



**Emissions Trading Scheme**  
**REVIEW 2011**

**ETS Review 2011**

**Summary of submissions**

This report can be cited as: ETS Review Panel. 2011. *ETS Review 2011 Summary of submissions*. Ministry for the Environment. Wellington

Published in August 2011  
by the Ministry for the Environment  
for the ETS Review Panel

ME 1062

This publication is also available at [www.climatechange.govt.nz](http://www.climatechange.govt.nz)

# Contents

<b>1</b>	<b>Introduction .....</b>	<b>1</b>
<b>2</b>	<b>Impacts of the ETS .....</b>	<b>2</b>
	Panel's assessment of current impacts (Question 1) .....	2
	Impacts experienced to date (Question 2) .....	5
	Macroeconomic impacts after 2012 (Question 4) .....	10
	Panel's assessment of impacts after 2012 (Question 5) .....	12
	Expected impacts after 2012 (Question 6) .....	12
<b>3</b>	<b>Impacts of the ETS on Māori.....</b>	<b>19</b>
	Panel's assessment of the impacts on Māori (Question 8) .....	19
	Impacts at a sector level (Questions 9 and 10) .....	19
	The concentration of Māori interests in forestry .....	20
	Impacts at a whanau level .....	26
	Impacts on the Māori households.....	27
<b>4</b>	<b>International framework and objectives of the ETS .....</b>	<b>28</b>
	Future international framework (Question 11).....	28
	Implications for the objectives of the ETS (Question 12) .....	30
<b>5</b>	<b>Transition phase .....</b>	<b>41</b>
	Scaling the ETS up to full obligation (Question 13) .....	41
	Fixed price option (Question 13a) .....	45
	One-for-two obligation (Question 13b).....	48
	Importance of certainty about the transitional phase .....	50
	Amendments to industrial allocation if the transition phase is not extended .....	50
	Price floor .....	50
	Other comments about the transition phase.....	50
<b>6</b>	<b>Agriculture .....</b>	<b>51</b>
	The extent of agriculture sector abatement options (Question 14) .....	51
	Conditions under which the agriculture sector should enter the ETS (Question 15) .....	60
	Other comments about agriculture in the ETS.....	64
<b>7</b>	<b>Waste.....</b>	<b>65</b>

	Arguments for and against retaining current ETS entry date (Questions 14 and 15).....	65
	Arguments on the coverage of the waste sector in the ETS .....	66
	Other comments about waste in the ETS.....	66
<b>8</b>	<b>Synthetic greenhouse gases .....</b>	<b>68</b>
	Arguments for and against retaining current ETS entry date (Questions 14, 15 and 17) .....	68
	Alternative measures .....	70
	Allocation issues for SGG.....	71
<b>9</b>	<b>Forestry.....</b>	<b>72</b>
	ETS incentives for forestry investment (Question 7).....	72
	Other comments about forestry in the ETS.....	79
	The impact forestry’s inclusion in the ETS has had on biodiversity .....	80
<b>10</b>	<b>Allocation .....</b>	<b>82</b>
	Allocation settings after 2012 (Question 16) .....	82
	The effectiveness of allocation in reducing competitiveness risks or carbon leakage (Question 16a).....	86
	Impact of allocation on incentives to reduce emissions (Question 16b).....	89
	Allocation thresholds (Question 16c).....	91
	The process for determining allocative baselines (Question 16d).....	94
	Efficiency of allocation to SMEs (Question 16e).....	94
	Other comments about allocation .....	95
<b>11</b>	<b>Operation of the ETS .....</b>	<b>97</b>
	Compliance costs associated with the ETS (Question 3a).....	97
	Complexities of ETS reporting requirements (Question 3b) .....	98
	Penalties for breaching ETS obligations (Question 3c).....	100
	Government administration of ETS and the role of the Environmental Protection Authority (Question 3d).....	101
	Other comments about ETS administration.....	102
<b>12</b>	<b>Other issues (Question 18) .....</b>	<b>103</b>
	Climate change science .....	103
	Measurement of New Zealand’s emissions position.....	103
	Public interest in climate change .....	103
	Climate change negotiations .....	103
	General comments on the ETS .....	103

Purposes of the ETS .....	104
Fair share .....	104
Emission reduction targets .....	105
Overseas action .....	105
Eligible emission units .....	105
Fossil fuels .....	106
Other transition measures .....	106
GST treatment of NZU transactions .....	107
Relief from the ETS costs in certain circumstances .....	107
Information issues .....	107
Entering contracts with private actors .....	107
Offset mechanism.....	107
Complementary measures and alternative policies.....	108
Using NZUs to pay for increased electricity costs .....	109
Market liquidity .....	109
Process for the ETS Review.....	109

# 1 Introduction

At the ETS Review 2011 Panel meeting on 3 May 2011 a draft summary of submissions was provided (Panel Paper 1). This is the final version of the summary of submissions.

In March 2011, the ETS Review Panel published its *Issues statement and call for written submissions* (the *Issues Statement*). The closing date for submissions was 6 April. This Panel paper summarises the 162 written submissions received in response to the *Issues statement*. It should be noted this paper is only a summary and does not cover every single comment made by each submitter. If further detail of a specific submitter's submission is needed then their submission should be read instead.

The names of some submitters that asked not to be named are also included. These names will be withheld before this summary is published.

## 2 Impacts of the ETS

### Panel's assessment of current impacts (Question 1)

A number of submitters made comments on the Panel's assessment of the impacts of the ETS to date. Some agreed and made no further comments, a number disagreed with components of the assessment, and their reasons are outlined in more detail below. Some submitters felt that the Panel had not provided enough background to their assumptions and figures for them to adequately assess them.

#### Agreed with the Panel's assessment

Numerous submitters agreed with the Panels assessment of impacts to date and made no further comment. [Oregon Group (080), Escea (006), Southern Forestry (029), Marlborough Forest Industry Association (030), Contact Energy (089), Meridian Energy (092), Nelson Forests (098), Pacific Shipping (041), OMFinancial (047), NZ Sugar Company (103), Environment and Conservation Organisations of NZ (161)]

Some agreed generally with the Panel's assessment but made additional comments:

- Impact is beyond input costs, compliance costs and emissions reductions [Wairakei Pastoral (056)]
- The ETS goes beyond its immediate impact on transactions. It encourages people to take action voluntarily, such as driving less, driving a smaller car, installing insulation and installing solar power [Euan Mason (108)]
- The impacts being very significant for energy intense firms has not been stated [Ballance Agri-Nutrients (048)]
- There is no real assessment of the indirect costs of the scheme to consumers and taxpayers [Carbon Farm (102)]

#### Disagreed with the Panel's assessment

A number of submitters disagreed with aspects of the Panel's assessment of impacts set out in its *Issues Statement* for the reasons outlined below.

##### ***Disagreed with the estimated impact on fuel and electricity prices***

Talleys (007) noted that the actual ETS impact on petrol and diesel, and electricity prices has been much greater than the figures presented in the *Issues Statement*. The WWF NZ (055) noted that the estimated ETS cost impact on petrol prices differed from estimates produced by AA petrol watch, which shows prices were unchanged and that electricity prices increased more before the ETS was introduced than afterwards, making it difficult to disaggregate ETS impacts from other factors that influence price.

### ***Disagreed with the cost impacts on business***

Some submitters noted that the increase in their business costs from higher fuel and energy costs is significantly greater than the average figure (of 1 per cent of revenue) presented in the *Issues Statement* [Qualityarns (033), Horticulture NZ (148), [withheld] ].

BusinessNZ (149) noted that characterising the ETS cost as a small proportion of revenue hides the fact that for those businesses which face an elastic demand curve any cost increase will reduce profits, in turn reducing the rate of return and investment opportunities. Holcim (112) noted that the ETS cost impact should be measured against margins, rather than revenue.

Comparing the ETS cost impact on businesses to other cost increases (e.g. labour) is generally invalid as the incentives provided by each increase are quite different and other costs may be faced by international competitors as well, unlike the ETS costs [BusinessNZ (149), Genesis (053), Fletcher Building (076), Northland Regional Council (069), Climate Realists (050), Seafood Industry Council (065), NZ Pork (068), Employers & Manufacturers Association (070), Ballance Agri-Nutrients (048)]. Holcim (112) noted that ETS costs should not be compared with oil price increases because oil price increases affect all players globally, while unilateral emissions costs are asymmetric.

Methanex (105) argued that the implications of adjustment costs and lags, the potential for persistent contraction/stagnation and the prospect of step changes to a lower economic equilibrium caused by capital/labour mobility and potential reductions in capital /labour productivity have not been adequately addressed.

### ***Disagreed with statements about the current state of New Zealand's economy***

Several submitters commented on the current fragile state of the New Zealand economy [Methanex (105), Steve Wrathall (018)]. David Slack (008) blamed the ETS for being partially responsible for causing New Zealand's double dip recession.

### ***Disagreed with the impacts on forestry.***

Piers Maclaren & Associates (034) noted that the problem with forestry is not that forestry emissions are cyclical but rather that New Zealand has allowed an imbalance in the age-class structure to appear in the forest estate.

Climate Realists (050) disagreed that the increase in afforestation from 2010 is due to the ETS. The submitter also notes that there was increased deforestation in 2006 and 2007 because of companies removing forests prior to facing ETS liabilities from 2008 onwards. In addition, plantings fell due to uncertainties about how the ETS was going to affect forestry. Current planting is therefore only making up for lost time.

