

SUBMISSION BY O-I NEW ZEALAND

Topics for NZ ETS Review 2015/2016 consultation

About the consultation

The Government is reviewing the New Zealand Emissions Trading Scheme (NZ ETS) to assess how it should evolve to support New Zealand in meeting future emissions reduction targets and its ongoing transition to a low emissions economy. This follows the announcement by the Government in July this year that New Zealand's post 2020 target is to reduce greenhouse gas emissions to 30 per cent below 2005 levels by 2030.

The Ministry for the Environment is leading the consultation and welcomes your feedback on how the NZ ETS is working and how it might work better in the future.

The review will focus on:

- some transitional measures introduced to moderate the impacts of the NZ ETS
- what is required for the NZ ETS to evolve with changing circumstances including future targets
- operational and technical improvements.

Discussion document

For more information about the consultation, read our [discussion document](#). It sets out the issues on which the Government is consulting, the objective and drivers for the review. It also contains the terms of reference for the review.

See the following two technical notes for information on specific issues relating to forestry and on operational matters that could be improved. Submissions on these matters close at 5pm on 30 April 2016.

- [Operational matters technical note](#)
- [Forestry technical note](#)

The following three technical notes were made available to support submissions on the NZ ETS review's priority issues. Submissions on priority issues are now closed.

- [The New Zealand Emissions Trading Scheme evaluation report 2016](#)
- [Economic impacts of removing NZ ETS transitional measures](#)
- [Afforestation responses to carbon price changes and market certainties.](#)

Closing dates for submissions

- Submissions on priority issues closed at 5pm on 19 February 2016
- Submissions on other review matters close at 5pm on 30 April 2016.

Publishing and releasing submissions

All or part of any written submission (including names of submitters), may be published on the Ministry for the Environment's website www.mfe.govt.nz. Unless you clearly specify otherwise in your submission, we will consider that you have consented to website posting of both your submission and your name.

Contents of submissions may be released to the public under the Official Information Act 1982 following requests to the Ministry for the Environment (including via email). Please advise if you have any objection to the release of any information contained in a submission and, in particular, which part(s) you consider should be withheld, together with the reason(s) for withholding the information. We will take into account all such objections when responding to requests for copies of, and information on, submissions to this consultation under the Official Information Act.

The Privacy Act 1993 applies certain principles about the collection, use and disclosure of information about individuals by various agencies, including the Ministry for the Environment. It governs access by individuals to information about themselves held by agencies. Any personal information you supply to the Ministry in the course of making a submission will be used by the Ministry only in relation to the matters covered by this consultation. Please clearly indicate in your submission if you do not wish your name to be included in any summary of submissions that the Ministry may publish.

Contact for queries

Please direct any queries to:

Phone: +64 4 4397400

Email: nzetsreview@mfe.govt.nz

Postal: NZ ETS Review Consultation, Ministry for the Environment, PO Box 10362, Wellington 6143

Questions to guide your feedback

The questions below are a guide only, and all comments on topics are welcome. To ensure your point of view is clearly understood, please explain your rationale.

Contact information

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|---------------------------------|---|
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Submission Form

**** Please note: Items in square brackets indicate information that O-I considers to be commercially sensitive. O-I requests that this information be withheld from any publicly released copies of its submission ****

Discussion Document

Context and drivers for the review

1. Do you agree with the drivers for the review?

Yes

No

Unsure

2. What other factors should the Government be considering in this NZ ETS review?

O-I particularly supports the objective of the ETS review to “increase certainty about future policy settings.” Maximising certainty regarding ETS settings, and signalling any changes clearly and with adequate time to allow businesses to prepare for the changes, is critical to enable business to properly factor the future cost of emissions into operational and investment decisions.

Certainty and advance warning are necessary to ensure that New Zealand businesses can remain competitive. O-I considers itself a “good corporate citizen”, as evidenced by the role it plays in recycling glass waste in New Zealand. O-I’s operation is an example of world best practice in terms of energy efficiency.

