

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.

Some transition measures are being given priority and have the first deadline for submissions as they may be candidates for legislative change in 2016 (see closing dates for submissions below). Refer to the discussion document for detail on the priority and other matters under review.

Technical notes on the following specific issues will be available in December or early 2016 to support submissions:

- modelling of the impacts of the priority issues outlined in the discussion document
- forestry sector matters, including accounting methodologies for post-1989 foresters
- operational and other technical matters.

To be notified of when these technical notes are available, please email nzetsreview@mfe.govt.nz.

Closing dates for submissions

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

You may make submissions on both priority issues and on the other matters. If you provide feedback on both you can do so in a single submission or separate submissions. Please note submissions on priority issues must be received by 19 February 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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Submission Form

Context and drivers for the review

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

Yes

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

There are a number of “other matters” that I am assuming will be further amplified as part of the submission due on 30 April 2016.

Moving to full surrender obligations

3. Should the NZ ETS move to a full surrender obligation for the liquid fossil fuels, industrial processes, stationary energy and waste sectors?

Yes

4. What impact will moving to full surrender obligations have on you or your business?

I am a forest owner and forestry consultant. The 1:2 subsidy was as I understood it, a temporary phasing in measure that was meant to end in 2012. Its continuation has undermined the “market based” mechanisms of the NZETS. In the case of the forestry sector it effectively halved the value of forestry credits and deferred decisions by many forest owners to sell their ETS units. The liquidity of supply of units has therefore been affected. The move to a full surrender obligation should help raise carbon prices and restore confidence in forest growing as a viable business.

I realise this is a simplistic explanation of a the ETS market which was also seriously undermined by the GFC and the availability of European units at low prices. However the important point is that we need to try to move forward and allow carbon price signals to again be an influencer of forestry investment behavior. Forest investment in new planting has seriously declined over the past 5 years, and when that is combined with the “wall of wood” that is expected to be harvested over the next 8 to 10 years, the surplus of forestry related ETS units is expected to rapidly decline by 2025.

Please include specific examples or evidence of the impacts on you or your business of:

- a) *increased carbon prices, including actions to reduce emissions and future investment decisions. Please comment on effects that may occur at carbon prices ranging from \$5 to \$50, including any evidence of actions taken previously when carbon prices were higher.*

One of my greatest concerns is whether many of the “wall of wood” forests planted in the mid 1990’s will be replanted, or the land diverted to other forms of land-use. I am assisting a number of partnership forests where discussions are already taking place on whether to replant or not following harvesting. The collapse of carbon prices (and in fact the whole irrelevancy/ failure of the ETS system) is a major part of discussions. A much higher price ((at least \$25) for NZETS units is urgently needed to prevent an acceleration in the decline in plantation forest areas.

- b) *any NZ ETS administrative or operational issues, for example the option for participants to apply for a unique emissions factor.*

There are a number of other administrative and operational issues that need careful thought when designing the NZ forestry rules post the Paris Accord. I am assuming these will be part of submissions due on 30 April 2016. However they include:

- A more enlightened treatment of the pre-1990 forests;
- A gradual phasing in of agriculture;

- The “Covec Report” and the option of “averaging” at the time of harvest;
- Repayment to the forest owners who were holding ERUs at May 2014 of the value of their ERUs, to help restore credibility and greater certainty in the ETS;
- A clarification of the auctioning system the Government introduced.

5. If full surrender obligations are applied, when should this be implemented?

a) 2016 to apply to the May 2017 surrender of units by emitters.

Outline the reasons for your answer, and include any comments on the pros and cons of applying an increased surrender obligation to a partial or a full NZ ETS reporting year.

The sooner the better, because:

- The need for more optimistic signals to the forestry sector as explained in (4) above;
- The earlier Independent Review recommended an increase of \$5/year from 2013;
- Reduce the cost on the NZ Government budget;
- Many emitters have been using the \$25 cap as a benchmark for their pricing over the past 5 years;
- Frankly emitters are already expecting the change to come.

Managing the costs of moving to full surrender obligations

6. If the NZ ETS moves to full surrender obligations, should potential price shocks be managed?

Unsure

The forestry sector requires greater certainty in how the ETS and carbon prices will move. Large price fluctuations, as have happened over the past 5 years are not in the best interests of replanting or increased plantings.