### ***Disagree with the impact on farmers***

A number of submitters said the ETS impact on farming costs should be compared to net revenue or average bottom line, rather than working expenses [Holcim (112), Greenhouse Policy Coalition (114), Fonterra (120)]. Fonterra (120) said it would be more appropriate to compare the ETS costs for an average dairy household with the annual ETS costs for other households. Several submitters said the

presentation of on-farm costs from the ETS in the modelling is misleading (Greenhouse Policy Coalition (114), Pastoral Farming Climate Research (131)). Wairakei Pastoral (056) noted the *Issues Statement* does not take into account the cost to farmers of obtaining advice on the ETS.

### ***Regional and sector impacts not adequately addressed***

Several submitters argued sector or regional impacts were not adequately addressed [Methanex (105), Fletcher Building (076), Greenhouse Policy Coalition (114)].

### ***Disagreed with the environmental impacts of the ETS***

Environment and Conservation Organisations of NZ (161) argued the scope for adjustment is understated and the cost impact of the ETS is over-stated. The submitter also argued that cost of inaction (in terms of the liabilities New Zealand will face if it exceeds the 1990 emissions target) should also be counted as well as the cost of action.

### ***Disagreed with the basis of the estimates presented***

A number of submitters raised concerns about the ETS impact estimates presented in the *Issues Statement*. For example, they were generalisations, or averages, or based on old modelling work, or lacked evidence and assumptions used [WWF NZ (055), Qualityarns (033), Seafood Industry Council (065), Lake Taupo and Lake Rotoaira Forest Trusts (142), Methanex (105), Environment and Conservation Organisations of NZ 161]].

### ***Other impacts should have been considered***

Some submitters suggested the Panel should have focused on or provided information on other impacts, such as:

- future council rates, given the impact on land values [South Waikato District Council (044)]
- renewable power generation [Greenhouse Policy Coalition (114)]
- the coal sector, given that it is a major source of energy in the South Island and there are currently no alternatives available [Rockies Mining (024), NZ Coal & Carbon (111), Coal Association (132)]
- the inequitable rise in wages versus further inflation as a result of the ETS [NZ Coal & Carbon (111)]
- the potential opportunity cost to the economy of lost investment [Holcim (112)]
- the inequity of the distribution of costs and impacts of the ETS to date [Sustainability Council (151), Coal Association (132)]
- the fairness of the current ETS, e.g. imposing a huge burden on the future and on those who are not able to respond by reducing their emissions [Environment and Conservation Organisations of NZ (161)]

- the integrated forestry and wood processing sector's viability, as any decline in local wood processing capacity could lead to a reduction in new forest planting [NZ Institute of Forestry (119)].

The Sustainability Council (151) thought the *Issues statement* provided an inadequate basis for review of the ETS as it did not provide enough quantitative data or adequate forward forecasting, nor did it provide an appropriate structure for analysis. It also raised a number of specific issues in relation to the Panel's assessment.

## Impacts experienced to date (Question 2)

### Overview

Almost all submissions commented on how the ETS had impacted on them directly. A number of submitters commented that it is too early to review the ETS and/or that there is not enough information available to quantify accurately its impacts to date and expected impacts.

Most submitters commented on the impacts they had experienced to date. A number of general themes emerged and a number of sectors or companies also raised specific issues.

A number of submitters noted that the cost impacts have been minor, with some reporting that the ETS has had a positive impact on their business.

Submitters noted that the ETS cost increases might be small compared to other price drivers but they are significant for some businesses and the costs are different because they are discretionary.

An increase in energy prices due to the ETS was seen as an issue for a number of submitters, and is a particular issue for coal users in the South Island where alternative energy sources are limited.

Energy intensive sectors who are trade exposed but do not qualify for ongoing allocation such as the fishing sector are feeling significant impacts of increased energy prices. In addition, some companies who receive 90 per cent allocation are still facing pressure because of increases in energy prices.

The submitters also made comments on:

- How they are treating the costs i.e. passing on or absorbing costs
- Competitive risks that the ETS is creating
- How the ETS is influencing investment decisions, and that uncertainty is limiting investment.

A number of comments were made about the costs being inequitable across sectors.

While the majority of submitters focused on the economic or financial impacts other impacts that were mentioned include:

- Environmental impacts
- Social impacts
- Impacts on householders

## Impacts on business

A number of submitters commented that it is too early to review the ETS and/or that there is not enough information available to quantify accurately its impacts to date and expected impacts. [WWF NZ (055), Seafood Industry Council (065), Carter Holt Harvey Pulp & Paper (040), Straterra (084), GL Bowron & Co (074), Fletcher Building (076), Wellington City Council (058), BusinessNZ (149), Holcim (112), Origin Energy (122), Bank of New Zealand (124)]

A number of submitters felt that the impacts to date have been modest. One submitter noted that to date the impact has been material but manageable. [Escea (006), WWF NZ (055), OMFfinancial (047), Bank of New Zealand (124), Bioenergy Association (138), Nelson Forests (098), Greenhouse Policy Coalition (114), Southern Forestry (029), Carbon Farm (102), BusinessNZ (149), Wellington City Council (058), Northland Regional Council (069), NZ Sugar Company (103)]

Some submitters noted that the ETS has had a positive impact on their business, such as the forestry sector and clean energy businesses. [Escea (006), Southern Forestry (029), Taumarunui Sustainable Land Management Group (031), Contact Energy (089)]

A number of submitters noted that the price of energy inputs had increased as a result of the ETS. [Straterra (084), Nova Trust (066), KiwiRail (086), NZ Pork (068) Seafood Industry Council (065), Cavalier Wool Holdings (038), Taumarunui Sustainable Land Management Group (031), Coal Association (132)]

Numerous submitters noted that the energy cost increase due to the ETS had had a significant impact on their business. This was also the case for businesses that had received allocation, although allocation had relieved some of the impact. Some submitters provided data on the cost increases experienced and/or the impact this has had on their profitability or investment decisions. [Methanex (105), Fletcher Building (076), Qualityarns (033), Cavalier Wool Holdings (038), Talleys (007), Pacific Shipping (041), Horticulture NZ (148), Holcim (112), TA & DM Turner (127), Beef + Lamb New Zealand, the Meat Industry Association and Dear Industry New Zealand (107), [withheld] (121), Fonterra (120), ExportNZ (104), Ballance Agri-Nutrients (048), Horticulture NZ (148), NZ Steel (135), [withheld], Carter Holt Harvey Pulp & Paper (040)]

A number of submitters raised concerns about the increase in coal prices. The ETS imposes significant cost on the coal mining sector, particularly from liability associated with fugitive emissions of methane. Some argued that this cost increase cannot be passed on to customers, as customers would switch to imported coal. Others argued that there was limited ability for coal users to switch from coal to other fuels. [NZ Coal & Carbon (111), Rockies Mining (024), [withheld], [withheld], Coal Association (132), Heaphy Mining (128), Gelita (017), Horticulture NZ (148)]. Some coal users noted that they had seen a significant increase in their coal costs [Sylait Milk (046), Tony Norton (036)]

Other submitters noted that the ETS had increased the cost of local goods and services [Carter Holt Harvey Pulp & Paper (040), GL Bowron & Co (074), ALSCO NZ (057), Employers & Manufacturers Association (070)].

Greenpeace (085) noted that subsidies to emissions-intensive firms and other domestic settings will lock in investment in polluting activities. Eventually this will be fiscally and economically unsustainable.

The fisheries sector noted that they have experienced increases in their fuel costs (some also provided estimates) but had not received any form of assistance despite being trade exposed. It was also noted that there have been few quota trades since the introduction of the ETS so it was not possible to assess the impact on quota prices. [Talleys (007), Seafood Industry Council (065), Sanford (156)]

## **Business responses to increased costs**

A number of submitters noted they, or their suppliers, were primarily passing on part or all of the costs associated with the ETS [Kiwirail (086), BOC (032), [withheld]]. One submitter noted that businesses more generally seem to be able and willing to pass on ETS costs to consumers without any real impact [Bank of New Zealand (124)].

Other submitters noted they (or firms they were aware of) had absorbed all of the extra costs imposed by the ETS for a range of reasons. For some it was because a large proportion of their products are exported and/or open to import competition. For others it related to other competition constraints or contractual arrangements. [Bowron Sheepskins (74), Wairakei Pastoral (056), Carter Holt Harvey Pulp & Paper (040), Cavalier Wool Holdings (038), Methanex (105), Beef + Lamb New Zealand, the Meat Industry Association and Dear Industry New Zealand (107), TA & DM Turner (127), Holcim (112), [withheld] (121), Seafood Industry Council (065), BusinessNZ (149), Qantas (158), Origin Energy (122)]

[withheld] was concerned that the increase in electricity prices attributed to the ETS may be more than the current price of emission units. As a result this reduced the benefit of free allocation and potentially enables a windfall gain for upstream electricity suppliers.

## **Competitive risks**

A number of submitters raised issues around the effect the ETS has had on their competitiveness or on New Zealand's competitiveness in general. [Horticulture NZ (148), Seafood Industry Council (065), Tony Norton (036), NZ Coal & Carbon (111), ExportNZ (104), Carbon Farm (102), [withheld] (121), Taumarunui Sustainable Land Management Group (031)]

## **Impact on investment decisions**

Numerous submitters noted the ETS has had an impact on their investment decisions or on business investment decisions more generally. This is because the return on such investments had increased as businesses factor in a cost on emissions. For example the ETS had impacted on investment decisions to improved energy efficiency, use of renewable energy, the waste sector and forestry. [Carter Holt Harvey Pulp & Paper (040), Oregon Group (080), Fletcher Building (076), Wellington City Council (058), Contact Energy (089), Meridian Energy (092), Ballance Agri-Nutrients (048), Mighty

River Power (130), Rio Tinto (094), BusinessNZ (149), Holcim (112), Carbon Farm (102), Southern Forestry (029), Genesis (053), Fletcher Building (076), Richard Leckinger (096)]

Some noted the ETS has had a negative impact on business investment decisions. This was because production had moved offshore, it had become more difficult to attract investment in New Zealand operations, or overseas investments are being considered instead. [GL Bowron & Co (074), [withheld]]

Other submitters said the ETS has had little impact on their investment decisions or on business investment decisions more generally. Numerous reasons were provided for this, such as the provision of free allocation, current low carbon prices and business expectations for these prices to remain low, uncertainty around the future of the ETS, and limited abatement options. [Greenpeace (085), 350 Aotearoa (064), Nelson Forests (098), Beef + Lamb New Zealand, the Meat Industry Association and Dear Industry New Zealand (107), BusinessNZ (149), Horticulture NZ (148), Wairakei Pastoral (056), Bank of New Zealand (124)]

The Sustainability Council (151) said it is uncertain whether the ETS has made a material difference to the mix of future power stations. Pacific Shipping (041) noted while the ETS has not had a significant impact on investment decisions to date it is likely that it would do so in future.

