

**Submission from Straterra
To the Ministry for the Environment
Improvements to the Emissions Trading Scheme
September 2018**

Introduction

1. Straterra is the industry association representing the New Zealand minerals and mining sector. Our membership is comprised of mining companies (including coal), explorers, researchers, service providers, and support companies.
2. We welcome the opportunity to make this submission on the [*Improvements to the New Zealand Emissions Trading Scheme*](#) Discussion Document which the government is consulting on.

General Comments

3. Straterra acknowledges the global imperative of reducing carbon emissions but believes New Zealand must act in concert with global progress so that we retain our competitiveness and avoid carbon leakage.
4. In principle, we support the Emissions Trading Scheme and a carbon price as a tool to meet the government's Paris commitments to reduce emissions, subject to specific conditions.
5. These conditions include a means of identifying and mitigating any adverse impacts on the competitiveness of, particularly, New Zealand's energy intensive and trade exposed (EITE) businesses.
6. Without access to global markets for CO₂, the market for CO₂ in New Zealand needs to be managed through free allocation mechanism and price caps in order that environmental and economic objectives are appropriately balanced.
7. Currently only 15% of global emissions are subject to any carbon price, and energy-related greenhouse gas emissions are continuing to increase globally. This significantly limits the extent to which a carbon price in New Zealand can be used to drive emissions down – subject to sector, and sometimes company specific, assessment of the impact of increased costs on, particularly, the energy-intensive, trade-exposed (EITE) sectors.

8. We argue that there is no global or New Zealand benefit if costs are imposed on New Zealand emitters that are not matched by our trade partners and trade competitors.
9. A high CO2 price may reduce New Zealand emissions, and increase forest planting, but will lead to carbon leakage – with investment lost and energy intensive industries moving to those countries¹ without similar imposts achieving little or nothing for an overall reduction in global emissions. New Zealand is a very efficient producer of many energy intensive products that we export and any loss of investment, economic activity and jobs in these sectors would typically be a negative global contribution.
10. Because climate change is a global issue, an international market covering the majority of global emissions is needed but we accept this is not achievable at this time. An international market would enable countries and sectors that can emit more efficiently than others to do so. That is the purpose of a global emissions trading scheme. This would deliver a fair playing field for New Zealand energy users, and would be a more efficient way to reduce global emissions.
11. We support the New Zealand government placing a high priority on working with other countries to developing a robust and credible international carbon market.
12. Against these general comments we now discuss some of the specific issues that the document consults on relating to the workings of the Emissions Trading Scheme and how it can be improved.

Unit Supply Decisions

13. The supply of New Zealand Units influences both the carbon price in the ETS and the total emissions permitted in a set period. For the reasons outlined in the previous section, decisions on the supply of units and their rate of reduction over time must first and foremost take account of what our trade partners and competitors are doing.
14. Such decisions also need to take account of the fact that many New Zealand emitters, particularly in the South Island, do not have access to cost effective alternatives and that emissions abatement is expensive.
15. It is unclear from the document how the decisions on the supply of units will be made and what institution will be making them. It is important that there is a transparent and robust decision making framework, supported by appropriate analysis and which involves discussion with industries impacted.
16. We agree with the document that an auction is the best way to introduce the units. This should be held monthly or quarterly with all New Zealand Emission Trading Register account holders being able to participate. Proceeds from the auction should be directed towards purposes related to emission reductions as opposed to going into general crown revenue.

¹ This can take the form of international investment relocating offshore, or production moving offshore as business downsize or close, allowing international demand to be met by producers in other countries.

