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Chris Bunny
Deputy Chief Executive Building, Resource and Markets
Ministry of Business, Innovation and Employment
by email: chris.bunny@mbie.govt.nz

Dear Chris

I write in relation to the recent consultation on *Transforming Operational Efficiency – Building for climate change programme*, which a part of your Group released in August 2020.

Unfortunately, we were unaware of the consultation, and missed the submission deadline. Nonetheless our twofold interest in good public policy and the natural gas sector leads us to bring some comments to your attention.

The problem definition is inadequate

As you know, good public policy stands or falls on the clarity with which the market failure to be solved is identified. In this case, the problem definition seems inadequate to justify interventions of the nature proposed. While correct in stating that the building sector produces emissions, this is itself not enough to justify the regulations especially given the Emissions Trading Scheme (ETS) already prices all non-agricultural emissions. This means that commercial decision-making *already* accounts for the externalities associated with emissions, so firms have a current incentive to reduce emissions up to the point where costs exceed benefits.

Emissions policy should drive efficient reductions, not eliminate emissions

Even where building sector emissions remain, it is important to consider that the goal of emissions pricing and climate policy should not be to necessarily *eliminate* emissions, but to simply ensure that reductions are made when it is cost-effective and economically efficient to do so.

If regulations force abatement at high marginal costs in one sector, there will be fewer resources available across the economy to pursue lower-cost emissions abatement elsewhere. Given resource constraints, it is crucial for New Zealanders' well-being that emission reductions are made at lowest marginal abatement cost.

Policies require careful analysis

After regulating greenhouse gas emissions through an ETS to internalise costs, further direct interventions should only be made where there remain residual genuine and material market failures. It is possible that information asymmetries are present in the market, but even if Government considers it has a role in addressing these, the answer is likely to be simply providing information rather than direct market interventions.

Direct regulations have the highest risk of unintended consequences compared to market-based instruments. A high evidential threshold should be made before promulgating new regulations – both in terms of problem definition and establishing through high-quality economic analysis that benefits outweigh costs. When considering costs, the risk of government failure should also be factored in (whereby perverse outcomes arising from regulations make the problem worse). Crucially, policies outside of the ETS should also be assessed on a cost-per-tonne of emission reductions.

Climate policy is the best tool to achieve emissions reductions

Emissions should, in our view, be managed within climate policy, i.e. the ETS, wherever possible. This contrasts with sectoral interventions across a range of portfolios using statutes intended for another purpose (and which are therefore not well-designed for achieving emission reductions especially since many statutes pre-date the Zero Carbon Act framework and the legitimate contemporary concern for climate change). Sectoral goals have a high risk of misallocating resources across the economy due to coordination issues that would be unlikely to occur under simple emission pricing.

Indeed, sectoral goals and targets risk falling into the trap of reductionism – the pursuit of analysing a complex systemic problem in terms of its component parts on the basis that it is analytically easier to do so. While analytically seductive, it inevitably results in partial solutions to systemic problems and either the misallocation of resources, or parts of the problem not being addressed.

Implications for the gas market

Finally, it is important that the broader economic and social effects of regulations are considered and properly accounted for. The regulations for fossil fuel use will artificially and prematurely weaken demand for natural gas in the building sector. This will directly cut across expectations that producers and service providers have based plans upon and will reduce employment opportunities. New rules, even if implemented over time, will change behaviours immediately as people and firms incorporate future changes into current decision-making.

Ultimately, we consider that consumer choice should be afforded significant weight as individual actors can best determine their own preferences. This is entirely consistent with climate objectives as all decisions are made under an economy-wide emissions cap and trade system.

I would welcome the opportunity to discuss this with you or your officials.

Yours sincerely

John Carnegie
Chief Executive