### **Impact on operation decisions**

A number of submitters discussed the impact the ETS was having on their operational decisions. One argued that it had had no impact yet [Seafood Industry Council (065)]. Another noted that the ETS has reinforced operating decisions that were already well established [Holcim (112)].

### **Impact on forestry and land use investments**

Some submitters said the ETS had influenced further investment in forestry as forest owners gain revenue. This has reduced the conversion of land from plantation forest to pastoral farming. [Oregon Group (080), Wellington City Council (058), Waikato Regional Council (072), Southern Forestry (029)]

Others noted the ETS has had minimal impact on new planting rates/afforestation and any increase that has occurred may reflect the increase in log export prices or other Government forestry schemes. Some said that the ETS will do little for afforestation until landowners believe the carbon price has stabilised and there is an international carbon market in place. [NZ Farm Forestry Association (039), NZ Institute of Forestry [119]].

Others noted the loss of land use flexibility for pre-1990 forests. In particular, it was noted that there was a negative impact on the primary sector as the land is locked into forestry even if a higher return could be earned under another use, such as pastoral farming. Several submitters also noted that the compensation paid to pre-1990 forest owners, in the form of allocation, was inadequate. [Wairakei Pastoral (056), South Waikato District Council (044), NZ Institute of Forestry (119), Fonterra [120]]

## Equity considerations

A number of submitters raised concerns about equity of the ETS in terms of sectors receiving allocation and how its impacts are distributed. For example:

- Several submitters argued that the current allocation rules resulted in inequities between sectors and needed to be revisited [Seafood Industry Council (065), Vector (097), NZ Coal & Carbon (111)]
- The ETS disadvantages smaller, less resourced councils as it imposes unrealistic costs on smaller landfills [South Waikato District Council (044)]
- The ETS is missing natural justice (equity) as agriculture contributes to 50 per cent of emissions but pays only indirect costs [Qualityarns (033)]
- The ETS disadvantages those firms that had already made investments to reduce their emissions relative to those who have not [NZ Institute of Forestry (119)]
- Dairy farmers carry an inequitable share of the ETS costs as an average dairy farming household bears ETS costs of more than five times the average New Zealand household. This disparity will increase once agricultural gases enter the scheme [Fonterra (120)]
- Households and small and medium sized businesses are responsible for a disproportionately large share of the ETS costs [Sustainability Council (151)]
- Under the current ETS, most of the Kyoto Protocol liability would be transferred to future taxpayers [Sustainability Council (151)]
- South Island horticulture growers, because of their need for more heating, are at a significant disadvantage to North Island growers [TA & DM Turner (127)].

## Social impacts

Some submitters raised concerns about the impacts on communities and low socio-economic households. For example,

- The ETS impacts on essential public services, such as hospitals and schools, because of higher energy costs [Rockies Mining (024), NZ Coal & Carbon (111)]
- The complex and abstract nature of the ETS means the public is often critical and sceptical. Assisting councils to provide more tangible on-the-ground benefits would be a way of building long term, broad-based political support for the scheme [(Hamilton City Council (028)]
- The ETS does not have any demonstrated social outcomes, and will not have any while design elements such as the absence of a cap, over-allocation of free emissions units to businesses and the transition measures remain in place [Carbon Farm (102)]
- Householders will bear half the costs under the ETS for the first 5 years, while accounting for a fifth of all emissions [Sustainability Council (151)]

- The economic effect of the ETS is to lower living standards by increasing the price of commodities [Simon Breeze (021)]
- More needs to be done to alleviate the impact on low-income households [Richard Leckinger (096), Environment and Conservation Organisations of NZ (161)].

In contrast, two submitters said afforestation, to the extent that the ETS encourages this, should be seen as an asset as it contributes to the economic, social and environmental wellbeing of a region [South Waikato District Council (044), NZ Farm Forestry Association (039)].

## **Emission and other environmental impacts**

Many submitters noted that the ETS had had no or only a limited impact on reducing emissions. Some provided reasons as to why this may be the case. These included the current low carbon prices due to the transition measures and it was too soon to measure an impact. [Seafood Industry Council (065), WWF NZ (055), Steve Wrathall (018), Raymond Scampton (025), Contact Energy (089), Sustainability Council (151), Lake Taupo and Lake Rotoaira Forest Trusts (142), Arthur Thorstensen (009), Carbon Farm (102), Greenpeace (085)].

Two submitters argued the impact on emissions is the most important consideration as this is the whole purpose of the ETS [WWF NZ (055), Steve Wrathall (018)]. Richard Leckinger (096) noted that the ETS will come nowhere near the Government's target for emissions reductions.

Mighty River Power (130) said the ETS is resulting in emissions reductions through renewable power developments that have significantly displaced coal generation and by encouraging new forest plantings.

Contact Energy (089) noted that, whilst the ETS may have had little impact to date it is a key step in developing a platform for future change.

## **Macroeconomic impacts after 2012 (Question 4)**

### **Comments on the modelling**

Numerous submitters raised concerns about the modelling results referred to in the *Issues Statement*. [WWF NZ (055), Sustainability Council (151), BusinessNZ (149), Greenhouse Policy Coalition (114), Seafood Industry Council (065), Escea (006), Southern Forestry (029), Craigmore Forestry (144), NZ Steel (135), Methanex (105), Beef + Lamb New Zealand, the Meat Industry Association and Dear Industry New Zealand (107), Euan Mason (108), Coal Association (132), Straterra (084), Oregon Group (080), Wairakei Pastoral (056), Carbon Farm (102), Carter Holt Harvey Pulp & Paper (040), GL Bowron & Co (074), Employers & Manufacturers Association (070), Motu Economic and Public Policy Research (139), Environment and Conservation Organisations of NZ (161)]

These concerns included:

- an assumption there is no technology change
- the focus on economy-wide costs and benefits rather than sector-specific or regional impacts
- the appropriateness of the carbon prices assumed
- the need to take account of actions taken by New Zealand's key competitors
- a lack of information on the assumptions used and a lack of recognition of the limitations of such models
- the difficulties of estimating land use change from agriculture to forestry at very high carbon prices.

Two submitters noted that economic models have a role in predicting the long-term economic impact of a carbon price. However their limitations mean they are not well suited to advising policy makers about the short-term economic adjustments [BusinessNZ (149), Fletcher Building (076)].

Greenpeace (085) also submitted that the macroeconomic impacts of the ETS will depend largely on the quality of Government decisions on complementary measures, and that availability of substitutes will lower the macroeconomic impact of the ETS.

## **General economic comments**

Many submitters noted the current difficulties the New Zealand economy faces as a result of the global financial crisis and the Christchurch earthquakes. This makes it difficult for businesses to absorb additional costs [NZ Business Roundtable (083), Fletcher Building (076), Holcim (112), Methanex (105), [withheld] (081)].

Greenpeace (085) noted that if the ETS reduced New Zealand's wealth then this will make closing the income gap with Australia even harder [Steve Wrathall (018)]. Another argued that if the carbon price reached \$100 then there would be a drastic decline in New Zealand's economy - there would be no New Zealand manufacturing [Rockies Mining (024)]. Another argued that to reduce the costs of adjustment then Government policies should assist this process rather than work against it.

Hamilton City Council (028) noted the impact of the ETS on GDP is relatively slight compared to the impacts of the recession, the Christchurch earthquakes, Government expenditure cutbacks, exchange rates and international prices [Environment and Conservation Organisations of NZ (161)]. Another noted the notion of the ETS negatively impacting the economy is false; it should aim to shift modes of production and if it doesn't achieve this it is not effective [350 Aotearoa (064)]. Another submitter said provided that carbon is priced appropriately then the ETS should drive dynamic efficiency gains in the long term.

BusinessNZ (149) believed New Zealand's relatively unique factors, such as the availability and cost of abatement technologies, are likely to mean the ETS transitions to a high price, low emissions reduction world.

## **Panel's assessment of impacts after 2012 (Question 5)**

Some submitters broadly agreed with the Panel's assessment of the expected impacts of the ETS after 2012. Others agreed with the Panel's assessment to some extent but made some additional comments. [Contact Energy (089), Nelson Forests (098), OMFinancial (047), Craigmore Forestry (144), Carbon Farm (102), Origin Energy (122), Holcim (112), Rockies Mining (024), Environment and Conservation Organisations of NZ (161), Ballance Agri-Nutrients (048), NZ Steel (135), Greenhouse Policy Coalition (114), Bank of New Zealand (124), Carbon Market Solutions (145), BusinessNZ (149)]

These additional comments included:

- the risk that New Zealand businesses may be exposed to very high carbon prices after 2012 is not considered
- forecasts beyond 2012 cannot be made accurately given the range of complex variables at play
- behaviour change will be slow if industry is shielded from the full costs.

