

New Zealand ETS review 2015/16 consultation

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

Answer 1:

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

Answer 2:

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

Answer 9:

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

Answer 10:

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

Answer 11:

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?

Answer 12:

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

Answer 13:

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

Answer 14:

15. What are your reasons for the above answer?

Answer 15:

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

Answer 16: c) other

16A. Please explain your answer:

There is also an opportunity to reduce the cost of NZ meeting its commitments through links with other emerging trading schemes in Asia and elsewhere. Linking of emissions trading schemes enlarges the scope for cost-effective emissions reductions as a single carbon price signal is now shared among a larger number of emitters. These then all have the common incentives to reduce their emissions in a way that the cost at the margin of doing so is equal to the prevailing carbon price. This captures additional gains from trade that are available internationally but not to any individual country. Such linking will become more important as more countries target stronger emissions reductions in the future.

17. Should auctioning be introduced in the NZ ETS?

Answer 17: Yes

when

17A. Please explain your answer:

The NZ ETS still freely allocates a large fraction of permits to emissions-intensive trade-exposed sectors instead of running more auctions. Industrial activities that are deemed to be highly emissions-intensive and exposed to international trade receive up to 90 percent of their allowances for free under the NZ ETS. Auctioning of NZUs was only introduced in 2012. Such free allocations represent a transfer of wealth from taxpayers to industry; the funds could instead be used to reduce taxes elsewhere, cut the public debt, or fund research & development. International experience to date suggests that the competitiveness and leakage impacts of carbon pricing are largely modest (Vivid Economics, 2014; Partnership for Market Readiness, 2015). Carbon trading should thus rely more on auctioning.

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

Answer 18:

18A. Please explain your answer:

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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?

Answer 19:

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

Answer 20:

20A. Please explain your answer:

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

Answer 21:

21A. Please explain your answer:

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

Answer 22:

22A. Please explain your answer:

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

Answer 23:

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The NZ ETS carbon price lags substantially behind other international jurisdictions, which have price signals up to 25 times stronger. In late 2015, its price was equivalent to US\$5/tCO_{2e}; this placed it in the company mainly of pilot trading schemes in China. The NZU price crashed from around NZ\$20 to below NZ\$5 within the space of 18 months between early 2011 and mid-2012. Although permit prices in the EU trading scheme are currently at a similar level, several European countries have additional measures which strengthen the carbon signal to a level of around US\$15-30. In Scandinavian countries prices are generally above US\$50 – with a US\$130 carbon tax in Sweden (World Bank, 2015). Moreover, the NZ ETS currently has operated with a price cap of NZ\$25 per unit, and many participants obtain a 50 percent price discount due to the “one-for-two” compliance scheme.

The NZ ETS has not set an emissions cap in the way that is standard practice in other carbon trading schemes. International emissions trading schemes such as the EU ETS operate with a pre-defined cap on emissions over a multi-year horizon. This limits the supply of emissions permits, and is the primary vehicle for ensuring a significant carbon price, now and in the future. By contrast, New Zealand has not fixed a specific emissions cap for its ETS but rather has allocated permits to emissions-intensive industry in proportion to their production.

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

Answer 24:

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

Answer 25:

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

Answer 26:

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

Answer 27:

28. Please comment here

Answer 28:

Our key points for the NZ ETS are:

- International experience suggests a need for reform of the NZ ETS:
- the price signal generated by the NZ ETS lags substantially behind international carbon-pricing leaders,
- the NZ ETS has not set an emissions cap in the way that is standard practice in other carbon trading schemes, and
- the NZ ETS still freely allocates a large fraction of permits to emissions-intensive trade-exposed sectors instead of running more auctions.
- In order to meet the proposed commitments agreed at Paris at least cost, the NZ ETS should also consider greater sectoral coverage and links with trading schemes in Asia and elsewhere.

Introduction

New Zealand has made a pledge to transition to a low-carbon economy, which now requires follow-through. In July 2015, the New Zealand Government announced a new target to reduce greenhouse gas (GHG) emissions to 30 percent below 2005 levels by 2030, which is equivalent to 11 percent below 1990 levels, with a 50 percent cut by 2050. This formed its INDC for the Paris COP21 negotiations that took place in December 2015. New Zealand's pledge has been criticized for falling short of the commitments made by other developed countries. Particular features of the New Zealand economy include the large role of forestry emissions as well as an electricity sector

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which already generates around 80 percent from renewable sources.

The overarching rationale behind carbon pricing is to achieve a reduction in GHG emissions in a cost-effective manner. The key to the effectiveness of an ETS is that regulated entities incorporate the carbon price in their decision-making. A substantial emissions reduction that recognizes the social costs of carbon requires a significant carbon price.

To meet its INDC at least cost, the New Zealand Government should consider increasing sectoral coverage. The current design of the NZ ETS involves only partial coverage amounting to around 55 percent of NZ's GHG emissions. The NZ ETS began with forestry in 2008 and has since been amended and expanded on several occasions. Participating sectors that are obliged to surrender New Zealand Units (NZUs) now include stationary electricity generation, emissions-intensive industry, forestry, liquid fossil fuels (production and imports), and waste. The scheme does not include transport. The agriculture sector, which accounts for 40 percent of GHG emissions, only has reporting obligations and may be difficult to fully integrate into the NZ ETS.

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