Companies such as O-I compete against imports, whose manufacturers do not face constraints such as emissions trading. If O-I’s competitiveness is undermined, there will be “carbon leakage” as glass demand will shift to imports from countries that do not impose GHG reduction schemes, in regions such as the Middle East and Asia. Glass manufacturers in these regions are less energy efficient, or use less recycled content, than O-I. On a global scale, GHG emissions will therefore increase through greater (less efficient) offshore production and more emissions from shipping.

Political risk relating to the ETS is a significant problem for business. The risk of major changes to ETS settings (or potentially even abandonment of the ETS entirely) following a future change of government creates significant uncertainty for business and erodes business confidence in the ETS. If New Zealand is committed to a carbon-constrained future, then political parties should strive for cross-party agreement on core elements of climate change policy (including core elements of the ETS).

O-I’s view is that, in addition to the four key drivers for the review identified in the discussion document, the Government should also be mindful of the need to avoid making too many major changes to the ETS at once. Businesses will need time to adjust to new ETS settings (such as moving to full surrender obligations), so O-I considers that between now and 2020 the Government should aim to minimise the number of changes to the ETS settings, with a focus on providing as much certainty and advance warning about intended future changes as possible. After 2020, further changes (such as any reduction in free allocation of units) could then be phased in over an appropriate period of time.

Moving to full surrender obligations – submissions on these priority issues closed on 19 February 2016.

Managing the costs of moving to full surrender obligations– submissions on these priority issues closed on 19 February 2016.

Other issues: business responses to the NZ ETS

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

Yes

If yes, how do you do this?

Any volatility in the cost of participation in the New Zealand ETS has a major impact on O-I's business decisions. O-I's New Zealand operation is a subsidiary of a global recycling and manufacturing business, which could easily choose to locate its plants elsewhere. A volatile New Zealand business environment will reduce the confidence of O-I's international parent in investing capital and resources into the New Zealand operation. Accordingly, any changes must be introduced gradually, to ensure that O-I can plan well in advance for any changes resulting in more volatility or increased costs.

O-I emphasises again that it must compete with imports from countries where businesses do not have to factor in similar constraints. New Zealand already has high costs per tonne of output. While fluctuations in the market are inevitable, the government should also ensure that domestic businesses can compete on as level a footing as possible with overseas manufacturers.

No

If no, please explain your answer?

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

Certainty about future policy settings and price stability would improve O-I's ability to take into account the future cost of emissions. O-I accepts that the ETS will change over time. However, the government must clearly signal any changes in advance, and with sufficient warning so that businesses can plan for the changes. In particular, ETS participants will need time to prepare for any changes that are likely to materially impact on the level of its emissions liability and the price of emission units. See also O-I's response to Question 9 above.

Other issues: protecting competitiveness through free allocation

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

Free allocation critical for protecting O-I's operations in New Zealand

O-I is an Emissions Intensive, Trade Exposed (EITE) business. Accordingly, the free allocation regime is critical to the viability of O-I's operation in New Zealand. Put simply, without sufficient free allocation support, ETS costs could result in O-I's New Zealand manufacturing operations closing (and moving overseas).

O-I's trade exposure stems from the fact that it must compete with overseas glass manufacturers, in regions such as the Middle East and Asia, whose processes are much less energy efficient than O-I's New Zealand operation. [REDACTED]

In pure economic terms, many of these overseas manufacturers are at an advantage over O-I, as New Zealand's legislative environment imposes costs that are not present elsewhere. O-I is not suggesting that New Zealand's regulatory environment should be relaxed. Nonetheless, the New Zealand government must acknowledge that it imposes high standards on New Zealand enterprises and, in consequence, should offer appropriate support to assist businesses to meet those standards.

The government should remain mindful of the purpose of the ETS – that is, to reduce GHG emissions. GHG emissions are a global concern, and should be assessed on a global scale. If the ETS forces environmentally conscious New Zealand businesses out of the market, the likely outcome is that those operations will simply be transferred offshore to less well-regulated jurisdictions. Consequently, the global GHG emissions profile will increase.

