year.

The RPS does not provide direction for how this limit will be achieved, except that the limit will be allocated amongst land use activities (Policy WL 5B) and that rules will be required to managed the reduction of any nutrient losses that are in excess of the limits (Policy WL 6B).

Key projects and budgets have been agreed in the Ten Year Plan (2012-2022) in order to achieve Lake Rotorua's nitrogen limit. In particular, a nutrient reduction fund of \$45.5 million has been provided¹ to facilitate 200 t/y nitrogen reductions from rural land.

On 27 June 2012, a workshop was held with Councillors to discuss the potential ways for incentivising nutrient reduction in the Lake Rotorua catchment. At this workshop, staff were asked to develop a business case on how a market based scheme could be designed and delivered. In developing the business case, staff were asked to give consideration to:

- Taking a collaborative approach
- Ensuring the focus on whole of catchment outcomes
- Understanding the risks for Council
- Providing principles and criteria
- Managing unintended consequences
- Ensuring flexibility

At this workshop, staff were also asked to progress rules for Lake Rotorua as a matter of urgency and in conjunction with the incentives scheme. Key reasons were:

- In order for the incentive scheme to work, landowners need to know what the rules are going to be. The rules are the main driver for change; incentives are tools that can be used to help people achieve the target
- Both pieces of work address nutrient loss from land (particularly rural land) and will have the same stakeholders and issues to resolve
- We need to ensure that the incentives scheme complements the rules and that all work supported through the incentives scheme will help to reach the required targets

A paper was presented to the Strategy, Policy and Planning Committee on 31 July 2012. This paper agreed:

- That the development of rules for Lake Rotorua would begin immediately and in conjunction with the development of the incentives scheme
- That the previously agreed streamlined approach for developing rules in the Rotorua Te Arawa Lakes would be expanded for Lake Rotorua rules to ensure active engagement with stakeholders.

¹ Subject to Crown approval

On 28 September 2012, the Rotorua Te Arawa Lakes Strategy Group endorsed a terms of reference for the “Lake Rotorua Catchment Stakeholder Advisory Group”. The Group was proposed as a way to provide rural landowners in the lake catchment with the opportunity to help design and develop the rules and incentives scheme.

The key purpose of the Group is to provide oversight, advice and recommendations on “rules and incentives” options that will achieve the nutrient reduction targets needed from rural land in order to meet Lake Rotorua’s water quality target. Staff have met with the Group each month since November, to progress development of both rules and incentives.

On 1 November 2012, the Operations, Monitoring and Regulation Committee were asked to make a decision on how to progress land use change in the Lake Rotorua catchment while the rules and incentives programme is developed. Options considered included:

- Stop all land use change activity and defer all decisions through the future Incentives Scheme.
- Change the current [land management] activity to focus only on low risk opportunities identified through specific funding criteria
- Continue the current [land management] activity using the previously agreed approach of only incentivising initiatives that will achieve a reduction of at least 10% relative to an approved Rule 11 benchmark.

The Committee deferred the decision and no further direction has yet been sought.

Comment

Councillors have set a clear direction to develop the rules in conjunction with the incentives scheme. The rules are seen as the main driver to change and incentives are a tool that can be used to help support people achieve the target.

Ideally, we would want to be clear about what the rules are going to look like in order to run an incentives scheme effectively. This is because certainty can help landowners make business decisions. However, draft rules will not be delivered until December 2013, and they will not be notified until 2014. Individual property owners will not know the specific impacts of the rules for some time.

Staff, councillors and key stakeholders will have enough information when the rules are drafted in December 2013 to confidently establish an incentives scheme that complements the rules and does not give significant advantage or disadvantage to any sector of the community.

There is also an opportunity to use the incentives scheme to fund some land-use change *before* the rules are developed. If the Council delays, we may miss these opportunities to remove nitrogen from the lake. Staff note that in order to proceed with immediate opportunities, a Council and RTALSG decision is required.

The draft approach and principles have been developed to fit administration of the incentives scheme immediately and into the future (recognising a Council decision to act immediately is required).

