Update on NZ ETS reforms

2 June 2020
Contents

1. Overview
2. Emissions Trading Reform Bill
3. Provisional Emissions Budget and NZ ETS settings
4. Auctioning rules
1. Overview
2. Emissions Trading Reform Bill
3. Provisional Emissions Budget and NZ ETS settings
4. Auctioning rules
The NZ ETS will help meet our climate targets

The Government is reforming the New Zealand Emissions Trading Scheme (NZ ETS) so it plays the key role in meeting our emission reduction targets

- Covered sectors must surrender an emission unit (NZU) for each tonne of greenhouse gases they emit
- The Government will cap the volume of NZUs supplied into the scheme each year, reducing this over time to align with our targets
- NZUs will be sold at auction up to this cap
- The NZU price will be determined by the market
- Emission prices give incentive to reduce emissions and increase removals
Government’s announcements today cover three NZ ETS topics

- **Emissions Trading Reform (ETR) Bill**
  - Supplementary Order Paper (SOP) for the ETR Bill tabled in Parliament

- **NZ ETS settings (regulations)**
  - Decisions on the Provisional Emissions Budget (PEB) and the NZ ETS unit supply and price control settings

- **NZ ETS auction rules (regulations)**
  - Decisions on the detailed rules for auctioning NZUs
Timelines

ETR Bill process
1. Bill introduced
2. Agricultural emissions SOP
3. Review and report by ENV select committee
4. 2nd reading and releasing the Govt. SOP
5. COTW, 3rd reading and Royal Assent

NZ ETS settings process
1. Consultation document on settings released
2. Public consultation on settings
3. Advice on settings from officials to Ministers
4. Cabinet decisions on settings
5. Public announcement of settings
6. Make settings in regulations under the amended Act

NZ ETS auction rules process
1. Consultation document on auction rules released
2. Public consultation on rules
3. Advice on rules from officials to Ministers
4. Cabinet decisions on rules
5. Public announcement of rules
6. Set rules in regulations under the amended Act

Today (2 June 2020)
Documents and information being released this week

Released by MfE and MPI
- Cabinet papers
- Website updates
- Briefing notes (advice to Ministers)
- Regulatory Impact Analyses (RIA)

Released by Minister Shaw
- Press release
- Government SOP to Parliament (updated full version of ETR Bill)
New Zealand’s climate change legislation architecture

Both Bills amend the Climate Change Response Act (CCRA)

Zero Carbon Bill (ZCB)

Emissions Trading Reform Bill (ETR)

2050 target

Emissions budgets

NZ ETS framework and settings

Policies to drive mitigation & a just transition

Climate and economic outcomes
Domestic climate change targets

The 2050 target looks forward 30 years.

Emissions budgets look forward 10-15 years and are updated every 5 years.

NZ ETS settings look forward 5 years and are updated annually.

- Climate and economic outcomes
- Policies to drive mitigation & a just transition
- NZ ETS framework and settings
- Emissions budgets
- 2050 target
Today’s announcements

The Provisional Emissions Budget (2021-25)

The first NZ ETS settings (2021-25)
Timelines

ETR Bill process

1. Bill introduced

2. Agricultural emissions SOP

3. Review and report by ENV select committee

4. 2nd reading and releasing the Govt. SOP

5. COTW, 3rd reading and Royal Assent

Today
(2 June 2020)
**Parliamentary stages still to come**

**Second reading (2 June 2020)**
- Parliament debates the contents of the Bill
- A series of speeches
- No amendments can be made to the Bill at this stage
- The House votes on whether to proceed with the Bill at the conclusion of this session

**Committee Of The Whole (COTW)**
- Any Member of Parliament can propose changes to the Bill
- These changes are proposed by tabling ‘Supplementary Order Papers’
- Parliament debates and votes on each of the SOPs
- The total number of SOPs is unknown at this stage
- The Government SOP has been released today (2 June)

**Third reading**
- Parliament debates the contents of the Bill
- A series of speeches
- No amendments can be made to the Bill at this stage
- The House votes on whether to proceed with the Bill at the conclusion of this session
## Summary of the ETR Bill before the SOP (incl. Select Committee)