A number of submitters disagreed with the Panel's assessment and made a number of comments in this regards. [Simon Breeze (021), Fletcher Building (076), WWF NZ (055), Sustainability Council (151), BOC (032), Richard Leckinger (096), NZ Farm Forestry Association (039), Oregon Group (080), Climate Realists (050), Carter Holt Harvey Pulp & Paper (040), Coal Association (132)]

These comments included:

- the Panel's forestry assumptions were too optimistic, whereas others said they were too pessimistic
- the carbon price assumed was too low and that this was likely to rise substantially (up to \$50) once all sectors are included and all allocations are removed
- a simplistic view of the impacts on the SGG sector is presented
- regional and sector-specific impacts need to be considered

Some submitters felt the Panel hadn't focused enough on the expected benefits of the ETS, such as job creation, the transition away from the reliance on fossil fuels, environmental benefits and the economic impacts of climate change. [WWF NZ (055), Hamilton City Council (028)]

## **Expected impacts after 2012 (Question 6)**

### **General expectations after 2012**

A number of submitters commented on how the ETS will impact negatively after 2012 primarily in relation to reduction in economic output/growth. [Simon Breeze (021), David Slack (008), BusinessNZ (149), [withheld] (049), Seafood Industry Council (065), Talleys (007)]

BusinessNZ (149) identified a number of other factors that will affect the ability of New Zealand to reduce its emissions after 2012. These factors included New Zealand's population growth and that many New Zealand emitters already operate at world's best practice so there is limited opportunity to reduce emissions.

Others believe ETS costs will remain small compared to other economic changes, such as oil prices, or will be moderated by access to international markets [WWF NZ (055), Carbon Farm (102)].

Northland Regional Council (069) noted that price increases (such as petrol) would be disproportionately felt in rural areas.

### **Expected carbon prices**

Several submitters expect price volatility after 2012 [Greenhouse Policy Coalition (114), [withheld] (121)]. Bank of New Zealand (124) expected carbon prices to rise significantly [Rio Tinto (094)].

Talleys (007) believes that international carbon prices are heavily influenced by rogue traders in the derivatives markets. Federated Farmers (137) noted that carbon prices in New Zealand's ETS are less driven by abatement cost and mitigation potential within our national borders, but more by the value of traded units in the EU ETS. It considered that this is a nod towards the need for more balance between an ETS designed for New Zealand's interests and a scheme replicating conditions better suited for other countries.

### **Removal of the transition phase**

Numerous submitters expected the carbon price to increase after 2012 due to an increase in the international price of carbon and/or greater exposure to this price under the ETS. Some also noted what the potential negative consequences might be if the transition phase was removed. [Greenpeace (085), Wellington City Council (058), Northland Regional Council (069), Employers & Manufacturers Association (070), Rio Tinto (094), Ballance Agri-Nutrients (048), [withheld], BusinessNZ (149), Horticulture NZ (148), Federated Farmers (137)]

These consequences included:

- increased risk of carbon leakage
- some businesses would not survive
- new investment in new production methods and capacity will be deferred.

Other submitters noted the potential benefits the removal of the transition phase might bring such as incentivising the biofuel production and renewable electricity capacity. [Bioenergy Association (138), Mighty River Power (130)]

See chapter 5 for a summary of other points made in relation to the transition phase.

## **Agriculture sector impacts**

Submitters from the agricultural sector expect significant costs for farmers and /or meat processors, relative to profits or income, when the agriculture sector enters the ETS. A number provided cost estimates for them or their sector generally. Some also noted the likely scale of the cost increase was not sustainable as it would impact on farm profitability and result in reduced output. [Taumarunui Sustainable Land Management Group (031), Climate Realists (050), Escea (006), Beef + Lamb NZ, the Meat Industry Association and Dear Industry NZ (107), Fonterra (120)]

See chapter 6 for a summary of other points made in relation to the agriculture sector.

## **Fishing sector impacts**

Submitters from the commercial fishing sector noted that the sector will be adversely affected by the ETS to a greater degree than other sectors. One noted the ETS costs were likely to double which would affect international competitiveness. Another noted a high carbon price (of \$50 to \$100) could have a catastrophic impact on the sector. [Seafood Industry Council (065), Talleys (007)]

## **Industry sector impacts**

Some industry submitters felt their business would be negatively affected by the ETS after 2012 and this impact could be significant. Many noted that they would not be able to pass on the increase in costs once the transition phase ends in 2012 as they are trade exposed. As a result this would reduce their profitability and could, depending on the level of the carbon price after 2012, mean certain businesses become loss-making. In these circumstances, this would increase the risk that these businesses would close. [Gelita (017), NZ Steel (135), Cavalier Wool Holdings (038), Methanex (105), Wood Processors' Association (042)]

## **Waste sector impacts**

Several councils said the ETS costs for the waste sector would be significant for them. Some said that this would lead to increases in rates or waste disposal gate charges to cover these increased costs. It was also noted the difficulties that smaller provincial and rural councils would face because it is uneconomic for them to install gas collection and destruction facilities. [Central Hawke's Bay District Council (123), Porirua City Council (129), Hastings District Council (062)]

See chapter 7 for a summary of other points made in relation to the waste sector.

## **Coal sector impacts**

Submitters for the coal sector raised a number of concerns about the impacts on their business after 2012. Some thought the way the ETS worked would favour large mining companies over small- and medium-sized mining companies. Others noted the long-term threat to the viability of South Island coal mining communities as coal users switch to imported coal. [[withheld] (049), [withheld], Rockies Mining (024), Heaphy Mining (128), Coal Association (132)]

## **Impact on business investment decisions**

Submitters noted the continuing uncertainty which will impact on business investment decisions. There is uncertainty about a wide range of factors such as future carbon prices, future ETS design and the future international framework and commitments to reduce emissions. [Holcim (112), Straterra (084), Waikato Regional Council (072), GL Bowron & Co (074), Fletcher Building (076), Kyoto Forestry Association (078), Rockies Mining (024), Contact Energy (089), Meridian Energy (092), Richard Leckinger (096), Ballance Agri-Nutrients (048), Horticulture NZ (148), Greenhouse Policy Coalition (114), Holcim (112), Pastoral Farming Climate Research (131)]

A number of submitters expect the ETS after 2012 to influence business investment decisions. Some thought there would be a positive impact on certain investment decisions, such as for forestry, biofuels and waste. [Proprietors of Taharoa C Block (051), Craigmore Forestry (144), Greenhouse Policy Coalition (114), Porirua City Council (129), Wellington City Council (058)]

Others felt there would be a negative impact on business investment. For multi-national companies, investment in New Zealand may be harmed if the ETS reduces the profitability of New Zealand operations. Others felt the reduction in profitability from increased ETS costs would affect the ability of businesses to make investments [Ballance Agri-Nutrients (048), Federated Farmers (137), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Seafood Industry Council (065)].

Others felt there would be no impact on investment particularly where businesses did not have viable options to reduce emissions, for example, because they were already operating at best practice [Cavalier Wool Holdings (038), Methanex (105)].

## **Competitiveness risks and carbon leakage**

Many submitters thought the end of the transition phase will put New Zealand businesses at a competitive disadvantage if their international competitors do not face a similar cost on their emissions. Competitiveness risks are therefore likely to increase after 2012. Many also noted that this would also increase the risk of carbon leakage. [Bryan Leyland (001), Talleys (007), Gelita (017), Rockies Mining (024), Cavalier Wool Holdings (038), Carter Holt Harvey Pulp & Paper (040), Pacific Shipping (041), Wood Processors' Association (042), NZ Refining Company (043), Genesis (053) DairyNZ (061), Employers & Manufacturers Association (070), GL Bowron & Co (074), Fletcher Building (076), Straterra (084), KiwiRail (086), Rio Tinto (094), [withheld] , NZ Sugar Company (103), ExportNZ (104), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Greenhouse Policy Coalition (114), NZ Institute of Forestry (119), Fonterra (120), Origin Energy (122), Bank of New Zealand (124), Oamaru Landscape Centre (126), TA & DM Turner (127), Heaphy Mining (128), Pastoral Farming Climate Research (131), Taumarunui Sustainable Land Management Group (031), Coal Association (132), NZ Steel (135), Horticulture NZ (148)]

Carbon Farm (102) noted that competitiveness risks will arise if the ETS does nothing for emissions as well as if the ETS does too much and added that carbon leakage has so far proven to be insignificant. Richard Leckinger (096) noted that there is a risk of carbon leakage to New Zealand given the vast subsidies given to emitters here.

## **Emission and other environmental impacts**

Some submitters thought the ETS would not reduce emissions significantly and/or would cause adverse environmental outcomes. [Taumarunui Sustainable Land Management Group (031), Sustainability Council (151), Beef + Lamb New Zealand, the Meat Industry Association and Deer Industry New Zealand (107), Local Government New Zealand (099), Hastings District Council (062), Central Hawke's Bay District Council (123), Porirua City Council (129), [withheld] , Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]

Potential adverse environmental outcomes included:

- increased illegal dumping of waste (which in turn could result in contamination of waterways, aquifers and drinking water supplies)
- increased burning of waste
- reduced use of recycled materials in production processes (which will increase the use of raw materials and more waste sent to landfill)
- the inclusion of agriculture in the ETS is likely to result in further deforestation and loss of biodiversity.

Others thought the ETS would reduce emissions significantly in the long term and/or would cause positive environmental outcomes. [Southern Forestry (029), Oregon Group (080), Carbon Farm (102), Euan Mason (108), Craigmore Forestry (144)]

Potential positive environmental outcomes included:

- large scale rehabilitation of native forests which in turn will result in less soil erosion and better water quality
- greater diversity in planted forest species
- the inclusion of forestry could result in greater afforestation.

