Submission from Straterra
to the Ministry for the Environment
Emissions Trading Scheme Settings for 2023
June 2023

Introduction

1. Straterra is the industry association representing the New Zealand minerals and mining sector (including coal). Our membership is comprised of mining companies, explorers, researchers, service providers, and support companies.

2. We welcome the opportunity to make this brief submission on the Government's proposals for the Emissions Trading Scheme (ETS) as set out in the consultation document, Annual updates to the New Zealand Emissions Trading Scheme limits and price control settings for units 2023 (the document).

Summary

3. We do not support the changes proposed by the Climate Change Commission which are likely to result in reduced units being available and higher prices. These will come at a time of high inflation and cost of living pressures for households and are likely to lead to significant business closures with emissions transferring offshore (so no reduction in global emissions). They are also likely to lead to mass afforestation of radiata pine which is contrary to the objectives of other parts of Government policy.

4. The ETS settings are required to be reviewed annually. There have now been two proposed updates. The magnitude of the changes proposed on both occasions combined with the frequency creates uncertainty which impacts on confidence in the market and of its participants in investing in the scheme. Stable and predictable ETS settings are needed for the scheme to work efficiently.

5. We supported the Government's decision to reject the Climate Change Commission's recommendations at the 2022 review of the ETS unit limit and price control settings. Given little has changed in the economic environment since then in terms of persistent inflationary pressures and a global energy crisis, as well as the short period that has since lapsed, we fail to understand why another major disruption to policy and investment settings is being proposed. It makes little sense with the wider review of the Emissions Trading Scheme being imminent.

Submission

6. Most of the proposals in the document pave the way for significantly higher NZU prices – much higher than market participants and businesses generally anticipate under the existing settings. These will, if implemented, in turn feed into higher prices generally throughout the economy largely through higher energy costs. This comes at a time when New Zealanders are battling a cost-of-living crisis. The Government is also facing a continuing high inflationary environment in New Zealand and around the world, as well as an ongoing international energy crisis, triggered largely by the Russia-Ukraine war.

7. The Climate Change Response Act 2002 says both inflationary impact and impact on households and the economy have to be taken into account when considering NZU limits and price control settings.

8. We go through the main changes proposed in turn.

ETS limits / Auction volumes

9. We support the status quo option in Table 12 on page 28. We do not support a reduction in units available for auction.

10. The Commission's alternative proposed reductions would have a major upward impact on price and squeeze emitting businesses to such an extent that business closures and carbon leakage are likely.

11. The ability to change the first two years is limited by the Climate Change Response Act so that regulatory predictability is maintained. But the abrupt change as proposed by the Commission in year three, from 15.3 million tonnes to 8.5 million, undermines this intention.

12. A large part of the proposed reduction is driven by adjusting for the stockpile and reducing the number of units issued at auction accordingly.

13. As the document says on page 24, all emissions trading schemes around the world allow 'banking' of units and there are good reasons for allowing it, namely it helps reduce price volatility, ensures the NZU price is forward-looking, and supports participants to manage their future liabilities.

14. There seems to be an assumption that withholding NZUs from auctions would result in units being made available on the secondary market, but this will not necessarily be the case.

15. Lowering the supply of units at auction will not necessarily make those holders of banked units use or release them. All it will do is reduce availability for participants and cause the price to rise. The consequences will be severe for many businesses if the banked units are not released and if there is a shortfall of units.

Price floor / Auction reserve

16. We support Option one – the status quo in Table 13 on page 36. We oppose an increase in the auction reserve price beyond what has already been signalled.

17. The Commission has repeated its 2022 recommendations to raise auction reserve prices plus an inflation adjustment. This would result in an auction reserve price of $79 in 2028 compared with the status quo of $47.50.

18. As stated in the consultation document, such an abrupt and precipitous rise would undermine regulatory certainty. It would also send a high signal for land use to change to forestry which is contrary to what is trying to be achieved elsewhere.

Cost Containment Reserve

19. We support Option one, on page 38 – the status quo of a single tier cost containment reserve.

20. We do not support the alternatives of no CCR or a two-tiered CCR.

21. The analysis in Table 15 on page 39 of the consultation document does not provide good reasons for doing so. The only argument provided in support is that it "reduces the risk of slowing stockpile drawdown". As stated earlier in the submission, we do not agree with the Government's rationale for stockpile drawdown.

22. We agree with the comment in the table about the additional complexity it will introduce.

Cost containment reserve total volumes

23. As discussed on page 40, the CCR's purpose is to release additional units beyond a specified threshold to stabilise prices. We support the current reserve volume of units and we do not support the proposal to reduce it.

24. One possibility in the future would be for international units, once they are available, to be among the units introduced as part of the cost containment reserve. It goes without saying that all such overseas units would have to be verified and have environmental integrity. It also goes without saying that New Zealand access to these units currently does not exist and may never exist.

Cost containment reserve trigger prices

25. We support Option one, in Table 16 on page 42 – the status quo extended.

26. The CCR trigger price is deemed to be "the upper extreme of acceptable prices in the New Zealand ETS" and can be seen as a de facto cap. The Commission's proposed increases to the trigger price are excessive (from $91.84 to $184/$231 (low trigger/ high trigger) in 2024, increasing to $226/$282 in 2028) and, as stated in the document, will have significant impacts on households and the economy including inflationary effects. These price rises would likely occur before the price is actually triggered in the auction because of the signal it sends the market as to how high prices are allowed to go.

27. In addition to this, the high prices and the uncertainty created would result in carbon leakage and business closures if the NZU price reached them.

28. The document acknowledges this on page 48 where it says: "In the event that prices increased to reach the Commission's recommended CCR trigger prices, this price rise, in combination with the phase-out of industrial allocation, might have the impact of closing down firms in some industries, unless they rapidly decarbonise".

29. Given the practical inability for such rapid decarbonisation to occur, this statement cannot be emphasised enough as a rationale for maintaining status quo ETS settings generally. If the proposals go ahead, the Government will have to manage the risk of a major adverse consequences for the New Zealand economy.

Other points

International units

30. We make the point that climate change mitigation requires a global approach i.e. a reduction in global emissions. Allowing the purchase of legitimate overseas units with high environmental integrity allows emission reductions to occur where abatement costs are the lowest, and so we urge the Government to press ahead with discussions with overseas counterparts to enable international units to be included.

31. The carbon price faced by New Zealand emitters, and the stringency of other policies to reduce emissions, need to parallel those faced by our international trade competitors and partners as much as possible, so we can remain competitive and emissions leakage does not result.

32. We note that pricing schemes only cover 23% of global emissions (according to the World Bank's State and Trends of Carbon Pricing 2023) and that the average price provided by ETS schemes and carbon taxes in 2021 was US$4.50 compared with New Zealand's of around NZ$62.50 (US$39.00).