O-I acknowledges that it carries out a significant industrial operation. However, O-I notes that there are wider benefits to "NZ Inc" of retaining an on-shore glass recycling and manufacturing plant. O-I directly employs approximately 260 people at its plant in Penrose. O-I recycles approximately 120,000 tonnes of crushed glass (*cullet*) each year – waste that would otherwise go to landfill or have to be shipped offshore to be recycled. A domestic glass recycling plant is a crucial component of New Zealand's waste management system, and ensures that glass can be efficiently recycled on-shore.

More widely, O-I's operation has indirect benefits for other domestic industries such as New Zealand's wineries. New Zealand's premium wine industry depends on bottles made from recycled glass. The biggest single source of CO₂ emissions (roughly a third) in getting wine to market is the manufacture of the bottles. Using recycled glass in wine production is more CO₂ efficient, which is a valuable "marketing point" for wineries that export to carbon sensitive overseas markets. As this example demonstrates, other New Zealand businesses benefit from the ability to source packaging from a sustainable domestic glass producer.

Need to retain existing free allocation until at least 2020

O-I supports the Government's stated intention of keeping the free allocation regime in place until at least 2020. It is critical that O-I retains its full existing 60 percent level of free allocation assistance (based on the classification of the production of glass containers as a moderately emissions-intensive activity) until at least 2020. Increasing free allocation proportionately with any removal or phasing out of the one-for-two surrender obligation is essential in order to continue to protect the competitiveness of New Zealand EITE businesses such as O-I. If the ETS moves to full surrender obligations but has proportionately the same level of free allocation as is currently the case, the increased cost of buying twice as many units (to cover the free allocation 'shortfall') will still be a major financial incentive for O-I to mitigate its emissions (if at all possible).

Reduction in free allocation after 2020

The discussion document refers to the potential reduction in the rates of free allocation after 2020. O-I seeks clarity as to what the post-2020 free allocation support to EITE businesses would look like. Is the Government intending to remove the temporary suspension of the phase-out rates of free allocation (that is, activate the 0.01 phase out rate for EITE industrial activities in section 81 of the Climate Change Response Act 2002), or is something else proposed? Clarity and sufficient advance warning of the nature of any post-2020 reduction in free allocation rates are essential.

If the Government opts to impose a “sinking lid” policy on free allocation of units after 2020, O-I considers the following conditions are essential:

- The Government should clearly flag the reductions now, and explain how they will operate, when they will come in to effect, and how quickly the free allocation will decrease;
- The Government should establish alternative policy measures to ensure that EITE operators such as O-I will continue to remain viable as businesses in New Zealand as levels of free allocation reduce; and
- Continuing recognition of O-I as an EITE business. Post-2020, O-I anticipates that its New Zealand operations will remain highly trade exposed, and the production of glass containers is inevitably an emissions intensive activity.

Subject to the above conditions, O-I would accept a gradual (0.01 per year) decrease in the level of free allocation assistance after 2020.

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?

If the government phases out free allocation after 2020, O-I considers that a clear pathway is necessary to allow O-I to make informed investment decisions. In particular, a detailed programme of changes to the ETS would give O-I’s international parent confidence in its New Zealand investments. Please see O-I’s responses to Question 9, 20 and 23 for details about the impact of increasing costs on O-I’s New Zealand operation.

Other issues: managing unit supply – international units

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

a) restrictions on where units can be sourced from (location of and/or types of projects)



b) restrictions on how many units can be surrendered



c) others

Please explain your answer.

O-I considers that the environmental integrity of eligible international units is critical, so restrictions on the source of eligible international units may be needed. The Government should work with business to identify the markets that provide credible units.

O-I believes that there should be restrictions on the quantity of international units to help ensure NZ is a genuine contributor to domestic emission reductions.