## **Social impacts**

Some submitters noted that there may be no social benefit and indeed there could be significant negative social impacts after 2012. [Fletcher Building (076), Northland Regional Council (069), Bryan Leyland (001), NZ Steel (135), Taumarunui Sustainable Land Management Group (031), Ballance Agri-Nutrients (048), Climate Realists (050), Horticulture NZ (148), Federated Farmers (137), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Heaphy Mining (128)]

These negative social impacts included:

- the loss of employment if businesses close which would particularly be felt in rural areas
- forestry is not a labour intensive activity and therefore afforestation will reduce rural employment

- rural communities will shrink
- South Island schools and hospitals will be forced to close during winter months due to the increased energy costs
- the incentive to convert agricultural land to forestry does not make sense given the high price of food and the need to feed a growing population
- impacts on household incomes and living standards.

Others felt there may be positive social impacts after 2012 such as employment benefits for rural communities through forestry development [Oregon Group (080)].

General Electric (150) said the Government should ensure assistance for disproportionately impacted sections of the community and the economy.

## **Abatement technology development**

While it was acknowledged that technology and innovation are critical in achieving emissions abatement there is uncertainty about technology development. Options may become more attractive when the price of carbon increases. [Wellington City Council (058), Straterra (084), GL Bowron & Co (074), Fletcher Building (076), Employers & Manufacturers Association (070)]

A number of submitters discussed abatement options available to them or for their sector generally. Many noted that these are currently limited and/or expensive. Several noted that they nevertheless continue to improve energy consumption and emissions intensity. [Rio Tinto (094), NZ Steel (135), Holcim (112), NZ Coal & Carbon (111), Ballance Agri-Nutrients (048), TA + DM Turner (127)]

In the agriculture sector a number of submitters noted the difficulties for reducing emissions from their livestock and that it is unlikely that any technologies would emerge by 2013. [Steve Wrathall (018), DairyNZ (061), Greenhouse Policy Coalition (114), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]. Carbon Farm (102) argued that once the agriculture sector enters the ETS, uptake and the sophistication of abatement options will develop rapidly. The submitter also noted that technology costs generally decrease with time.

Others noted that a price on emissions in New Zealand alone is unlikely to result in significant technology development as New Zealand is a technology taker [BusinessNZ (149), Fletcher Building (076)].

Others noted areas for potential technology development or for improving emissions abatement, such as:

- bio-oil and biochar technologies [Oregon Group (080)]
- use of biofuels [Nelson Forests (098), NZ Farm Forestry Association (039), Proprietors of Taharoa C Block (051)]
- trees that can absorb more carbon [NZ Farm Forestry Association (039)]

- sustainable aviation fuels [Qantas (158)]
- facilitating greater technology transfer across industries [Sylait Milk (046)].

## **Business opportunities and benefits**

A number of submitters noted potential business opportunities and benefits that could emerge. These included:

- Multiple business opportunities are expected to arise from the ETS such as clean technology, finding answers to agricultural emissions that have international applicability, and developing service expertise in carbon accounting and trading [Carbon Farm (102)]
- New Zealand could supply international carbon markets with emission units which could become New Zealand's biggest export [Southern Forestry (029)]
- transitioning away to a low carbon economy would reduce New Zealand's reliance on fossil fuel imports [Hamilton City Council (028)]
- New Zealand can strategically market itself on environment stewardship and emission trading mitigation [Sylait Milk (046)].

Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) noted that there were no business opportunities or benefits for it.

## 3 Impacts of the ETS on Māori

### Panel's assessment of the impacts on Māori (Question 8)

Overall there were 30 submissions received relating to the current and future impacts the ETS have on Māori/iwi.

Seven submitters explicitly agreed with the Panel's assessment, and a further 6 partially agreed. The issues raised by the 'partially agreed' submitters included:

- The Panel's assessment failed to take into account that Māori are very unlikely to sell their land compared with Non-Māori for non-economic reasons [Te Uri o Hau Settlement Trust (082)].
- The Panel's assessment lacked any meaningful analysis of the impact on lower socio-economic New Zealanders, bearing in mind the Māori are disproportionately over-represented in that group [Richard Leckinger (096)].
- Disagreement with the Panel's assessment that significant economic opportunities are present for Māori in forestry [Federation of Māori Authorities (109)].
- Not only was there inequality between Māori and non-Māori, but also between rural and urban Māori - while rural Māori bear the cost of the ETS, they also retain some opportunities, whereas urban Māori are mostly restricted to the burden of cost with little opportunities [Carbon Market Solutions (145)].
- The Panel made little reference to Māori ownership, preservation and upgrading of indigenous regenerating land [Carbon Market Solutions (145), Sustainability Council (151)].

### Impacts at a sector level (Questions 9 and 10)

Five submitters considered that Māori have experienced positive impacts as a result of the ETS. These submitters believe this is due to the concentration of Māori interests in the primary industries of agriculture, forestry and fishing [Escea (006), Southern Forestry (029), OMFinancial (047), Carbon Farm (102), Sustainability Council (151)], and because of their limited direct exposure to emissions costs in the industrial sector [Carbon Farm (102)].

However, 12 submitters considered that the larger representation of Māori in the primary industries meant that they have been adversely affected by a disproportionate share of the negative impacts of the ETS [Southern Forestry (029), Proprietors of Taharoa C Block (051), Northland Regional Council (069), Te Uri o Hau Settlement Trust (082), Richard Leckinger (096), Joint Submission: Beef + Lamb New Zealand Ltd/Meat Industry Association/Deer Industry NZ (107), Federation of Māori Authorities (109), Bioenergy Association (138), Craigmore Forestry (144), Carbon Market Solutions (145), OraTaiao: NZ Climate & Health (146), BusinessNZ (149)].

The Environment and Conservation Organisations of NZ (161) submitted Māori have been, and will continue, to be disproportionately affected by the negative impacts of the allocation policy. The Environment and Conservation Organisations of NZ argued that allocations falsely depress the price of carbon, which is a considerable risk to Māori investors, as investments may face 'depressed returns once the true costs kick in'.

Two submitters considered that the ETS impacts for Māori have been the same as for the rest of New Zealand [Climate Realists (050), [withheld] (081)].

## **The concentration of Māori interests in forestry**

### **Earning good revenue from post-1989**

Five submitters stated that to date Māori have been positively impacted by the ETS [Escea (006), Southern Forestry (029), OMFfinancial (047), Carbon Farm (102), Sustainability Council (151)]. They generally agreed with the Panel's statement that there are significant economic opportunities for Māori-owned forestry under the ETS in terms of the potential to earn emission units for carbon sequestration on land forested after 1989.

Seven submitters explicitly stated that in future the benefits of post-1989 forestry would continue and Māori would continue to have the potential to earn good revenues [Escea (006), Bill Sayer (014), Southern Forestry (029), OMFfinancial (047), Climate Realists (050), Oregon Group (080), Federation of Māori Authorities (109)].

Three submitters commented on the access to opportunities for Māori, with respect to the added incentive for conversion of marginal farming land to forestry [Southern Forestry (029), OMFfinancial (047), Bank of New Zealand (124)].

### **The role of indigenous forest estate**

Four submitters referred to the need for the Panel to recognise the extensive Māori interest in indigenous forest, which plays an important role in carbon sequestration [Federation of Māori Authorities (109), Carbon Market Solutions (145), Sustainability Council (151), Climate Change Iwi Leadership Group (159)]. Two submitted that as the single largest owner after the Government, Māori play a critically important role in biodiversity conservation in New Zealand [Federation of Māori Authorities (109), Climate Change Iwi Leadership Group (159)].

Two submitters [Federation of Māori Authorities (109), Climate Change Iwi Leadership Group (159)] believe some consideration should be given to Māori by way of:

- Free allocation of NZUs
- The creation of a new biodiversity credit recognising the carbon storage and biodiversity capacity of our indigenous forests.

Another submitter also pointed to the special provision for indigenous forests proposed by the previous Government by way of a one-off allocation, similar to pre-1990 forest allocation, and stated that the situation should be 're-emphasised and reviewed' [Carbon Market Solutions (145)].

### **Pre-1990 deforestation liabilities for Māori (to date)**

Ten submitters commented on the negative impact that the ETS has had on Māori to date, due to the deforestation liabilities for pre-1990 forestry [Southern Forestry (029), Proprietors of Taharoa C Block (051), Northland Regional Council (069), Te Uri o Hau Settlement Trust (082), Richard Leckinger (096), Federation of Māori Authorities (109), Bioenergy Association (138), Craigmore Forestry (144), Carbon Market Solutions (145), BusinessNZ (149)]. Many of these submitters restate that the negative impacts from the pre-1990 rules disproportionately disadvantage Māori. Many of these submitters also mentioned that Māori have strong commercial assets in forestry and these assets are commonly passed on in Treaty of Waitangi settlements, where Māori have not had any power over how the land has been used previously.

Craigmore Forestry (144) argued that there has been limited new planting by Māori as many forests that are considered suitable for 'forestry and carbon' are actually ineligible to be post-1989 forests under the ETS. This is due to some land already having a scrub cover as at 1990 and, because of reduced input costs to Māori farm land since the 1970-80s and the subsequent scrub regeneration, many Māori land owners are now excluded from partaking in the ETS. Carbon Market Solutions (145) also argue that the ETS has not led to new planting and state 'generally speaking iwi are asset rich and cash poor, meaning that for many iwi the ETS has not lead to significant investment in planting, but for those that already have significant forestry assets there have been revenues'.