Purpose

The purpose of the scheme is to incentivise land use change in the Lake Rotorua catchment to reduce nitrogen and help achieve the sustainable load for the lake.

The purpose of the scheme is not to:

- Pay for landowners to get to good practice
- Compensate for financial impacts of the rules
- Educate or raise awareness, or fund research projects
- Achieve the total reduction for the catchment

Incentive scheme approach

The incentive scheme will be run according to the following approach:

- An open and transparent process – information will be readily available about how proposals will be assessed and decisions made, scheme mechanisms will encourage competition
- Fair access – the incentives will be open to all landowners who are likely to be affected by nutrient reduction rules, there will be equal opportunities to apply for funding
- Well governed – there will be clear governance structures and accountability for decision making
- Based on efficient administration – we will use existing systems and resources where possible to ensure funding is used for the purpose intended
- Responsive to opportunities – within the boundaries of the agreed process we will engage with applicants to explore proposed outcomes and to look at funding options (such as loans, grants, joint ventures).

The **draft** principles are:

1. Nitrogen reduction to good management practice will not be incentivised
Incentives target the gap between good management practice and what the rules require. They are not intended to help farms get to good practice.
2. The most nitrogen reduction per dollar
All other things being equal, we will seek the lowest price for nitrogen
3. Only fund actions that make significant contributions
4. Reductions must be clear, quantifiable and measurable – e.g. through Overseer
5. We will only pay for the demonstrated cost of change
Funding should not be used to support nutrient reduction activities that are cost neutral to do or that are financially positive.
6. Perpetuity – we will fund activities that will achieve long term reductions
7. Nutrient reduction proposals with significant co-benefits will be favoured
Proposals that also include consideration of sustainable economic growth, natural capacity of the land, innovative technologies etc

Conservative approach before rules are developed

There is an opportunity to award funding before the rules have been significantly developed. If not approached correctly this could run the risk of undermining the overall incentive scheme. It could set precedent for funding activities that would not otherwise receive funding once the rules are in

place. This would disadvantage those that those seeking funding after the rule is developed and would be contrary to the approach and the principles.

However, if landowners are prepared to make changes now, we should take these opportunities while they exist. A reminder that a decision is required before this approach is taken.

To ensure there is no undermining of the overall incentives scheme, funding awarded prior to the development of the rules will be determined on a conservative basis.

Appendix One – SWOT Analysis

SWOT Analysis:

Provide incentives after rules developed

	HELPFUL (for your objective)	HARMFUL (for your objective)
INTERNAL (within organisation)	Strengths <ul style="list-style-type: none"> • Less work on incentives in the short term • Certainty of allocation before applying for incentive • People that are required most affected 	Weaknesses <ul style="list-style-type: none"> • Money in budget not spent for 2 years • Not making progress in reducing nutrient • May lose opportunities
EXTERNAL (outside organisation)	Opportunities <ul style="list-style-type: none"> • Greater uptake of funding once size of stick known • • • 	Threats <ul style="list-style-type: none"> • Underspend budget • Fail to meet TYP KPIs • Lose crown funding • Greater opposition to rule • Seen as compensation <u>d.t.</u> impact of rules.

SWOT Analysis:

Provide incentives before rules developed

	HELPFUL (for your objective)	HARMFUL (for your objective)
INTERNAL (within organisation)	Strengths <ul style="list-style-type: none"> • Meet TYP KPI • Meet obligations to community to • Reduce reserve • Minister wants to see plan before approving transfer • Improve water quality sooner 	Weaknesses <ul style="list-style-type: none"> • No established database • If we don't get right principles we may pay too much or pay • Not knowing what the rules will require • —
EXTERNAL (outside organisation)	Opportunities <ul style="list-style-type: none"> • People see action • Can still set portion of funding aside for people severely impacted by rules for use later in programme • Could use conservative Pilot for 2 years • Community has immediate need • Reduce opposition to rules • People volunteer change before being required to. 	Threats <ul style="list-style-type: none"> • People wait until rules are developed before applying • Opposition to criteria • Community doesn't like changes to trees