<table>
<thead>
<tr>
<th>Main non-forestry reforms</th>
<th>Main forestry reforms</th>
<th>Including agriculture</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Cap emissions and move to selling NZUs at auction, while considering future emissions budgets and targets</td>
<td>• Averaging accounting for post-1989 forests</td>
<td>• After extensive consultation, all agricultural emissions will be priced from 2025</td>
</tr>
<tr>
<td>• Auction price controls: replace fixed price option (FPO) with cost containment reserve to restrain high prices; set a price floor</td>
<td>• Replace Permanent Forest Sink Initiative (PFSI) with new permanent forestry activity</td>
<td>• Methane and nitrous oxide emissions from livestock will be priced at farm level; nitrous oxide emissions from fertiliser will be priced at processor level</td>
</tr>
<tr>
<td>• Phase down free allocations</td>
<td>• Suspend liability for carbon loss during temporary adverse events for permanent forests and post-89 using averaging</td>
<td>• Livestock emissions reported at farm-level from 2024 (fertiliser processors already face reporting obligations)</td>
</tr>
<tr>
<td>• Strengthen and simplify compliance regime, improve transparency, more data collection, advance notice for publishing emissions data</td>
<td>• Offsetting for post-89 forests using averaging</td>
<td>• Joint Action Plan on Primary Sector Emissions (He Waka Eke Noa)</td>
</tr>
<tr>
<td></td>
<td>• Operational improvements to simplify forestry operations, resolve inconsistencies, provide more flexibility</td>
<td>• Climate Change Commission will review progress of this and other milestones in 2022</td>
</tr>
</tbody>
</table>
## Changes made by the Government’s SOP

### Non-forestry changes
- Extend FPO to cover emissions from the start of 2020, raised to $35 *(more detail to come)*
- Deal with COVID-19 disruptions by introducing new (limited) power for Minister to extend Commission’s statutory deadlines
- Delay new penalty regime for small forest liabilities to investigate alternatives (avoid potential financial hardship) until 1 Jan 2023
- Simplify process for recalculating penalties if emission return amended (basically now just pay or be repaid the difference)
- Technical changes to unit entitlements and surrender obligation transfers in the Registry

### Forestry changes
- Deal with COVID-19 disruptions by delaying major forestry policies one year to 1 Jan 2023 (including averaging accounting and permanent forestry), and amend transitional arrangements:
  - Post-89 forests registered from 1 Jan 2023 must use averaging
  - any registered from 1 Jan 2019 to 31 Dec 2022 can choose to move in 2023
  - PFSI forests move into the NZ ETS from 1 Jan 2023
- Extend liability suspension for temporary adverse events to existing post-89 stock change forests — all post-89 NZ ETS forests now treated the same
The FPO will overlap with the start of auctioning

- The current FPO in the Act allows participants to meet their NZ ETS obligations by paying $25 to the Crown instead of surrendering a unit
- The original Bill removed the FPO entirely on the day of the first auction — could not be used for 2020 emissions from that date (or for future amended returns)
- Amendments in the SOP:
  - raise the FPO from $25 to $35 for emissions occurring in the 2020 calendar year
  - keep access to the $35 FPO available for all 2020 emissions, even if auctioning begins before surrenders for 2020 emissions are due on 31 May 2021
  - $25 FPO for pre-2020 emissions and $35 FPO for 2020 emissions stay indefinitely
  - as a backstop: $35 FPO remains available to cover activities in 2020 plus any additional *full* calendar year until the first auction
  - Forestry participants will be able to use the $25 FPO (for activities before 1 Jan 2020) and the $35 FPO (for activities in calendar year 2020) on a pro-rata basis
## Case studies for accessing the FPO in the post-SOP world

<table>
<thead>
<tr>
<th></th>
<th>If first auction is on 17 Mar 2021</th>
<th>If first auction is on 1 Sept 2021</th>
<th>If first auction is on 17 Mar 2022</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-forestry participants can use $35 FPO:</td>
<td>for 2020 emissions in standard return, up until 31 May 2021 deadline, including if amended later</td>
<td>for 2020 emissions in standard return, up until 31 May 2021 deadline, including if amended later</td>
<td>for 2020 and 2021 emissions in standard returns, up until 31 May 2021/2 deadlines, including if amended later</td>
</tr>
<tr>
<td>Forestry participants can use $35 FPO:</td>
<td>on pro-rata basis in a net emission return covering 2020 year, and $25 FPO for years before 2020</td>
<td>on pro-rata basis in a net emission return covering 2020 year, and $25 FPO for years before 2020</td>
<td>on pro-rata basis in a net emission return covering 2020 and/or 2021 years, and $25 FPO for years before 2020</td>
</tr>
</tbody>
</table>

This timeline is what the Government is working towards.
1. Overview
2. Emissions Trading Reform Bill
3. Provisional Emissions Budget and NZ ETS settings
4. Auctioning rules
**Timelines**

**Proposed NZ ETS settings:**
- December 2019 – February 2020

1. Consultation document on settings released
2. Public consultation on settings
3. Advice on settings from officials to Ministers
4. Cabinet decisions on settings
5. Public announcement of settings
6. Make settings in regulations under the amended Act

Today (2 June 2020)
The Provisional Emissions Budget (PEB) 2021-25

- PEB covers period until Commission’s first emissions budgets and advice in 2021
- PEB is roughly a straight-line reduction from today’s emissions towards the 2050 target
- It will require strong action across a range of sectors to achieve