Eight submitters stated that the pre-1990 rules need to be more flexible to ensure Māori interests are accounted for [Southern Forestry (029), Proprietors of Taharoa C Block (051), Te Uri o Hau Settlement Trust (082), Richard Leckinger (096), Federation of Māori Authorities (109), Bioenergy Association (138), Craigmore Forestry (144), Carbon Market Solutions (145)]. These interests are stated as being economic and non-economic.

In terms of economic Māori interests, some feel that the deforestation liability means that it is too expensive/not economically viable to change land-use (i.e. from forestry to farming) [Southern Forestry (029), Federation of Māori Authorities (109)]. Furthermore, some feel that the deforestation liability is unreasonable and leads to an illogical outcome in the situation where forest owners wish not only to put their land to a use that is more economically rewarding but more importantly to a use that is low/zero carbon [Federation of Māori Authorities (109), Te Uri o Hau Settlement Trust (082), Proprietors of Taharoa C Block (051), Bioenergy Association (138), Carbon Market Solutions (145)].

For example, Te Uri o Hau Settlement Trust (082) submitted that they wish to develop a forest into a wind farm. However, they feel that the liabilities are so high that it renders the development uneconomic. Others have mentioned this same impact in regards to developing geothermal energy

[Federation of Māori Authorities (109)] and biofuel crops [Proprietors of Taharoa C Block (051), Bioenergy Association (138), Carbon Market Solutions (145)].

Two submitters alluded to non-economic interests – the Māori cultural and spiritual connection to the land [Te Uri o Hau Settlement Trust (082), BusinessNZ (149)]. Te Uri o Hau Settlement Trust (082) argues that the blood connections to the land of Tangata Whenua Māori will override any commercial considerations. They state ‘for cultural reasons they cannot sell the land, and for ETS reasons they cannot achieve highest and best-use of the land’.

While recognising this point, BusinessNZ (149) also frame the interest of Māori as kaitiaki (long term guardians) of the land, as having the potential to make Māori ideal long-term business partners.

### **Pre-1990 deforestation liabilities for Māori (in future)**

Many of the eight submitters believe if there is no change (see recommendations below) then the pre-1990 liabilities will be detrimental to the future development of Māori. For example, Climate Realists (050) stated that despite the forestry allocation policy for pre-1990 land, Māori are going to suffer in the long term. Furthermore, Lake Taupo and Lake Rotoaira Forest Trusts (142) stated that there is a potential, if off-set planting is allowed (post-2012), for the second tranche of allocations not to occur. Lake Taupo and Lake Rotoaira Forest Trusts (142) argue that although offset planting may have some attraction to some owners of post-1990 forest, for many it is not a realistic opportunity, due to spiritual connections, governance issues and economic viability.

A number of submitters proposed recommendations for the Panel to consider. These included:

- Lake Taupo and Lake Rotoaira Forest Trusts (142) and Oregon Group (080) would like the Government to confirm the second tranche allocation
- Southern Forestry (029) would like to see pre-1990 forest land included in the carbon accounting that occurs for post-1989.
- The Federation of Māori Authorities (109) believe there should be an exemption or opt-out clause for land returned under Treaty of Waitangi settlements as the Māori owners had no say in how that land was used prior to its return
- The Federation of Māori Authorities (109) and the Climate Change Iwi Leadership Group (159) want the Government to continue to forcefully push as part of international negotiations for the acceptance of land use change flexibility, such as through offsetting.
- If offset planting is confirmed Lake Taupo and Lake Rotoaira Forest Trusts (142) recommend that the owners of pre-1990 forest should be given a choice of either taking the full allocation or electing to retain the right to undertake offset planting.
- Te Uri o Hau Settlement Trust (082) wish to see the ETS rules changed to allow the new land use activity and associated carbon offset benefits to be considered in the assessment of the ETS liabilities associated with the deforestation of pre-1990 land.

## **Multiply-owned land without governance structures or under Māori trusteeship**

Seven submitters made reference to particular challenges faced by Māori owners of multiply-owned land [Oregon Group (080), Beef + Lamb New Zealand Ltd, the Meat Industry Association and Deer Industry NZ (107), Māori Trustee (125), Lake Taupo and Lake Rotoaira Forest Trusts (142), Craigmore Forestry (144), Carbon Market Solutions (145), Climate Change Iwi Leadership Group (159)]. Two submitters specifically commented on the problem faced by Māori/iwi that collectively own land, as being a negative long term impact if appropriate structures are not put in place [Oregon Group (080), Craigmore Forestry (144)].

The following issues were identified and possible solutions to these issues are discussed.

### ***Inability to participate***

The Māori Trustee (125) submitted that the ability of owners of Māori land to transact business is often complicated because their land is governed by the Te Ture Whenua Māori Act 1993 (TTWMA), which requires collective decision making approaches. The TTWMA sets agreement thresholds of 50 per cent or 75 per cent for alienation and sale of land. This results in signatory issues. A significant proportion of land owners are unable to be located, or are deceased and succession has not taken place.

The Act requires the even higher agreement threshold of 100 per cent for allocation and exemption applications. Because there is no management structure in place, some Māori in effect are unable to apply for credit/exemption but still bear the liability.

Craigmore Forestry (144) submitted that their experience of dealing with Māori land trusts led them to believe that the protocols required in terms of signatures and authorisations for NZEUR accounts and ETS registrations has been a deterrent to Māori involvement in the forestry side of the ETS.

The Māori Trustee (125) recommended:

- The Act is modified in light of the TTWMA requirements and practicalities of land ownership.
- A mechanism is developed whereby owners can enter the scheme despite the lack of legal entity and owners are protected from liability where they are not in a position to apply for credits.

### ***Inability to meet timeframes***

Because of the problems associated with collective decision making, and low resourcing, three submitters stated that there are often time delays in working through the relevant applications [Lake Taupo and Lake Rotoaira Forest Trusts (142), Craigmore Forestry (144), Carbon Market Solutions (145)]. The cut-off date for applying for allocation in relation to pre-1990 forest land is therefore considered to unfairly penalise owners of Māori land.

Lake Taupo and Lake Rotoaira Forest Trusts (142) recommended that the cut-off date for pre-1990 forest land allocation applications is extended until 31 December 2012.

## **Complex nature of the ETS and high transaction costs**

The Climate Change Iwi Leadership Group (159) submitted that small to medium sized trusts are struggling to understand and engage the ETS and lodge applications for allocations and exemptions. They further submit that the Ministry of Agriculture and Forestry outreach programme may not get 100 per coverage. Lake Taupo and Lake Rotoaira Forest Trusts (142) also submitted that they are in fact aware of Māori Trusts who have small pre-1990 forests but know little about the ETS and have no plans to submit an application.

The Climate Change Iwi Leadership Group (159) also submitted that Māori trusts and incorporations lack the resources and technical expertise to engage in the ETS. This has meant that often use of advisers and intermediaries, and greater time commitments are required, which lead to high transaction costs. It recommended streamlining ETS administration towards fewer Government agencies, so as to reduce complexities and confusion, thereby also reducing some of their transaction costs.

## **Perpetuity**

The Māori Trustee (125) submitted that much of the Māori land base is leased and that in certain cases lessees have made decisions in relation to the land, such as planting forest pre-1990. However, it is the owners who are considered participants under the ETS in relation to this land. The nature of these owners' interests in land has been changed without due regard, and liabilities imposed on them in perpetuity. It is recommended that the point of obligation process is developed to enable obligations to be shifted. Furthermore, the Māori Trustee believes this process must take into account the practicalities of the long term leasing arrangements over Māori land and the nature of Māori land holdings.

## **Investment decision-making**

One submitter stated that problems in the agricultural sector arising from uncertainty and its adverse impact on investment decision-making will only be exacerbated by the constraints on decision-making in relation to jointly held land [Beef + Lamb New Zealand Ltd, the Meat Industry Association and Deer Industry NZ (107)].

## **Under 50 hectare exemption**

The Māori Trustee (125) submitted that the under 50 hectare exemption provided for in the CCRA is not practically available for forests where:

- There are multiple owners and no trust structure in place
- The land is held by a professional trustee holding more than 50 hectares
- The land is held by the Māori Trustee holding 50 hectares in total across several land trusts.

The Māori Trustee (125) further submitted that approximately 18 of about 60 exotic forests that the Māori Trustee administers are less than 50 hectares.

The Māori Trustee (125) recommended that the Panel considers options that enable Māori land owners to seek an exemption from participation as pre-1990 owners where lands are managed separately.

### **Liability imposed on the Māori Trustee**

The Māori Trustee (125) submitted that he is not in the same position as other professional trustees, as he is unable to seek contractual indemnification from beneficial owners directly. It was submitted that the land in question is generally too small and uneconomic to manage large liabilities. The impact is that if deforestation takes place on any individual trust's land, there is little capacity to meet the full liability from each trust's assets. This is because the Māori Trustee is not in a position to sell the land and the asset itself is unlikely to generate sufficient income. The Māori Trustee submitted that he would seemingly be liable to meet any shortfall if there is a deforestation liability which cannot be met by the assets of the trust.

### **Custodian trustee**

The Māori Trustee (125) submitted that he is from time to time appointed as a custodian trustee under the TTWMA. As custodian trustee, the Māori Trustee has no control over the trust's assets, forest management decisions, or decisions over whether to retain or sell credits. Decisions in such cases are taken by the responsible trustees that the Māori Trustee, as legal owner, then must fulfil. This means the Māori Trustee has little or no ability to manage the risk, despite the ability to seek a direction from the Māori Land Court.

The Māori Trustee (125) recommended that the system of allocation take into account the nature of a custodian trustee and provides clear guidance on where the point of obligation rests.

### **Impacts expected for land use, development options and agriculture**

One submitter asserted that the ETS has added about \$2,000 to the cost of the average sheep/beef farm and that because a high proportion of Māori assets are made up of primary industry, a disproportionate share of adverse impacts such as this are likely to fall on Māori [Beef + Lamb New Zealand, the Meat Industry Association and Deer Industry NZ (107)].

