



Submission on:

**New Zealand Emissions Trading
Scheme Review 2015/16
- Other issues**

From

Ballance Agri-Nutrients Limited

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SUBMITTER DETAILS

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COMMERCIAL SENSITIVITY

Nothing in this submission is commercially sensitive.

Introduction

Ballance Agri-Nutrients Limited (hereafter referred to as 'Ballance') would like to thank the Ministry for the Environment for the opportunity to make this submission on the New Zealand Emissions Trading Scheme Review 2015/16.

Company Overview

Ballance is a farmer-owned co-operative with over 18,000 shareholders and approximately 800 staff throughout New Zealand. We own and operate super-phosphate manufacturing plants located in Tauranga and Invercargill, as well as New Zealand's only ammonia-urea manufacturing plant located at Kapuni, South Taranaki. The Company also owns and operates 'SuperAir', an agricultural aviation company; 'SealesWinslow', a high-performance compound feed manufacturer; and 'AgHub', which provides on-line farm information and management tools. Ballance has a network of fertiliser storage and dispatch facilities across the country.

Ballance places a strong emphasis on delivering value to its shareholders and on the use of the best science to inform sustainable nutrient management.

Ballance's Exposure to the NZ Emissions Trading Scheme

Ballance's operations are directly impacted by the New Zealand Emissions Trading Scheme (NZ ETS):

- The Kapuni Urea manufacturing facility is an Emissions Intense Trade Exposed (EITE) industry (within the SEIP Sector), competing against imported Urea;
- As a manufacturer and importer of Urea, Ballance is a mandatory participant (within the Ag Sector), for synthetic fertiliser containing nitrogen.
- All of Ballance's operations are exposed to NZ ETS costs passed through by energy suppliers and second round impacts including freight costs and inflationary pressure.

Any change in policy that leads to an increase in ETS related costs is therefore a significant concern to Ballance.

Ballance's Engagement in Climate Change Policy Development

Ballance takes an active role in the development of climate change policy, dating from the original industry voluntary agreements of the late 1990's through to the current ETS.

Submission Points

In this submission we provide comments on **Other Issues** (Questions 9 to 27). We have already made a submission on 'Context and drivers for the review' and 'Priority issues'.

Submission Summary

Question 9

Yes, Ballance considers the future cost of emissions in our business planning.

Question 10

Reduced politicisation of NZ ETS scheme settings through greater cross-party agreement would improve our ability to take into account the future cost of emissions.

Question 11

Free allocation rates can start to be reduced only when the risk of trade exposure has materially reduced.

Question 12

Increased certainty of allocation criteria through a cross-party agreement would reduce the sovereign risk factor of investing in New Zealand.

Question 16

Any restriction on how many units can be surrendered should be driven by the Government's need to avoid over-recovery of international units.

Question 17

In the absence of international unit access, auctioning is required to ensure a liquid and functioning NZ ETS.

Question 18

The purpose of an auctioning function in the NZ ETS would be to both align supply in the NZ ETS more closely with our international target and actively manage NZU prices.

Question 19

Auctioning of NZUs should supplement other sources of unit supply.

Question 20

There is currently a moderate impact that requires a range of price scenarios to be used in evaluating projects, as well as, material changes in cash-flow.

Question 21

Yes, the NZ market is a small market that is very susceptible to any unit supply-demand imbalance.

Question 22

The fixed price option should be retained to provide a price ceiling.

Question 23

The government should consider (when managing price stability) the durability of the ETS and the domestic unit supply-demand imbalance.

[Question 24](#)

Yes

[Question 25](#)

Key NZ ETS information, guidance, and compliance activities are scattered across multiple Government websites.

[Question 26](#)

The ETS drives carbon reduction, but there is no market incentive to research alternative opportunities.

[Question 27](#)

The wider perspective on emission reduction policy is not transparent, so this risk results in limited capital investments.

Submission Details

Question 1 to 8 – Refer to our 19 February 2016 submission.

Question 9 - Do you consider the future cost of emissions in your business planning?

Yes, the future costs of emissions are explicitly taken into account during business planning. We utilise:

- Inclusion of forecast Carbon-prices in budgets
- Carbon-price scenarios to evaluate robustness of investments
- Comparison of ETS costs in NZ and competitor countries in investment location decisions

Operationally, the introduction of the NZ ETS has helped refocus Ballance's efforts to improve energy efficiency and reduce greenhouse gas emissions from its fertiliser manufacture and distribution activities.

Regarding the use of carbon price scenarios Ballance is currently evaluating the redevelopment of its Kapuni urea plant:

- The plant was opened in 1982 as part of Prime Minister Rob Muldoon's 'Think Big' project for New Zealand to boost its infrastructure and decrease its reliance on imports
- Imports still account for more than half of the Urea used in New Zealand
- Ballance called for tenders earlier this year for redevelopment which will both increase capacity and reduce the emissions intensity, requiring an investment of several hundred million dollars

Question 10 - What would improve your ability to take into account the future cost of emissions in your business planning?

Our ability to take into account the future cost of emissions would improve with:

- Greater certainty of NZ ETS scheme settings
- Improved market information
- Reduced politicisation of NZ ETS scheme settings through greater cross-party agreement

Significant business decisions are typically evaluated on an NPV basis over 10-15 year periods. Politicisation of NZ ETS scheme makes it difficult to commit high levels of new capital when a completely new political environment is only ever three years away.

Question 11 - Under what conditions should free allocation rates start to be reduced after 2020?

Free allocation rates should start to be reduced only when the risk of trade exposure has materially reduced. This needs to be assessed on an activity by activity basis and not be a politicised decision that blankets all EITE activities. For each activity the assessment of trade competitor jurisdictions should take into account:

- The level of Carbon-pricing, through trading or a carbon tax
- The level of Allocation/subsidy
- Other support mechanisms including non-tariff barriers

Phase out of allocation should only commence when a material proportion of competitor trade incorporates an auditable and internationally acceptable carbon price in-line with the New Zealand.

