

Proposed New Zealand Emissions Trading Scheme: Key Points

On 25th November, New Zealand passed an amended Emissions Trading Scheme into law. The original scheme, passed under the previous government, had already begun in 2009 for the forestry sector and was due to begin for several other sectors in January 2010. However, the new government, in response to the demands of several polluting industries, has pushed through an amended, and significantly weaker, scheme. What follows are the key elements of New Zealand's amended ETS.

Entry into the scheme

- 2009: Forestry
- June 2010: Stationary energy, industrial production (SEIP) and liquid fossil fuels (LFF)
- January 2015: agriculture

Allocation

- Free allocation to industrial, fishing and agriculture sectors, equivalent to 90% of 2005 emissions.
- Free allocation phased out at a rate of 1.3% per year from 2013 (2016 for agriculture).
- Allocation to 'energy intensive-trade-exposed' industry and agriculture (together accounting for between 55% and 60% of NZ's total emissions) is on an intensity-basis.

Transition phase

A transition phase will operate until December 2012. The transition phase will be implemented through:

- a progressive obligation requiring SEIP and LFF participants to surrender only one unit for every two tonnes of CO₂-e emitted
- a \$25 fixed price option whereby SEIP, LFF and forestry participants can satisfy surrender obligations by paying \$25 per unit.

The export of New Zealand units (NZUs) will not be permitted during the transition phase. However, the prohibition on exports will not apply to forestry-related units. There will be no restrictions on banking of units during the transition phase.

*"The Government currently has no plans to introduce any price controls after [the transition phase ends]. It is possible that this issue could be re-examined as part of the general review of the NZ ETS in 2011. If the NZ ETS is linked with the Australian CPRS a price cap may be necessary."*¹

*"All sectors will be permitted to bank units. This will allow firms in the SEIP, LFF and fishing sectors to sell units allocated to them in either the domestic or international markets at the end of the transition phase if they choose."*²

Implications

Agriculture accounts for 50% of NZ emissions. Delaying its entry into the scheme for 5 years will make it very hard for NZ to significantly reduce emissions by 2020.

¹ See: <http://www.mfe.govt.nz/publications/climate/emissions-trading-bulletin-11/index.html>

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Phasing out free allocation at a rate of 1.3% per year means that many NZ companies will still be receiving substantial free allocations beyond 2050.

The transition phase (2 for 1 deal + price cap) means that points of obligation will not receive a significant price signal for many years. The transitional price will be at most NZ\$12.50 per tonne. Ministry for Economic Development analysis shows that emissions will continue to increase in the transport and energy sectors even under a NZ\$25 carbon price.³

For the first 2.5 years of the scheme, free allocations will be significantly more than surrender obligations. Companies can bank these and, once the transition phase ends, either use them domestically to avoid making emissions reductions or sell them on international markets, thus having a potential downward impact on prices.

Un-capped intensity-based allocation means free allocations to agriculture and energy intensive trade-exposed industries (together accounting for between 55 and 60% of NZ's total emissions) will increase in line with increased production as long as the company/producer is at or below the industry average for emissions per unit of output. As the government's Regulatory Impact Statement (RIS) says, *"Under an intensity-based approach the number of units each firm receives will be updated each year to reflect changes in output levels, effectively reducing the price of carbon faced by those firms eligible to receive assistance... This change is likely to reduce the level of abatement from the scheme particularly beyond 2018 (when the current allocation is due to start phasing out). The RIS also states, "Protecting the competitiveness of more firms by providing a higher rate of assistance for a longer period will benefit eligible firms, but will come at a cost to the economy as a whole, by delaying the transition of the New Zealand economy to a carbon constrained world."*

The independent Parliamentary Commissioner for the Environment has stated that the proposed scheme *"has no chance of meeting [the government's] target of a 50% reduction of greenhouse gases by 2050."* This 50% target is itself significantly less than what is required of an industrialised country.

Conclusions

It is highly unlikely that the proposed ETS will make any contribution to New Zealand fulfilling its obligations under the first commitment period of the Kyoto Protocol. In fact, there is a strong likelihood that emissions will increase in the early years of the scheme. It is also unlikely that the scheme will make any significant contribution to New Zealand meeting any new 2020 targets that will be set through the current UNFCCC/Kyoto Protocol negotiations. As the RIS points out, intensity-based allocation in particular exposes the government to increased liability risk in the Kyoto Protocol and beyond; *"Both the transition phase and the intensity-based allocation shift some of the costs of New Zealand's international liability from emitters to the crown, and subsequently increase the risk to the Crown. This is a particular risk for intensity-based allocation. If the cost is on emitters, emitters have the choice as to whether to purchase permits to cover their emissions, reduce output or invest in mitigation options. The Crown has fewer options for managing emissions, and will be liable for any emissions that exceed the level of emissions specified in Kyoto and successive agreements."*

The amended ETS will not set New Zealand on a path to a low-carbon economy, make a contribution to tackling climate change, or help New Zealand meet its Kyoto obligations. What analysis exists suggests it may in fact see New Zealand's emissions increase, and it will instead provide a substantial effective subsidy to the largest polluters towards the true cost of greenhouse gas emissions.

Together with recent statements by New Zealand negotiators in Bangkok that New Zealand expects to meet up to 70% of its reduction target through buying credits from overseas,⁴ it presents a picture of a country trying to avoid responsibility and maintain business as usual.

³ MED. (2007). *Benefit-Cost Analysis of the New Zealand Energy Strategy*. November 2007. Ministry for Economic Development. Pages 5-4 and 6-4

⁴ IISD. (2009). *Earth Negotiations Bulletin* Vol.12 No.435, Tuesday 6 October 2009. International Institute for Sustainable Development (IISD).