Energy Resources Aotearoa
POWERING A BETTER NEW ZEALAND TOGETHER

energyresources.org.nz
energyskills.org.nz
energymix.co.nz
PO Box 25259, Wellington 6140

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Ministry for the Environment

By email: etsconsultation@mfe.govt.nz

Submission on annual updates to NZ ETS limits and price control settings for units 2024; and proposed changes to ETS regulations 2024

Introduction

1. Energy Resources Aotearoa is New Zealand's peak energy sector advocacy organisation. Our purpose is to enable constructive collaboration across the energy sector through and beyond New Zealand's transition to net zero carbon emissions in 2050.

2. This document constitutes our brief submission on your two consultations about the New Zealand Emissions Trading Scheme (ETS):

   a) annual updates to NZ ETS limits and price control settings for units 2024; and

   b) proposed changes to ETS regulations 2024.

Overarching comments

3. We agree the NZ ETS is the key tool to help New Zealand meet its emissions budgets, the Nationally Determined Contribution (the NDC), and the 2050 target. The ETS is the main incentive driving market-led measures to reduce **net emissions**.

4. However, updating NZ ETS settings every year has introduced significant price volatility and uncertainty for the market. Our advice is aimed at stabilising the ETS with appropriate legislative guardrails and providing much needed predictability in policy settings. This will enable the ETS to deliver net reductions in emissions in line with the budgets and targets without unnecessary and avoidable emissions leakage offshore or incentivising the premature shut-down of industry within New Zealand.

5. We support a least-cost transition to net zero. Recent energy and environmental policies have diverted New Zealand from the optimal pathway to net zero and

increased costs of operating and delivering energy. Such policies have included over-regulation of the fuel industry and a destructive ban on offshore natural gas exploration, which is in the process of being over-turned. These sorts of market-limiting policies have put New Zealand in a vulnerable position during a period of increasing demand for electricity and fuels.

6. It is necessary to turn this situation around. New Zealand needs all options to be available as part of a diverse and evolving energy and technology mix if we are to keep the lights on and the economy running, prevent emissions and jobs moving offshore, and provide energy and investment for the transition.

7. Significant adjustments to unit levels were proposed by the Climate Change Commission (the Commission) in its advice on ETS unit limits in March this year, invoking special circumstances because the Commission has, subsequent to its 2022 & 2023 advice now, deemed the market to have an additional supply of forestry units. The Commission attributes these changes to the impact of the mandatory 5-year emissions reporting period leading to a (one-off) increase in forestry NZUs being issued, some of which are for emissions reductions outside the 1st emissions budget and NDC periods. This matter should have been foreseen by the Commission and it is not appropriate to remedy this "error" through invoking a halving of auction volumes at short notice.

8. The indication by the Commission that an oversupply of units from forestry rather than the impact of price control setting uncertainty led the 2023 auctions to fail to clear warrants further analysis. While we support a reduction in units in line with the falling cap, the step change proposed by the Commission is not adequately evidence based and omits a proper analysis of market liquidity.

9. On the regulations update for 2024 we largely support the adoption of proposals for technical reasons but caution against unintended impacts from:

   a) over-prescribed reporting requirements resulting from changes; and

   b) missing out key fuel sources that could become available in future, such as wastewater, or biomass from forestry product.

10. We make recommendations below to support ETS policy that provides a stable regulatory backdrop for all forms of energy provision, while considering methodological changes that need to be accounted for.

Recommendations

11. On **annual updates to NZ ETS limits and price control settings for units 2024** we recommend:

   a) stabilising ETS settings through legislation so that the sinking cap is made visible to the market through to 2050;

b) reducing the frequency of reviewing ETS settings – annual is too frequent and has created price volatility and market uncertainty;[1]

c) considering a lower price corridor as a stabilising influence when reviewing the cost containment reserve;

d) ensuring that industrial allocation rights are preserved by legislation through to 2050;

e) decoupling forestry externalities (such as land use concerns with forestry planting) from ETS settings by managing them through appropriate other means, such as land use policies;

f) making minimum adjustments for methodological reasons to account for changes made in the latest Greenhouse Gas Inventory 2023;

g) reducing the surplus units in line with the sinking cap, not a one-off adjustment as proposed by the Commission for post-1989 forestry units that **may** enter the ETS (there is not sufficient evidence the market is or will be over-supplied); and

h) undertaking further analysis into potential forestry units entering the ETS and how these can be managed in future while retaining consistency in ETS unit settings.

12. On **proposed changes to ETS regulations 2024** we note that proposals for changes to default emissions factors (DEFs) are reflective of real changes to fuel volumes and quality and in respect of section 2 (natural gas), section 3 (liquid fossil fuels), and section 4 (waste sector) we recommend:

a) adopting proposed regulatory update 2 (updating DEFs for **natural gas** activities) in full, due to changes in the composition of mined natural gas over time, and particularly for the opening of new fields;

b) adopting proposed regulatory update 3 (updating DEFs for **liquid fossil fuels** activities);

c) adopting proposed regulatory update 4 (updating DEFs for **waste** activities) insofar as supporting that the ETS recognises the opportunity for biogas in the destruction of landfill gas and value-add in emissions reduction, however we note that not all waste types used as biogas feedstock are covered, which is important for a level playing field for incentivising biogas production;

d) streamlining the process for reapplications of unique emissions factors (UEF) to reduce costs for applicants, noting it will largely be a technical

1 The annual reviews also create unessential workload for officials, businesses and commentators who must participate.

correction to align with updates to DEFs and not of market advantage to applicants;

e) communicating publicly the consequential changes to carbon prices (and how to make calculations) from all the above, and breaking communications down into categories for producers, large users, businesses, and impacts for small users such as households; and

f) communicating to market participants who will have changes in reporting requirements and providing adequate lead time, information and easy to use templates for reporting to reduce the administrative burden.

Concluding comments

13. Thank you for the opportunity to submit on the two consultations. We appreciate the time and effort from officials that is evident in the consultation documents showing quality analysis and careful consideration of the options.

14. Our view remains that ETS settings need to be stable and predictable and provide incentives for businesses and producers to reduce harmful emissions while incentivising innovation and development of cleaner alternatives.

15. The last few years have revealed the unintended consequences of unstable ETS policy. Now is certainly the time to stop tinkering with ETS policy and create a stable platform for incentivising net emissions reductions through to 2050 and beyond.

16. We would like to maintain an open line of communication to provide further information from the industry on these matters as it comes to hand.