Price Ceiling Proposals

17. In the absence of an international carbon market, the carbon price faced by New Zealand emitters must resemble or reflect that faced by our international trade competitors and partners. This is needed to ensure New Zealand businesses are not put at a disadvantage relative to their international competitors. It is also needed to send an efficient signal to New Zealand emitters as to whether they should emit or abate.
18. We support the commitment expressed in the document for emissions prices in New Zealand to remain in line with international emissions prices. It is equally important that the purpose of this commitment is explicit – to retain competitiveness.
19. The price cap has an important role here – the nature of the market in New Zealand means that the carbon price can be almost guaranteed gravitate toward the cap. So whether it is the existing Fixed Price Option (FPO) or the proposed new Cost Containment Reserve (CCR) that is adopted, the price ceiling (as well as the number of units issued) must be linked to what is happening internationally.
20. The document provides two options for how the price ceiling is set – a mandated formulae or at the discretion of the decision maker. We believe it should be done by a combination of a mandated formulae linked to the carbon prices being faced by our trade competitors and discretion. A mandated formulae by itself may not be flexible enough to respond to unforeseen circumstances so some discretion is needed.
21. The document signals a rise in the price ceiling is likely. Given the need to link New Zealand prices to international prices the current \$25 price ceiling is not too low. Work commissioned by MFE from Sense Partners shows that New Zealand prices are at the higher end of the distribution when compared with other countries² which has implications for our emissions-intensive, trade exposed sectors (EITE) and economy generally. Analysis, including economic modelling is required to understand the impact of increasing the cap.
22. We agree that the proposed CCR system has advantages over the existing FPO but if implemented it is important that it not be used to curtail the number of units auctioned once the price ceiling is reached.
23. If the price ceiling is struck, we support the proposition of increasing the number of international units able to be purchased. A high domestic price is likely to be an indication of abatement costs in New Zealand being higher than overseas (see next section). The aforementioned work by Sense Partners, amongst other studies, confirms that mitigation in New Zealand is comparatively expensive.
24. We support the proposition in the document of reviewing the price ceiling if a significant event occurs such as a decision to link the New Zealand ETS with another carbon

² See [Sense Partners, 'Climate targets and implications for competitiveness, leakage and innovation'](#), page 50

market. Any review of the price ceiling should be done at least one compliance year in advance.

International Unit Proposals

25. While an international carbon market is not possible at this time, New Zealand's ETS must allow some trading in international carbon units. This would enable some sectors to meet targets by using emissions reduction from overseas and others, where we have a competitive advantage, to increase production and emit more efficiently. The units must, of course, meet accepted criteria for environmental integrity.
26. The document discusses the options of participants directly purchasing international units offshore compared with a model whereby the government purchases the units and onward sells them locally.
27. We think both pathways should be allowed. It is important that New Zealand ETS participants can purchase international units directly themselves at the international price as well as the government.
28. An indirect pathway whereby the New Zealand government buys the units and then auctions limited volumes would not necessarily reflect the price our competitors are facing which would be one weakness of this method.
29. There should be no volume limit on the trading of international units. Price should be the factor determining how many are purchased. If the units are genuine and have environmental integrity, they won't be underpriced. They may be lower than the New Zealand price but that is the point of a functioning trading system.

Industrial Allocation Proposals

30. Industrial allocations are free allocations of units to firms that carry out eligible industrial activities. They were introduced to mitigate the risk of carbon leakage.
31. The document seeks feedback on how decisions to phase down industrial allocation should be made.
32. There is an underlying assumption here that our trade competitors are taking similar actions to those being proposed, particularly around imposing similar levels of carbon pricing. However this is not the case and until such time as there is parity, free allocations to New Zealand's EITEs should remain.
33. Any phase down of industrial allocations would need to reflect what our trading partners are doing and be linked to the international carbon price. We should take a precautionary approach until it is clear how our trade competitors are going to act.
34. We suggest the phase down could be linked to an index measuring a cohort of regional CO₂ markets, perhaps specific to the industry/commodity in question. One suggestion

that should be considered is the model proposed (but not implemented) under the Australian Clean Energy Act which would have triggered a phase-down of allocated emission units when a set percentage of international competitors (70%) faced similar emission reduction measures.

35. We note that coal users in New Zealand (especially in the South Island) as well as other fossil fuel users, can only transition to other energy sources at significant cost, and those costs, given current options, would make many of those users uncompetitive. For example, Fonterra has recently indicated that converting a processing plant from coal to electricity would increase operating costs by about 50% and that replacing all of its coal-fired boilers with wood biomass would require access to a forest the size of Belgium every year to keep them running. To the extent that reductions in industrial allocations reduce coal usage, the industry would be adversely impacted with flow on effects particularly to the regional economies of Waikato, Canterbury, the West Coast and Southland.