

Reference: 20240037

20 February 2024



Dear 

Thank you for your Official Information Act request, received on 23 January 2024. Your request was:

*I was hoping you could answer a question I have about treasury balance sheets and the unaccounted for financial liabilities that will come with purchasing offshore mitigation to achieve New Zealand's NDC1.*

*I have tried to do a bit of research on this matter, but I could not find any distinct reasoning as to why these cost do not appear as a liability on the government's books. Do you know what the reasoning or logic behind this might be (ie what accounting standards are used and why are these liabilities excluded)?*

*Someone people have taken the cynical view that Treasury doesn't believe we'll ever have to pay, because there is the underlying assumption that everyone will fail to meet their Paris goals and will choose to let each other off. But because National and Labour have both agreed to the 2030 and 2050 goals I assume this isn't the case.*

*I understand no contracts have been signed with overseas jurisdictions regarding overseas mitigation projects, however it seems rather odd that these liabilities aren't recorded officially on the governments books.*

You are correct that offshore purchasing of mitigation to support meeting New Zealand's first Nationally Determined Contribution (NDC1) under the Paris Agreement is not currently recognised in the Crown's accounts as a liability. We are happy to explain this treatment further.

The Crown's accounts must be prepared in accordance with Generally Accepted Accounting Practice (GAAP). Under GAAP, three tests must be met for a liability to exist:

- Is there a present obligation?
- Is there a probable future outflow of economic resources?

- Is the obligation reliably measurable?

Our current judgement is that these tests are not met in relation to New Zealand's Nationally Determined Contribution. The main reasons for this are outlined below.

The Paris Agreement does not create a specific party who has the ability to enforce Nationally Determined Contributions. This means that the NDC cannot be treated as a legal obligation, even if the Party in question fully intends to achieve it.

Even when a legal obligation has not been created, liabilities can also include 'constructive obligations'. These represent circumstances where the Government has created a valid expectation that it will take on a responsibility to other parties through a sufficiently specific statement, such that it has little or no realistic alternative but to settle it through a transfer of resources.

For the purpose of the Government's financial statements, the Treasury has judged that NDC1 also does not generate a constructive obligation, because the Government has a range of options available to it in relation to the approach it could take to meeting the NDC. Decisions have not yet been made that narrow these options to such an extent that the government has little or no realistic alternative but to settle the matter through a transfer of resources. For instance, the Government could use policy measures to pass the costs of achieving NDC1 onto private entities, but this has not yet been decided.

As an example of the specificity required, a previous constructive liability was created when the Government announced that it was prepared to purchase insured residential property in the red zones of Christchurch on a voluntary basis. This created a non-reimbursable economic sacrifice that was not adjustable at the discretion of the Government.

The tests of a probable future outflow of resources and the obligation being reliably measurable are also not yet met, because:

- the Paris Agreement does not require NDCs to be "settled" in any way if they are not met. By contrast, the First Round Kyoto Protocol agreement included a process for the settlement of Kyoto-related obligations that were reported as a liability.
- No reliable estimate of the cost of NDC1 can be made at this time because:
  - there is considerable uncertainty over the costs of the options that could be pursued to access emissions reductions
  - the Crown could choose to shift the costs of meeting NDC1 onto the private sector.

An explanation of the future fiscal costs and the rationale for the current accounting treatment is provided in Note 1 of the Financial Statements of the Government for the

year ended 30 June 2023.<sup>1</sup> You may also wish to refer to the key audit matter discussion by the Auditor General in the Financial Statements of the Government for the year ended 30 June 2022.<sup>2</sup>

While we do not consider that these costs should be recognised as a liability at this time, we have published scenarios for the costs of offshore mitigation. You can find these in “Ngā Kōrero Āhuarangi Me Te Ōhanga - Climate Economic and Fiscal Assessment” (CEFA), published in 2023. This report is available on our website here: [Climate Economic and Fiscal Assessment](#)

Chapter 7 of the CEFA explores several scenarios for the cost of offshore mitigation purchases required to meet NDC1.<sup>3</sup> The CEFA provides transparency over the possible future costs involved in meeting New Zealand's NDC1.

We hope this helps answer your query. Please note that this letter (with your personal details removed) may be published on the Treasury website. This reply addresses the information you requested. You have the right to ask the Ombudsman to investigate and review my decision.

Yours sincerely

Nicky Lynch  
**Manager, Climate Change**

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<sup>1</sup> <https://www.treasury.govt.nz/sites/default/files/2023-10/fsgnz-2023.pdf#page=60>

<sup>2</sup> [https://www.treasury.govt.nz/sites/default/files/2022-10/fsgnz-2022\\_2.pdf#page=40](https://www.treasury.govt.nz/sites/default/files/2022-10/fsgnz-2022_2.pdf#page=40)

<sup>3</sup> <https://www.treasury.govt.nz/sites/default/files/2023-04/cefa23.pdf#page=81>