This submitter also commented that for many Māori sheep and beef farms, sale of land is not culturally and/or legally feasible. The submitter states that this will lead to an inability to borrow on the security of their land assets and a relatively (when compared with the rest of the sector) heavy reliance on cash-flow for sustainability. It was further stated that this makes the impact on profitability arising from the ETS additionally severe for those businesses that rely on strong cash-flows to cover both operating costs and to fund the required land development. The effect of the ETS on farm cash flows is therefore expected by the submitter to heavily reduce Māori farm owners' ability to achieve the full development potential of certain land areas.

Te Uri o Hau Settlement Trust (082) considers that in the long term, there will be a continuation of low yielding Māori land, stunting the economic growth of Māori and New Zealand in general.

The Federation of Māori Authorities (109) submitted that some of their constituent members felt that the ETS, as it relates to the agricultural sector, would impact on them so severely that many would feel forced to leave the agricultural industry. They further stated that as a result of the TTWMA greater constraints are already felt by Māori than non-Māori, resulting in lowered productivity and profitability of Māori farms. Therefore, the Federation of Māori Authorities (109) believe the entry of agriculture into the ETS will exacerbate this disproportionate impact on Māori.

Te Uri o Hau Settlement Trust (082) submitted that because some Māori cannot sell their ancestral land, special consideration needs to be given. This may help ensure that pre-1990 forest land under Māori ownership can achieve highest and best use criteria to provide an economic stimulus not only to Māori, but to New Zealand as a whole.

The Federation of Māori Authorities (109) considered that there is a need for some changes to the agricultural ETS. The Federation of Māori Authorities (109) and OraTaiao: NZ Climate & Health (146) both recommended that particular consideration be given to assist Māori towards reducing their emissions and transitioning to clean/renewable technologies.

## **Impacts expected for energy**

The Proprietors of Taharoa C Block (051) submitted that the ETS has a negative impact on Māori looking to develop in the energy sector. They stated that many Māori, as minority partners in geothermal energy companies, are at a relative disadvantage as compared to their partners.

The Proprietors of Taharoa C Block (051) believe the Panel should also assess many other forms of renewable energy which are relevant to Māori, such as wind and wave/tidal. They stated that existing renewable energy generators receive windfall gains relative to new entrants. They further submitted that the nature of the New Zealand electricity market system is such that established energy companies have significant market power. As a consequence Māori, as independent developers of renewable energy, suffer a major competitive disadvantage.

## **Impacts at a whanau level**

### **Future employment**

The Wood Processors' Association (042) submitted that Māori are disproportionately represented in forestry, not only as owners, but also as employees. For example, the wood processing employs a large number (18,000) people from rural areas with high Māori populations. Therefore, they argue that measures that damage the wood processing sector, such as 'costly domestic policy settings', may have a disproportionately negative impact on Māori. A similar argument was provided with respect to Māori employment in the red meat processing industry [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)].

The Environment and Conservation Organisations of NZ (161) submitted that the real social impacts, especially surrounding future employment for Māori, were largely ignored by the Panel. The Environment and Conservation Organisations of NZ argue that a higher price on carbon will mean

greater investment in energy efficiency and that this will create future employment opportunities (retrofitting housing), in comparison to capital intensive activities that will provide far fewer jobs (mining, oil/gas exploration). It is argued that this will be of benefit to Māori, many of whom may face short term costs as a result of the ETS.

The Environment and Conservation Organisations of NZ recommends that the Panel request advice on the relative labour: capital and labour: output ratios and recent trends, since these can provide insights into social impacts of the ETS.

## **Impacts on the Māori households**

Many submitters mentioned that Māori households have been, and will continue to be, disproportionately impacted through rising energy costs from the ETS [David Slack (008), Steve Wrathall (018), OraTaiao: NZ Climate & Health (146), Sustainability Council (151), Climate Change Iwi Leadership Group (159)]. This is due to Māori being over-represented amongst New Zealand's low income households. Furthermore, OraTaiao: NZ Climate & Health (146), The Environment and Conservation Organisations of NZ (161) and Sustainability Council (151) submitted that the ETS, particularly the allocation policy, is in essence a taxpayer subsidy for big polluters. These submitters believe this is a regressive and inefficient distribution of the costs of the ETS which reduces the funds available for critical health and social services. OraTaiao: NZ Climate & Health (146) submitted that Māori will in future be particularly affected by these costs, as they consider Māori an already vulnerable group who will be more severely affected by risks and inequities. The Environment and Conservation Organisations of NZ (161) added to this by submitting that Māori, as a vulnerable group, are likely to be most affected by the various adverse health impacts of climate change.

One submitter believed there had been no impact to date and that any long term impacts would be the same as for the rest of New Zealand [[withheld] (081)].

OraTaiao: NZ Climate & Health (146), Environment and Conservation Organisations of NZ (161) and Climate Change Iwi Leadership Group (159) recommended that the Government should continue to provide assistance which is targeted at helping Māori households withstand the effects of the ETS through demand-side management mechanisms, such as the home insulation programme.

# 4 International framework and objectives of the ETS

## Future international framework (Question 11)

The *Issues Statement* presented three possible international framework scenarios for the period 2012 to 2020:

- A legally binding multilateral framework, which would provide some form of binding emissions reduction target on New Zealand
- An international political accord, which would provide for only political commitments at the international level
- A continued period of medium-term political uncertainty, with no international commitments beyond the general commitments that New Zealand has as a party to the UNFCCC.

Fifty-three submitters commented on the question of whether the international scenarios capture the most likely outcome for the international framework after 2012. The majority view of submitters was that the three scenarios presented the most likely outcomes over the next few years. Of those submitters that considered that these were the most likely scenarios, the majority considered that scenario 3 was the most likely, a prolonged period of medium-term uncertainty.

Twelve submitters disagreed with the scenarios submitted, or nominated an alternative scenario. Of those submitters that held alternative views to the three scenarios, there were two groups. One group offered specific variants on the scenarios (such as internal trading linked by bilateral agreements). A second group of submitters considered that all efforts to address climate change would be abandoned.

Thirteen submitters discussed the international framework in general terms, but neither explicitly agreed or disagreed with the scenarios presented.

### Summary of those submissions agreeing with the Panel's scenarios

BusinessNZ (149) submitted that a successor to the Kyoto Protocol is unlikely to be in place from 2013. It further submitted that it was difficult to judge the true intent of some countries on climate change initiatives. It suggested that it was inappropriate to base the design features of a New Zealand ETS on the stated intent or content of policies in other countries, if these policies were taken at face value. It also drew the Panel's attention to international policy inconsistencies between climate change policies and other sector policies (e.g. coal subsidies). These make it difficult to judge the true impact of declared climate change initiatives in other countries.

Holcim (112) submitted that an outcome between scenario 3 and scenario 2 is most likely, with an international political accord in some form, but accompanied by further instability.

The NZ Business Roundtable (083) submitted that scenario 3 is the most likely outcome. It further submitted that the Review should significantly discount the probability that other countries will actually implement price-based policies to reduce emissions, drawing particular attention to the USA and Australia.

Similarly, the Seafood Industry Council (065) submitted that New Zealand should not act based around the intent of other nations, without seeing evidence of the details of proposed carbon pricing schemes.

Qantas (158) submitted that it is likely that the CDM will continue even if there is no immediate successor to the Kyoto Protocol.

Fonterra (120) submitted that a mix of scenarios 2 and 3 is the most likely outcome, and the outcome the Government should use for its base policy design. Key features of the most likely outcome would be where emissions reduction targets are political and governed by domestic accounting rules. International markets would then be formed from the integration of various domestic markets.

## **Summary of those submissions with alternative views on international scenarios**

Carbon Market Solutions (145) submitted that the panel should consider a scenario of the Kyoto Protocol being amended for a second commitment period, but as an interim measure. This would free up time to enable a comprehensive multilateral agreement to be developed.

Climate Realists (050) submitted a fourth scenario where all countries abandon emission reduction targets. Similarly, David Slack (008) and Steve Wrathall (018) submitted that international efforts to reduce climate change would be abandoned.

The Employers & Manufacturers Federation (070) submitted that the international focus will likely turn to technology solutions, especially in the energy field.

Federated Farmers (137) submitted that there should be a further scenario that explicitly covers linked domestic schemes governed by bilateral agreements.

OraTaiao: NZ Climate & Health (146) submitted a further two scenarios: Firstly, a top down international agreement with stronger emissions reductions based around the goal of limiting warming to two degrees. Secondly the emergence of 'bottom up' emissions reductions driven by citizens and corporations.

The Environment and Conservation Organisations of NZ (161) submitted that the scenarios presented fail to examine consumer-driven impacts on emissions reductions.

## Implications for the objectives of the ETS (Question 12)

### Costs that New Zealand should impose on its economy

Twenty-five submitters considered that the international scenarios pointed to the Government needing to take steps to moderate the costs that the ETS imposes on the economy. Twelve submitters considered the international scenarios have no (or immaterial) implications for the costs that New Zealand should impose on the economy.

#### ***Summary of those submissions proposing to moderate the costs imposed by the ETS***

The Greenhouse Policy Coalition (114) advocated a cautious approach. The international scenarios suggest that the transitional arrangements should be extended to limit costs.

The Bank of New Zealand (124) suggested that there is a level of risk associated with including sectors in the ETS that have exposure to market pricing.

GL Bowron & Co (074) submitted that with scenarios 2 and 3 it is important that carbon costs in New Zealand should not exceed those imposed on international competitors.