If international units are to be eligible for NZ ETS compliance after 2020, O-I considers that a phased approach is appropriate – that is, a gradual re-introduction of access to international units in order to support market predictability and price stability. O-I considers that international units have been introduced too quickly in the past, which has destabilised the market for emissions units. As with any changes to the ETS, O-I would prefer a more gradual approach to the introduction of international units.

Other issues: managing unit supply – auctioning

17. Should auctioning be introduced in the NZ ETS?

Yes

No

Unsure

If yes, when?

a) in the next two to three years

b) within five years (before 2020)

c) after five years (post 2020).

O-I opposes auctioning in the ETS – see response to Question 18 below.

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

a) to align supply in the NZ ETS more closely with our international target

b) to more actively manage NZU prices

c) other

Please explain your answer.

O-I does not support an auctioning mechanism at this stage. O-I submits that auctioning will add further complexity to the New Zealand ETS. ETS participants already need to adapt to the recent removal of access to international units, and are likely to also need to adapt to a number of potential changes to the scheme, including a move to full surrender obligations. Adding an auctioning mechanism at this stage would add complexity by requiring participants to manage another process and make decisions on whether and how to participate in auctions. Increasing market complexity increases costs for business – particularly for ETS participants like O-I who are not experienced and sophisticated carbon market traders.

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?

O-I opposes auctioning in the ETS – see response to Question 18.

Other issues: managing price stability

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

a) minor

b) moderate

c) significant.

Please explain your answer.

Volatility makes it difficult for O-I to forecast its operating costs. In turn, it becomes more difficult for O-I's New Zealand operation to attract investment from its international parent and thus remain viable. The government must recognise the global nature of many of the businesses that operate in New Zealand. These businesses must compete for investment with overseas economies that have lower compliance costs, and rapidly growing domestic markets. These factors automatically make overseas economies a more attractive destination for investment. Added volatility in the New Zealand business environment will compound the difficulties that New Zealand subsidiaries face in maintaining investments from their international parent companies.

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

Yes

No

Unsure

Please explain your answer

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

a) upper price limits (eg, fixed price option, or a price ceiling implemented through an auctioning mechanism)

b) lower price limits (eg, price floor)

c) other

Please explain your answer

O-I supports maintaining the current fixed price option until at least 2020. O-I considers the fixed price option remains important to protect against price shocks, and in particular to protect business competitiveness. If the fixed price option is removed post-2020, the Government must signal this change as early as possible, and inform ETS participants of how the ETS will function after the removal of the price cap.

O-I opposes a price floor for emissions units, which it considers would add a further, unwarranted layer of complexity to the ETS. Provided unit supply is appropriately managed, a price floor should not be necessary in order to achieve the ETS' aims of supporting and encouraging global efforts to reduce GHG emissions by assisting New Zealand to meet its international obligations and by reducing New Zealand's net emissions of those gases to below business-as-usual levels.

23. What should the Government consider when managing price stability?

The government must consider the need for New Zealand businesses to remain competitive against imports. Any increases in the cost of participation in the ETS will have unintended outcomes, if those cost increases result in local manufacturers being forced out of business. In O-I's case, those consequences would include the loss of a domestic manufacturer and associated employment, a reduction in New Zealand's on-shore recycling capacity, and flow-on impacts to other industries such as wine. Price stability will assist O-I to ensure that its New Zealand operation remains viable.

Other issues: operational and technical matters

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

Yes

No

Unsure

25. Can you provide further information to support your answer?

We would be interested in comments on:

- a) complexities involved in NZ ETS participation
- b) penalties for breaching NZ ETS obligations
- c) any technical or operational changes that could be made to the NZ ETS to improve efficiency.

Other issues: addressing barriers to the uptake of low emissions technologies

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

O-I agrees with the discussion document's point that "the NZ ETS alone will not drive New Zealand towards a low emissions economy".¹ Effective waste management and recycling processes are an example of an additional policy measure that will assist New Zealand in the transition to a sustainable, low-carbon economy.