7. If potential price shocks associated with moving to full surrender obligations should be managed, how should this be done?

c) gradually move to full surrender obligation

This should start with a \$25 cap for say a two year period, but then be signal that the intention is to review it and remove it.

8. If the \$25 fixed price surrender option value should change, what should it change to and why?

The Government already has the right to set a price cap, allocates units to EITE business and can operate an auctioning system that will give it ample (probably too much) flexibility.

Other issues: business responses to the NZ ETS

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

Yes

If yes, how do you do this?

Sensitivity analysis utilising a range of short term and longer term price assumptions.

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

Historical proof that the ETS is being soundly managed for the longer term and not subject to poor knee-jerk decision making. (e.g the shock announcement for those holding ERUs at May 2014!)

Other issues: protecting competitiveness through free allocation

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

I am unsure about the magnitude and current promises to free allocation holders

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?

A clear and logical pathway for their removal will obviously be advantageous to forestry investment, but as mentioned in (11) I have not studied this area recently.

Other issues: managing unit supply - forestry

13. How does the carbon price impact your forestry investment decision-making?

In your answer, we are interested in the:

a) extent to which the NZU price impacts decisions, compared to other factors

b) impacts of the current price, and of your expectations for future prices.

Forestry investment decision making is all about the anticipated return and a careful analysis regarding the robustness of the assumptions used. We like to get a 7% to 8% IRR pre-tax. In 2011/12 when carbon prices were high, and land prices reasonable this level of return became achievable, hence the jump in new plantings through that period.

Since then, with agriculture (dairying and dairy runoffs) doubling the price of forestry land and NZUs prices becoming insignificant, it is hard to generally show more than a 2 to 3% IRR. Higher NZU prices are therefore critical to new investment, as are other measures to get a more level playing field of forestry vs agricultural investment.

14. Are there opportunities for the NZ ETS to increase incentives for forestry investments, outside of NZU price?

Yes

There are a number of other issues that need to be addressed at the same time, including:

- Provide greater certainty this time that the NZ ETS will deliver (see my comments under (10) above). The image of the NZ ETS with the forestry sector has been seriously damaged and is currently at a very low ebb.
- Taxation provisions (including the near non-existent spreading of income regime, the fact that a vendor of a forest has to pay tax at the time of sale but the purchaser has to carry forward the purchase cost until the time of harvesting – this has created an illiquid market for forestry investments);
- Local body rules impeding plantings in ways that do not apply to agriculture – particularly their rules on “outstanding natural landscapes” and “sites of ecological significance”;
- Local body rules and forestry roading – local bodies collect rates annually on forestry land (on the same basis as farming land), but once it needs to utilise roads at the time of harvesting, have a range of penalty charges to utilise roads;

- Possibly (sadly) some sort of land purchase subsidy to better balance the subsidies (irrigation etc) that go to inflating land costs that forestry has to try and match.

15. What are your reasons for the above answer? If you answered yes, we would be interested in comments on:

- any barriers to participating in the NZ ETS that could be reduced*
- other factors.*

I think I have covered these under (14) above.

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?

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

Yes

- restrictions on how many units can be surrendered*

Possibly, but could just add to the complexity

- others (please explain).*

Not sure

Other issues: managing unit supply – auctioning

17. Should auctioning be introduced in the NZ ETS?

Unsure – the reasons for including this measure have never been adequately explained – it has become another source of uncertainty for forestry investment.

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

- other (please explain).*

See (17)

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?

See (17)

Other issues: managing price stability

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

- significant.*

See (13) above.

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

Yes

But with some reservations that it is transparent and clearly understood in a manner that will reduce the temptation for political meddling.

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)*

Possibly

b) *lower price limits (eg, price floor)*

Probably

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

The need for certainty by all stakeholders in the scheme to have as much certainty as possible as to price management limits.

Other issues: operational and technical matters

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

Unsure – However, I am generally satisfied that the ETS administrative efficiency from a forestry perspective has been ok. It was a massive legislative and administrative change to NZ and has been introduced professionally and operated competently.

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.

Nothing that immediately comes to mind, but will put some thought into it for the April 16 submission

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?

Yes – the collapse in the prices of petroleum based products would be one example.

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

Unsure!

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

28. Please comment here

I will save these for the April 16 submission!

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 close at 5.00pm on 19 February 2016.

Submissions on Other matters close at 5.00pm on 30 April 2016.

