

Matters that the Minister must consider when recommending limits and price control settings for units

Section 30GC of the Climate Change Response Act 2002 (the Act) requires that you be satisfied that the limits and price control settings are in accordance with items listed in 30GC(2)

(2) (a) the emissions budget, and the nationally determined contribution for New Zealand under the Paris Agreement, that applies to—

(i) the period for which the limits or price control settings are being prescribed; or

(ii) any period after that, if a budget or contribution exists for that period; and

(b) the 2050 target.

(3) However, they need not strictly accord with the budgets or contributions as long as the Minister is satisfied that the discrepancy is justified, after considering the other matters under this section.

The proposals accord with the emissions budgets that were set in May 2022. These budgets are set with a view to meeting the 2050 target, which means that accordance with these budgets is akin to accordance with the 2050 target. The calculation of limits and auction volumes is designed so that all units supplied within these limits are from within the emissions budgets.

Additionally, the update to the calculation of the cost containment reserve volume means that this will no longer include supply that may result in the emissions budget being exceeded. The price controls are consistent with those in the Commission's *Ināia tonu nei* advice, and the Commission has confirmed that these remain its best estimate of the abatement costs associated with meeting budgets¹.

Accordance with New Zealand's nationally determined contribution (NDC) under the Paris agreement needs careful consideration. Government has indicated that offshore mitigation will contribute to meeting the NDC. Proposed settings are in accordance with the NDC on the assumption that offshore mitigation becomes available.

Additionally, the severe social and economic risks of limits in line with the NDC, without consideration of the role government has signalled will be played by offshore mitigation, would mean that after consideration of other matters the settings should not be set to achieve NDC via domestic emissions reductions only.

The proposed price control settings enable prices that align with the Climate Change Commission's best estimate of the abatement costs associated with meeting emissions budgets and the 2050 target.

Section 30GC also requires that you consider the main matters listed in s30GC(5) when recommending the limits and price control settings for units. These are described below.

¹ See, e.g., page 50 of the Commission's advice on NZ ETS unit settings: [NZ ETS settings for 2023-2027 \(amazonaws.com\)](https://amazonaws.com)

5(a) the projected trends for New Zealand's greenhouse gas emissions in the 5 years after the current year, including—

- (i) the anticipated volumes of greenhouse gas emissions to which the emissions trading scheme applies (meaning emissions for which participants are required to submit returns or surrender units under this Act); and*
- (ii) the anticipated volumes of greenhouse gas emissions to which the emissions trading scheme does not apply:*

The recommended settings are consistent with the most recent projected trends for New Zealand's greenhouse gas emissions in the 5 years after the current year, including the volumes of greenhouse gas emissions to which the emissions trading scheme applies and to which the emissions trading scheme does not apply. Auction volumes, which are an input to limits for units, are calculated with reference to projected emissions and emissions budgets.

5(b) the proper functioning of the emissions trading scheme

The recommended settings are consistent with the proper functioning of the emissions trading scheme. They support alignment of the NZ ETS unit limits and price control settings with the first emissions budgets.

Additionally, the supply of NZUs via auction supports people meeting their obligations to surrender units for their reported emissions. The upper and lower price control settings act to mitigate the risk of NZU prices reaching unacceptably high or low prices.

5(c) international climate change obligations and instruments or contracts that New Zealand has with other jurisdictions to access emissions reductions in their carbon markets

The recommended settings are consistent with New Zealand's international climate change obligations, including New Zealand's NDC. New Zealand has no current instruments or contracts with other jurisdictions to access emissions reductions in their carbon markets.

5(d) the forecast availability and cost of ways to reduce greenhouse gas emissions that may be needed for New Zealand to meet its targets for the reduction of emissions

The recommended settings are consistent with the forecast availability and cost of ways to reduce greenhouse gas emissions that may be needed for New Zealand to meet its targets for the reduction of emissions. It is, however, worth noting that there are some limitations to the information available on emissions reductions available and how these respond to emissions trading scheme pricing.

Details on the cost of offshore mitigation to support meeting New Zealand's NDC remain unknown.

5(e) the recommendations made by the Climate Change Commission under section 5ZOA of the Act:

The Commission has provided advice on settings under section 5ZOA and this advice is available on the Commission's website. All recommendations from the Commission were canvassed as part of public consultation, considered by MfE in its regulatory impact assessment, and have been duly considered.

The Commission's advice on adjusting limits for units to address the 'surplus' component of the stockpile of privately held units have been followed. Additionally, the Commission's advice to set the volume of the cost containment reserve as equal to this 'stockpile reduction adjustment' has been followed.

Other updates to settings vary from the Commission's advice

5(f) any other matters that the Minister considers relevant.

The emissions reduction plan was agreed in May 2022. The actions within this plan are matters that the Minister considers relevant and these have been considered.

Section 30GC requires that you also consider the additional matters listed in s 30GC(6) when recommending price control settings for units.

The *additional matters* are as follows:

6(a) the impact of emissions prices on households and the economy

The recommendations on price control settings are made after considering the impact of emissions prices on households and the economy. Price controls are not intended to be major drivers of price movement on the NZ ETS secondary market, however it is noted that prices have been observed to rise towards the upper price control. While the likely change in NZU prices in response to changes to settings cannot be predicted, impacts of any price increases on households and the economy have been considered.

Given that the updates do not result in unit settings that vary much from the status quo, the impacts of the updates are expected to be negligible.

6(b) the level and trajectory of international emissions prices (including price controls in linked markets)

The recommendations on price control settings are made after considering the level and trajectory of international emissions prices. The recommended price control settings will support domestic emissions prices in line with those in overseas carbon markets, which New Zealand may link with in the future. These prices vary significantly, ranging from below \$30 a tonne for allowances in the Korean scheme to \$150 a tonne in the United Kingdom's scheme.

6(c) inflation.

The recommendations on price control settings are made after considering inflation. The recommended price control settings include annual increases to account for inflation. These annual increases have been updated to reflect recent increases in the rate of inflation and projected inflation.

As described above, price controls are not the major driver of price movement on the NZ ETS secondary market. It is noted that prices have been observed to rise towards the upper price control. The inflationary impacts of any such increase of NZU prices are difficult to quantify and have been considered as part of the overall impacts on the economy.