As a producer of glass containers, O-I's ability to reduce its GHG emissions is intrinsically linked to waste management and recycling policies and systems. In essence, the more good-quality recycled glass O-I can source and re-use in its manufacturing of glass containers, the lower O-I's GHG emissions will be. Use of cullet in the manufacture of new glass containers reduces carbon emissions because:

- Creating glass from raw materials (soda and lime) involves a chemical reaction that releases GHGs. This chemical reaction does not however occur when cullet is re-melted.
- Cullet melts at a lower temperature than the virgin raw materials used in new glass. Accordingly, the higher the cullet content, the less energy is needed to manufacture new glass containers, which directly relates to the level of CO₂ emitted in the manufacturing process.

Use of cullet in the production of new glass containers also has broader environmental benefits, such as waste minimisation and reducing the quantity of other raw materials that must be extracted and processed.

¹ *New Zealand Emissions Trading Scheme Review 2015/16: Discussion Document and Call for Written Submissions* (Ministry for the Environment, 24 November 2015) at page 24.

The major problem currently preventing O-I from further reducing its GHG emissions is access to good quality cullet. The quantity of glass able to be recycled depends in turn on effective recycling policies, particularly at local government level. O-I commends a number of local authorities that have rolled out efficient recycling policies that are easy for households to follow.

By contrast, other local authorities have prioritised short-term costs over long-term waste management strategies that will improve recycling practices and ultimately reduce emissions. In Auckland and Christchurch – New Zealand’s largest centres – recycled materials are “co-mingled” at the collection point, meaning all recycling is put into one bin at the collection point.

Co-mingling makes it much more difficult to isolate glass at the collection point (where it is cheapest to do so) and recover that glass for colour sorting and recycling. Additionally, in a combined recycling bin, glass shatters and becomes embedded in paper and cardboard, which makes those recyclable materials impossible for local cardboard manufacturers to reuse.

Co-mingling therefore diminishes the amount of cullet that is available to recycle, with as much as 40-50 percent of the glass not able to be used. This glass will ultimately end up in landfill or used as aggregate substitute under new roads. Reduced access to cullet in turn affects O-I’s ability to reduce its GHG emissions.

Conversely, using a separate bin to collect glass means that 98 percent of the glass collected can be colour sorted and turned into bottles or jars.

The way for O-I to most efficiently reduce its GHG emissions is to have ready access to good quality cullet. Local government recycling collection and waste minimisation therefore have a direct impact on O-I’s emissions, as well as wider environmental effects. In tandem with the ETS review, the New Zealand government should therefore seriously investigate and implement more effective methods to improve recycling and waste management practices nationwide.

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

O-I considers there is a role for central government in improving national waste management strategies. Central government has tools available to provide national direction through waste minimisation legislation and policies. Such national direction could include more effective recycling policies, and measures to avoid co-mingling of recyclable materials.

In particular, central government should consider directive measures to prompt local government to move towards rubbish collection models that are genuinely focused on recycling and sustainability. Such measures could include:

- Performance standards/targets for recovery of recyclable materials (that is, setting a percentage target for glass, paper, cardboard and other materials that must be recovered from the waste stream);
- Performance standards/targets for reductions in the level of waste sent to landfill;
- Regulations establishing how recycling is to be collected and processed; and
- Funding support for local authorities to reform their recycling collection systems.

Any other comments related to issues set out in the discussion document

28. Please comment here

Although the ETS puts a price on carbon by requiring emitters to purchase emission units, it does not currently act as a source of funds to drive initiatives to reduce GHG emissions. Presently, the ETS imposes an extra cost on businesses, with the ultimate policy objective of supporting and encouraging global efforts to reduce GHG emissions. O-I sees value in investment in research and development and innovation, and would like to see the Government explore the potential for the ETS to generate some funds that could be hypothecated for investment in research and development into technologies to reduce carbon emissions, particularly in the agricultural sector.

When your submission is complete

Email your completed submission to nzetsreview@mfe.govt.nz or post to NZ ETS Review Consultation, Ministry for the Environment, PO Box 10362, Wellington 6143.

Submissions on priority issues closed at 5pm on 19 February 2016

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