Evonik Peroxide Ltd PO Box 196, Morrinsville, NZ, 3340

Reforming the NZ ETS: Proposed Settings
Ministry for the Environment
PO Box 10 362, Wellington 6143.

By email to etsconsultation@mfe.govt.nz

28th February 2020

Arnold Yeoman
[redacted]

<u>SUBJECT: Submission on Reforming the NZ ETS: Proposed Settings</u>

Evonik Peroxide Limited thanks the Ministry for the Environment for the opportunity to make this submission on the Reforming the New Zealand Emissions Trading Scheme: Proposed Settings consultation document.

Our submission is attached.

<u>FOR EVONIK PEROXIDE LTD</u>

Arnold Yeoman
Site Manager

Submission on Reforming the New Zealand Emissions Trading Scheme: Proposed Settings consultation paper

Contact information

Company Name	Evonik Peroxide Limited
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Submitter Information:

Evonik Peroxide should be classified as follows:

- Business/industry
- Industrial processors
- Stationary energy (excluding electricity)

NZ ETS Participation:

- Evonik Peroxide is an Emissions Intensive Trade Exposed (EITE firm) for the eligible activity of manufacturing hydrogen peroxide.

Commercial Sensitivity

- Nothing in this submission is confidential.

Summary of Submission

Evonik Peroxide Limited (Evonik) would like to thank the Ministry for the Environment for the opportunity to make this submission on the Reforming the New Zealand Emissions Trading Scheme: Proposed Settings consultation document.

Evonik supports the overall reform of the NZ ETS to ensure that it contributes to New Zealand meeting its international commitments.

We are however concerned about the potential economic and social impacts that may result from the proposed settings in their current form.

Moving too fast and with high carbon prices may drive significant negative economic impacts ahead of New Zealand's abatement potential being realised through cost effective technology and afforestation.

Company Overview

To provide the context to our submission points please find below a brief overview of our Company and the uses of our hydrogen peroxide products.

Evonik Peroxide Limited (Evonik) is a wholly owned subsidiary of Evonik Industries (www.evonik.com):

- Evonik Industries is an industrial group from Germany which is a global leader in specialty chemicals.
- Evonik Industries is convinced that corporate responsibility is one of the prerequisites for success in the long run. This flows through to company sustainability strategies and emissions reduction targets.

In New Zealand Evonik owns and operates New Zealand's only hydrogen peroxide manufacturing facility, located in Morrinsville:

- The manufacture of hydrogen peroxide is energy intensive and therefore emissions intensive.
- The hydrogen peroxide product is used domestically in a wide range of applications as shown in Table 1 below. It is also exported to Australia.

Table 1 - Common Applications of our Hydrogen Peroxide Products

Industry	Application
Pulp and paper	Bleaching wood pulp
Drinking and wastewater treatment	An oxygen additive
Packaging	Aseptic packaging of milk and fruit juice
Textile bleaching	Bleaching of cotton fabrics
Wool scouring	Bleaching of wool
Mining	Detoxification of cyanide tailings

- Evonik faces competition from producers located in Australia, China, Indonesia, Korea, Thailand and Europe. The manufacture of hydrogen peroxide is therefore "trade exposed".

Evonik Peroxide Limited's Exposure to the NZ ETS

Evonik's operations are directly impacted by the NZ ETS:

- The manufacture of Hydrogen Peroxide is an Emissions Intense Trade Exposed (EITE) activity, the primary inputs being natural gas and electricity.
- Evonik's operations are exposed to NZ ETS costs passed through by energy suppliers and second round impacts including freight costs and inflationary pressure.
- Evonik's operations are also dependent on the competitive viability of its larger customers, the pulp and paper industry of New Zealand.

New Zealand's climate change policy is therefore of critical importance for longer term investment decisions.

Any change in policy parameters that leads to an increase in domestic climate policy related costs which are not borne by our competitors is of significant concern to Evonik.

Detailed Submission Points

Our submission follows the structured questions in the consultation document.

Q1. Do you agree with the proposal to set a provisional emissions budget of 354 Mt CO2-e for the 2021 –25 period? If not, why not?

- **Please include your views on:**
  - **using a straight-line approach towards the 2050 target**
  - **the considerations that were included in proposing the provisional emissions budget.**

Evonik does not support the provisional emissions budget proposed. A more relaxed non-linear budget is recommended:

- The consultation workshop presentation highlighted that officials have already concluded that a linear reduction in emissions is unlikely[1] (refer slide 19). Evonik agrees that a straight-line approach ignores the lag / inertia effect of project / policy implementation timing:
- The provisional budget setting is also too reliant on unproven/not yet implemented additional policy measures. Many of the complementary measures listed are yet to be approved or implemented and if they come to fruition will take time to scale up.
- The focus on avoiding future costs ignores the likely reduction in the cost of technologies over time e.g. the rapidly falling cost of renewables generation, EVs, H2 electrolysis, battery storage etc. In many cases it may be better to wait until technology is more mature, enabling lower cost and more effective abatement.
- For the industry sector, Evonik suggests that the abatement potential tabled Is overstated:
  - In the Marginal Abatement Cost Curve analysis for the industry sector there appears to be significant errors in the assumption base and materiality of the abatement opportunity identified. Industry should be contacted to validate MACC datasets before any reliance is placed on them for establishing budgets.
  - Since the release of the consultation paper a wide review of the industrial allocation settings has been signalled through the release of a cabinet paper. This has created significant investment uncertainty, with the risk that EITE firms can no longer rely on the carbon price signal when assessing projects as the allocative baseline or level of assistance may be retrospectively reduced.

