

## **Submission**

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**On: Improvements to the New Zealand Emissions Trading Scheme:  
Consultation document**

### **Introduction**

1. The Northland Regional Council (council) is grateful for the opportunity to comment on the consultation documents. This submission is made in the interests of promoting a sustainable environment and economy in Northland and with council's statutory functions and roles under the Local Government Act 2002 and other relevant legislation in mind.
2. The council understands the importance of the Emissions Trading Scheme (ETS) in promoting and enabling the transition to a low net emissions economy. Council agrees that there is a need to improve the framework of the ETS and strengthen incentives for permanent and commercial plantation forests. The Northland region has significant potential for land use change with large areas of land suited to conversion to forest and therefore has an interest in improvements to the ETS to facilitate this.
3. Council also considers there is potential to integrate abatement / offsetting measures into existing farm / agricultural systems that should be incentivised through ETS settings, particularly given the very limited tool box currently available. This will become increasingly important when agriculture enters the scheme if the government's objectives for a productive, sustainable and climate change resilient economy and just and inclusive society are to be achieved. Council therefore supports the decision not to include agriculture in the ETS until receiving advice from the Climate Change Commission and further offset / abatement measures for agricultural emissions can be considered.

## Submission

4. Council supports the intent set out in the discussion document to cap emissions from sectors in the ETS in a coordinated, transparent and predictable manner. The five proposals outlined to achieve this appear logical and council responds to each below largely following the consultation document format.
5. Unit supply volumes: Council understands that the ETS is a quantity based policy tool whereby the number of units available in the market has a direct bearing on price and the unit price in turn affects investment in low emissions technology and / or offsetting. Council agrees the matters listed in Question 1 should be considered in setting the unit supply. Council does however recommend the following be added:
  - The ability for a given sector to offset or mitigate emissions – some sectors (E.g. agriculture) may have limited ability to reduce emissions and this should be reflected in the unit supply volume to ensure an equitable regime and avoid financial ‘shocks’.
  - The potential financial / economic impact on a sector(s) of a reduced unit supply volume.

Council considers there should be restrictions on adjustment to unit supply volumes that include:

- unit supply volumes in the NZ ETS align with New Zealand’s emissions reduction targets
  - they can only occur when there has been a significant change in context (eg, changes in emissions projections or emissions budgets)
  - the Government is required to explain if it makes a change to unit supply volumes
6. Auctioning: Council understands the government has decided to introduce auctioning of NZ units to better align the ETS to emissions targets. Council sees auctioning a logical approach which will mean the market value is reflected in the price of units. In terms of the auction format to be used, council do not support options C given we have a secondary market (and therefore there are good price signals) or option D given it selects for the highest price (as opposed to efficient allocation). Council agrees Option A (uniform-price, sealed-bid, single-round auction) is the simplest, promotes market efficiency and protects against collusion and ‘hoarding’. Council supports quarterly auctions as this should provide an appropriate balance between participation costs, be frequent enough to ensure unit volumes released are appropriate while avoiding participation costs and disruption likely with more frequent auctions. Council is of the view that all NZ account holders should be able to participate in auctions (not just ETS participants) as this is more likely to lead to an efficient price, enables voluntary participation and limits collusion / manipulation.
  7. Use of auction proceeds: While we understand the New Zealand government does not typically link revenue from a particular source directly to a specific spending programme, council considers there is merit in doing so at least in the short to medium term given the potential for disproportionate effect on some sectors and / or communities. Council considers a significant percentage of the proceeds should therefore be ‘ring-fenced’ to assist particularly disadvantaged communities and investment in emissions reduction technology in those sectors where this is severely limited.

8. Price ceiling: Council supports price ceilings for NZ units as this will limit undue price increases. Council also supports retaining the fixed unit price approach until at least 2020 (acknowledging this was intended as a transitional measure and that the current \$25 / unit price may need adjustment). Council tends to agree that if the government moves to control the volume of units available a price 'floor' is unlikely to be needed. While the fixed price provides certainty for those with obligations, council understands the problems it could cause in the medium-long term, even if the price is regularly adjusted (largely related to limited control on the volume of units available and the lack of certainty emissions reduction targets will be met). The consultation document proposes a cost containment reserve (CCR) approach be used to control unit price, meaning the Government sets aside a number of NZUs (the reserve) to be sold only if a specified trigger price is reached - it therefore does not guarantee a maximum compliance cost per unit for participants and how much influence it would have on the price of units depends on the volume of units in the reserve. It is therefore more flexible and provides greater confidence emission reduction targets can be met but less certainty for participants on compliance / obligation costs (unit price). There are therefore two decisions to be made – the volume of units available (i.e. held in the reserve for auction) and the 'trigger' price at which the reserve would be sold. These decisions could either be made by:

- leaving it to the complete discretion of the government, or
- leaving it to the discretion of the government but requiring certain factors to be considered (E.g. forecasts of abatement required to meet reduction targets, inflation rates or international carbon prices) or
- Applying set formula set out in the ETS legislation or regulations.

The consultation document does not identify a preferred option for this decision-making process but does propose a five-year 'rolling' process for deciding and announcing these unit supply settings - meaning the price trigger and reserve volume would be set for five years in advance, and extended each year. If the government moves to a volume-limited auction system, council supports a cost containment reserve (CCR) to replace the fixed price as this would mean the price is set by the market (not the fixed price). As to how the CCR settings are decided, council suggests retaining flexibility at this early stage and avoiding a set formula at this time given the uncertainties. We therefore support decision-maker discretion subject to a range of mandatory considerations – these should include those identified in the consultation document but should also consider:

- forecasts of expected domestic abatements costs by sector
- ability to abate emissions by sector and likely demand for units.

The decision maker should also be required to document the rationale for the decisions on these settings. Council supports increasing the limit on international units if high domestic abatement costs cause high unit prices (as this should be a relatively quick solution).

9. Limit on international units: Council understands the government desire to control the use of international units. The two options available to manage use of international credits – allowing participants to purchase and surrender a limited volume or, by the government purchasing a limited volume of international units and including these in the domestic auction – have pros and cons. Council is of the view that the government should allow some industries / sectors to meet their obligations using a limited volume of international units. This should occur on the basis that they:

- Do not receive allocation of NZ units

- Have limited offsetting or abatement options available.
- The proportion of their obligations to be met with international units will be reduced over time as abatement / offsetting options become available.
- The international units able to be used are defined by government.

This recognises that some industries / sectors have limited emission reduction options and will retain some flexibility for those potentially disadvantaged industries / sectors to meet obligations both using NZ domestic units and international units.

10. Phase-down of industrial allocation: Council does not support option 1 (up-front decision to phase down industrial allocations) and prefers either of Option 2 (a 'test condition') or Option 3 (defined decision-making process). This is because these options use an evidence base and analysis rather than an uninformed decision. If a decision-making process (Option 3) is to be used council agrees with the matters to be considered in Question 15.
11. Market information: At this stage council does not see the need to or any benefit arising from publishing individual participants emissions data or non-compliance, particularly at this stage – there may however be a case for such once the revised ETS matures.
12. Compliance and penalties: Council supports an infringement regime for lower level offences as prosecution is often unwarranted and expensive. We have no strong views on the penalty provisions, but suggest a proportional approach seems the more equitable.
13. Technical and operational improvements: Council has little to contribute on these issues.

## **Conclusion**

14. Council thanks the Ministry for the opportunity to comment on the proposed changes to the ETS. Please do not hesitate to contact us should you wish to discuss any of the above.

Signed on behalf of the Northland Regional Council by:

Dated: XX September 2018

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