<table>
<thead>
<tr>
<th>Year</th>
<th>2021</th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
<th>2025</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agreed PEB (Mt CO₂-e)</td>
<td>72</td>
<td>72</td>
<td>72</td>
<td>70</td>
<td>68</td>
<td>354</td>
</tr>
</tbody>
</table>
Regulations for the unit supply settings

Unit supply settings determine auction volume by applying these steps to the PEB:

1. Remove emissions from outside the scheme from the NZ ETS cap (194m)
2. Make any required technical or forestry related adjustments (0)
3. Remove freely allocated units (43m)
4. Remove volume of units to drive stockpile reduction (27m) (more info on next slide)
5. Set a limit on approved overseas units (0)
6. The remaining volume is available to auction (90m)

These numbers will be updated annually

<table>
<thead>
<tr>
<th>Annual auction volumes (NZU millions)</th>
<th>2021</th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
<th>2025</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>19</td>
<td>19</td>
<td>18</td>
<td>17</td>
<td>15</td>
<td>90</td>
</tr>
</tbody>
</table>
Reducing the stockpile

• Large current stockpile of over 130m NZUs in private accounts — worth over three years of emissions
• Significant portion being held for future surrender obligations and can’t be sold freely

Helpful
Provides liquidity in the secondary market

But limits NZ ETS effectiveness
• Doesn’t help meet emission reduction targets
• Dampens NZU price

To reduce the stockpile:
1. Auction fewer units (supply less than cap)
2. Some obligations must now be met from secondary market
3. Stockpile reduces over time

PEB targets stockpile reduction of 27m NZUs by 2025
Auction price floor and CCR price trigger level

- Auction price floor will be $20 in 2021, rising an estimated 2% a year for inflation to 2025
- CCR price trigger will be $50 in 2021, rising an estimated 2% a year for inflation to 2025
Cost containment reserve volume

- How effectively the CCR dampens auction price depends on volume of units released.
- The CCR volume will be:
  - the units withheld from auction underneath the NZ ETS cap to reduce the stockpile; plus
  - five percent of the total NZ ETS cap
- Units sold from the reserve that exceed the NZ ETS cap will have to be backed by the Government procuring equivalent emissions reductions or removals.

<table>
<thead>
<tr>
<th>Year</th>
<th>Free allocation</th>
<th>Proposed auction volumes</th>
<th>NZ ETS cap</th>
<th>Stockpile adjustment</th>
<th>5 percent of cap</th>
<th>Total CCR volume (NZU millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>8</td>
<td>5</td>
<td>19</td>
<td></td>
<td></td>
<td>7</td>
</tr>
<tr>
<td>2022</td>
<td>8</td>
<td>5</td>
<td>19</td>
<td></td>
<td></td>
<td>7</td>
</tr>
<tr>
<td>2023</td>
<td>9</td>
<td>5</td>
<td>17</td>
<td></td>
<td></td>
<td>7</td>
</tr>
<tr>
<td>2024</td>
<td>9</td>
<td>5</td>
<td>16</td>
<td></td>
<td></td>
<td>7</td>
</tr>
<tr>
<td>2025</td>
<td>9</td>
<td>5</td>
<td>16</td>
<td></td>
<td></td>
<td>7</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td><strong>35</strong></td>
</tr>
</tbody>
</table>
Timelines

NZ ETS auction rules process

1. Consultation document on auction rules released
2. Public consultation on rules
3. Advice on rules from officials to Ministers
4. Cabinet decisions on rules
5. Public announcement of rules
6. Set rules in regulations under the amended Act

Proposed rules for auctioning: November – December 2019

Today (2 June 2020)
<table>
<thead>
<tr>
<th>Decisions on auctioning rules</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Frequency</strong></td>
</tr>
<tr>
<td><strong>Scheduling</strong></td>
</tr>
<tr>
<td><strong>Format</strong></td>
</tr>
<tr>
<td><strong>Volume released</strong></td>
</tr>
<tr>
<td><strong>CCR</strong></td>
</tr>
<tr>
<td><strong>Bidder registration and collateral</strong></td>
</tr>
<tr>
<td><strong>Bid size</strong></td>
</tr>
<tr>
<td><strong>Technical reserve price</strong></td>
</tr>
<tr>
<td><strong>Handling tied bids</strong></td>
</tr>
<tr>
<td><strong>Receiving purchased NZUs</strong></td>
</tr>
<tr>
<td><strong>Publishing results</strong></td>
</tr>
</tbody>
</table>
Next steps for auctioning

- In 2019 Government issued a request for proposals to supply and manage NZ ETS auctions
- Contract negotiations underway, successful supplier announced shortly
- Auction operator expected to begin participant training later this year