Question 12 - What impact would it have on your investment decisions over the next few years if there was a clear pathway or criteria for phasing out of free allocation after 2020?

Increased certainty of allocation criteria through a cross-party agreement would reduce the sovereign risk factor of investing in New Zealand.

Question 13 to 15 – Ballance has no views on these forestry related questions

Question 16 - If international units are eligible for NZ ETS compliance in the 2020s, should any of the following restrictions be placed on their use?

Ballance agrees there should be restrictions on the quality of international units that can be sourced for the following reasons:

- Environmental integrity and measurement reporting and verification (MRV) standards are important to maintain the integrity of the NZ ETS
- Political maturity of any linked scheme /projects mechanism source(s) should be carefully considered. The small size of NZ ETS market will make it very vulnerable to larger source market volatility

Any restriction on how many units can be surrendered should be driven by the Government's need to avoid over-recovery of international units. Over recovery poses the following issues:

- Once surrendered, the government risks undermining the environmental integrity of the NZ ETS should it resell surplus international units into the international market
- Carryover of excess international units to future obligation periods may also undermine the environmental integrity of the scheme

If linking with another scheme then the mutual recognition of emission units should be considered (including forestry NZUs). Environmental integrity is a two way street and mutual recognition of emission units would be an endorsement of the NZ ETS.

Question 17 - Should auctioning be introduced in the NZ ETS?

Yes. In the absence of international unit access, auctioning is required in the next two to three years to ensure a liquid and functioning NZ ETS. Ballance's advisors have made a compelling argument that the Ministry for the Environment's assumption that approximately 140 million banked NZUs being made available is unsound. It is very likely that a significant portion of these units will be withheld for the period post 2020.

It would be best if auctioning is phased in with pilot auctions and subsequent full auctioning prior to the NZ ETS becoming reliant on the fall back of the Fixed Price Option for NZU supply. This requires urgent action. The key auction settings need to be established as a priority and signaled in order to provide market certainty.

Question 18 - What should be the role or purpose of an auctioning function in the NZ ETS, if one were introduced?

The purpose of an auctioning function in the NZ ETS would be to align supply in the NZ ETS more closely with our international target and potentially actively manage NZU prices.

Post 2020, auctioning would help avoid too many international units being purchased and surrendered by participants. This problem eventuated in the period 2010-14 with a surplus of international units surrendered. It would have been better for revenue to remain in NZ rather than be used to purchase excess international units.

Auctioning would help mitigate the risk of under supply of NZUs with resultant reliance on the Fixed Price Option, or if no Fixed Price Option is available, the risk that NZU prices become politically unacceptably high leading to intervention. In both cases the longer term NZ ETS policy would be undermined.

Question 19 - How should auctioned NZUs relate to other sources of unit supply in the NZ ETS, especially NZUs generated through forestry removals and/or international units?

Auctioning of NZUs should supplement other sources of unit supply. It is possible that international unit trading may only be available at the sovereign level in the early 2020s. In such a situation the Government could purchase such units and auction domestic units matching these purchases through the NZ ETS.

Question 20 - What impact has carbon price volatility in the NZ ETS had on your business?

There is currently a moderate impact that requires a range of price scenarios to be used in evaluating projects, as well as, material changes in cash-flow. Ballance expects the scheme to be volatile and not conducive to business confidence. A recent example is the recent sharp rise in NZU price, in response to strong signals from Government that the scheme will move to a full surrender obligation, but without details on timing or unit supply.

Question 21 - Do you think measures should be in place to manage price stability?

Yes, the NZ market is a small market that is very susceptible to any unit supply-demand imbalance.

Question 22 - What do you consider are important factors for managing price stability?

The fixed price option should be retained to provide a price ceiling until robust experience with NZU auctioning has been developed.

Question 23 - What should the Government consider when managing price stability?

Ballance recommends that the Government should consider:

- The durability of the NZ ETS from a political acceptability viewpoint – this will be undermined by significant price shocks
- The domestic unit supply-demand balance
- Should access to international markets be re-established the risk of price controls creating unit arbitrage opportunities would need to be carefully evaluated to avoid unwanted outcomes

Question 24 - Are you aware of ways the administrative efficiency of the NZ ETS could be improved?

Yes.

Question 25 - Can you provide further information to support your answer?

Ballance recommends a review of the current arrangement where key NZ ETS information, guidance, and compliance activities are scattered across multiple Government websites. We also recommend that a review of market information access be made. In an NZU only market it is even more important that data on NZ ETS supply and demand should be more freely available.

Question 26 - Are there any barriers or market failures that will prevent the efficient uptake of opportunities and technologies for reducing emissions?

Perversely, water quality is currently a barrier to reducing greenhouse emissions. Water quality is the immediate issue and scarce resources are being diverted towards water and away from greenhouse gas research or mitigation.

The ETS drives carbon reduction, but there is no market incentive to research alternative opportunities for carbon sequestration (e.g., riparian planting, biochar). As a reflection of the NZ ETS design, Ballance undertakes limited research into greenhouse gas emission reductions through the agriculture sector. This is because the current scheme design provides no market incentive to invest in the significant opportunities of carbon soil sinks or nitrous oxide reduction through inhibitors.

Question 27 – If so, is there a role for the Government in addressing these barriers or market failures and how should it do this?

The ETS is only one tool within the government's policy tool box (e.g., incentives for electric vehicles or renewable energy, public funding to retire agricultural land). The wider perspective on emission reduction policy is not transparent, so this risk results in limited capital investments in technologies to either reduce or sequester carbon emissions.