Q2. Do you support the decisions made regarding the technical volume adjustment decisions? If not, why not?

The approach documented seems logical but Evonik is not qualified to review the decisions taken.

[1] Provisional emissions budget and proposed NZ ETS settings Consultation Meetings slides, p19

Q3.	**Are there other adjustments that need to be considered?** Refer Q2.
Q4.	**Do you agree with the proposal to address the NZ ETS unit stockpile by reducing the annual volume of NZUs available for auction? If not, why not?** No. Evonik is concerned that insufficient analysis has been carried out: • The classification of participants lacks detail. Specifically, Evonik is an EITE firm with no direct surrender obligation but we do have contractual obligations to transfer units to upstream point of obligation energy suppliers. Where do our units (which have a liability) sit? • With the full surrender obligation only being introduced in 2019 and with the NZU price undergoing a rapid escalation in recent years, market dynamics have not yet matured, • In a rising C-price market as signalled by recent legislative changes, it would be rational for entities to hold units for financial gain. The withholding of auction volumes risks strengthening market return signals and ultimately could cause a market failure through inadequate unit supply.
Q5.	**Do you agree with 27 million NZUs being removed from auction volume between 2021-25? If not, why not?** No, refer Q4. The proposal to withhold 27 million NZU units is also unsupported by any clear analysis of: • carbon price elasticity analysis against different supply volume options. • economic impact assessment. • participant trading strategy intentions.
Q6.	**Do you agree with the steps and calculations taken to reach the proposed annual auction volumes?** Yes, but the removal of units to reduce the stockpile should not be included in the calculation.
Q7.	**Do you support the proposal to auction 80 million NZUs over the 2021-25 period plus 2 million NZUs for auctioning trial in 2020? If not, why not? Please include your views on the process for adjusting auction volumes.** No. Evonik views the budget to be too stringent (refer Q1) and the stockpile adjustments are unwarranted (refer Q4 & Q5). The proposed auction volume of 80 million NZUs requites amendment. The provision of 2 million (or more) NZUs for "pilot auctions" in 2020 is fully supported.
Q8.	**Do you agree with the proposal to set an auction reserve price floor at $20 for 2020-25? If not, why not?** The proposal to set an auction reserve price floor is supported, However Evonik cannot endorse the specific value of $20 as it is not supported by adequate published analysis.

Q9. Do you agree with the proposal to increase the fixed price option to $35 for obligations arising from activities over 2020?

Evonik supports the extension of the fixed price option (FPO) for the 2020 compliance year but notes that this conflicts with the Emissions Trading Reform Bill, which as drafted requires the FPO to be removed once auctions commence. It is recommended that the Ministry publishes clear guidance on how this conflict will be resolved.

The FPO level of $35 is understood to have been arbitrarily set.

- Officials indicate that it has been chosen to be halfway between the $20 floor and the $50 ceiling trigger for the cost containment reserve, both of which are themselves arbitrarily set.
- The lack of adequate analysis behind the 40% increase FPO is a significant omission.
  - The release of the proposed settings consultation document and particularly the increase in the FPO, triggered an immediate rise in NZU prices which had a flow on economic impact to households and industry.
  - Evonik understands that the increased FPO remains a proposal but a regulatory impact analysis of this should be made available, including and assessment of the additional abatement expected through the 40% FPO price increase.

Q10. Do you agree with the proposal to set the price ceiling trigger of the cost containment reserve at $50 for the 2020–25 period? If not, why not?

The inclusion of a cost containment reserve is supported, but the ceiling trigger level is not adequately supported by analysis.

Q11. Do you agree with the proposed annual cost containment reserve volumes to be released if the price ceiling trigger is hit? If not, why not?

No, Evonik does not support the proposed annual cost containment reserve volumes:

- Evonik is alarmed by the Climate Change Minister's comments that the cost containment reserve may not be available if New Zealand cannot access international markets.[2]
- A restricted or unavailable cost containment reserve risks creating a run on the NZU price and market failure.
- The proposed penalty for not surrendering a unit being increased to three times the carbon price (refer ETS Reform Bill) compounds the risks of serious economic impact as participants face having to secure units at any cost or disruptive cutting of sales/production with resultant knock on impacts to the economy.

Evonik recommends that further analysis of potential market failure is carried out and put out for wide review. If the risk is material, additional NZU supply options should be introduced.

[2] https://www.stuff.co.nz/business/119067433/climate-change-minister-james-shaw-expects-carbon-credit-numbers-to-shock

Q12. Do you agree with the proposed approach for release of NZ ETS settings information? If not, why not? Yes, the proposed approach for release of NZ ETS settings information is welcomed. However, Evonik is uncertain as to which government agency should be releasing the data is appropriate: • Climate Change Commission – the independent authority • Environmental Protection Authority – the regulator • Ministry for the Environment – the policy designers	
Q13. Do you have any further comments? Evonik appreciates the efforts of the Ministry for the Environment NZ ETS policy team on this complex policy challenge.	

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