BusinessNZ (149) submitted that lack of sufficient international action means that the ETS may no longer be fit for purpose. Irrespective of the scenario that emerges there will continue to be a risk of carbon leakage. Also the current domestic market does not represent an optimal abatement price. It also submitted that the Panel should consider the costs of scaling up the ETS as scheduled. The Panel should explicitly consider the appropriate level of long-term economic burden for New Zealand. The level of economic burden that can be accommodated should inform the targets that New Zealand adopts.

The Employers & Manufacturers Federation (070) submitted that New Zealand should be minimising the costs imposed by the ETS.

DairyNZ (061) submitted that if the ETS is fully implemented the Government will make significant financial gains from the scheme post-2018, and that this was contrary to the intent of the scheme and the Government's stated policy intent.

Fletcher Building (076) submitted that the ETS should not impose costs that are disproportionate to the costs faced by international competitors.

Holcim (112) submitted that the degree of international uncertainty around landing on any one of the scenarios is considerable. Holcim submitted that the transition arrangements in the ETS should be continued until the next ETS review.

Similarly, NZ Steel (135) submitted that New Zealand should maintain the existing settings of the ETS until trade competitors face similar carbon costs to New Zealand across sectors. This view (or similar views) were shared by Qantas (158), Sanford (156), Straterra (084), Mobil (140), and Carter Holt Harvey Pulp & Paper (040).

ACT (141) said that emissions reduction obligations should be minimal until imposed in the context of a meaningful international agreement.

NZ Business Roundtable (083) submitted that the benefits of adopting mitigation measures for New Zealand are primarily international relations benefits and protecting commercial interests. The costs are reductions in living standards.

Fonterra (120) submitted that there is risk inherent in basing the ETS design on measures contained in the draft Australian CPRS. New Zealand design should reflect local conditions while learning from the principles of overseas approaches.

The NZ Climate Science Coalition (003) submitted that the ETS should be set to effectively achieve a zero carbon price until trading competitors introduced a carbon price.

### ***Summary of those submissions proposing no change to the costs imposed by the ETS***

Greenpeace (085) submitted the scenarios have no implications for the costs that should be imposed on New Zealand. Polluters should bear all costs of emissions.

Richard Leckinger (096) submitted that the gazetted 2050 goal for a 50 per cent emission reduction suggested that there was no alternative to strengthening the ETS and imposing higher carbon costs in the short term.

OraTaiao: NZ Climate & Health (146) submitted the ETS is not imposing costs on New Zealand. Switching to sustainable energy sources promotes economic growth. The ETS should be modified to rapidly reduce New Zealand's emissions.

Oregon Group (080) submitted the ETS is cost neutral with higher costs to consumers transferred to foresters for environmental services.

Shell (157) submitted the ETS is the most efficient way for New Zealand to reduce emissions regardless of whichever international scenario eventuates.

Wellington City Council (058) submitted the price ceiling on NZUs should not continue beyond the currently scheduled timetable. The transitional measures dampen investment signals.

WWF NZ (055) submitted that New Zealand would probably have an obligation to reduce emissions below 1990 levels by 2020. The ETS will need to be strengthened to achieve that objective. WWF NZ submitted that it is not certain that the ETS will impose costs and that the potential economic benefits of mitigation efforts should be recognised.

Meridian Energy (092) submitted the objective of the ETS should remain unchanged under any of the scenarios. The objective is to change behaviour that results in lower emissions.

The NZ Institute of Forestry (119) submitted the stated objective of the ETS should be retained: to reduce emissions, enhance carbon sinks, and to meet specific emission reduction targets.

Escea (006) submitted domestic policy consistency is important. New Zealand should choose its pathway irrespective of the actions taken by other countries.

Solid Energy (027) submitted the main purpose of the ETS is to enable New Zealand to meet its international commitments. The one to one backing of AAUs falls away without a continuation of Kyoto.

### **Allocation of costs across the economy and between taxpayers and industry**

Submitters were approximately equally divided with differing views on this question. Fourteen submitters suggested that some sectors should bear a greater burden of emissions reduction efforts than other sectors when deciding on coverage by the ETS. This included those submitters who explicitly or implicitly suggested that taxpayers should bear some of the costs of the emission reductions. Eleven submitters maintained that the ETS should be neutral across sectors with all emitters being treated equally regardless of real or perceived opportunities to abate greenhouse gases.

#### ***Summary of those submissions suggesting disproportionate burden sharing***

The Greenhouse Policy Coalition (114) submitted that the Government should defer the entry of agriculture into the ETS. This view was shared by the Bank of New Zealand (124) and DairyNZ (061).

BusinessNZ (149) submitted that design elements of the ETS should be decoupled from the Australian ETS now that this scheme is not proceeding. The impact across taxpayers, business and consumers should be balanced. BusinessNZ submitted that there is an asymmetric risk around under and over-allocation. Support should be provided by free allocation and perhaps expanded. Carbon Farm also explicitly suggested that costs should be shared between emitters and taxpayers.

The Employers & Manufacturers Federation (070) submitted that New Zealand needs to maintain the competitiveness of trade-exposed sectors. The Federation also emphasised the importance of rebalancing the economy towards exports. No New Zealand sectors have significant scope to reduce emissions.

Fletcher Building (076) submitted that costs should be allocated based on availability of emissions reduction options.

Holcim (112) questioned the dichotomy presented in the Issues Statement between emitters and taxpayers. If a business is not trade-exposed price increases can be passed through to businesses using energy intensive products as intermediate inputs and to consumers (who are taxpayers). The exception is trade-exposed businesses that receive an allocation.

NZ Business Roundtable (083) submitted that the modelled costs presented in the issues statement are not insignificant. It further submitted that agriculture should be brought into the ETS as scheduled because excluding agriculture is inefficient. It acknowledged that there may be few short term options to reduce agricultural emissions but that this was also true for other sectors. The review should not make judgements about where abatement opportunities lie. Elements of

agriculture that are trade-exposed should be treated the same as other trade-exposed industries. However the Government should not proceed with any phase out of free allocations pending the outcome of the 2014 review.

NZ Steel (135) submitted that the transitional arrangements that apply to New Zealand Steel should not be changed. This is because the abatement options available are limited – similar to the situation faced by agriculture.

Qantas (158) submitted that if it is not feasible for other sectors to enter the scheme it will be important that taxpayers share the burden of international agreements so that transport (and other included sectors) is not unduly burdened.

Straterra (084) submitted that a key determinant of this balance between taxpayers and industry is how the issue is managed in other countries.

Fonterra (120) submitted that the price cap be maintained until other countries implement emissions trading policies.

Ballance Agri-Nutrients (048) submitted that the ability to reduce emissions is an important parameter in allocating the costs of the ETS across the economy.

### ***Summary of those submissions suggesting neutral burden sharing***

Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) submitted that policies should be aimed across the economy and not redirect resources from one sector to another, for example from pastoral food production to forestry. Crown liability should not be devolved if NZ over promises in international negotiations.

Greenpeace (085) submitted that taxpayers should not bear costs. Subsidies should be directed at vulnerable individuals.

Richard Leckinger (096) submitted that the nature of international obligations should not have a significant bearing on how the ETS works, that is obligations should fall on emitters.

Mighty River Power (130) submitted that it was important that all sectors participated in the ETS at the earliest opportunity.

Oregon Group (080) submitted that agriculture should come into the ETS as scheduled. This view is based on equity arguments.

[withheld] (121) submitted that all sectors should be treated equally.

Environment and Conservation Organisations of NZ (161) suggested that those who emit carbon should meet the costs. The cross-subsidies in the ETS blunt incentives.

Southern Forestry (029) submitted that the full weight of the adjustment task should fall on emitters.

## **The role of the ETS in preparing New Zealand for future international obligations**

Twenty submitters who explicitly commented on this question were equally divided on whether the ETS should have a prominent role in preparing New Zealand for future international obligations. Ten submitters considered that the ETS should have a prominent role in preparing New Zealand for future international obligations. Ten submitters considered that the ETS should not have a prominent role in preparing New Zealand for future international obligations.

### ***Summary of those submissions proposing a prominent role for the ETS***

Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) submitted that a key advantage of the ETS was that it is a credible policy tool to achieve international commitments.

BusinessNZ (149) submitted that the current design of the ETS is the best domestic policy solution if a deep international carbon market evolves. BusinessNZ submitted that there is still a need for a domestic emissions reduction target even in the absence of an international agreement. It is unlikely that there will be international obligations to reduce emissions. The UN will have a role in collectivising domestic emission reduction efforts and targets.

Carbon Farm (102) submitted that the ETS should allow NZ to meet all its future international obligations.

Carbon Market Solutions (145) submitted that the ETS plays an important signalling role in highlighting New Zealand policies in forestry and agriculture.

Fletcher Building (076) submitted that the role of the ETS is to introduce a marginal price on emissions and to increase awareness of the importance of reducing greenhouse gas emissions.

Greenpeace (085) submitted that the ETS should be one of a range of tools available to the Government to prepare New Zealand for future international obligations. The carbon price should act as a barrier to new emissions-intensive development.

Holcim (112) submitted that the ETS is a necessary but not sufficient mechanism to prepare New Zealand for its obligations. Other complementary policies are necessary, such as home insulation and vehicle fuel efficiency standards.

WWF NZ (055) submitted that the primary objective of the ETS should be to reduce emissions. New Zealand will need to meet further emission reduction obligations in coming decades. WWF NZ submitted that the efficacy of the ETS is critical because of the lack of complementary measures adopted to reduce emissions.

### ***Summary of those submissions not proposing a prominent role for the ETS***

The Greenhouse Policy Coalition (114) supported a broad carbon market but not if it imposes trade-exposed sectors to risks not faced by competitors.

GL Bowron & Co (074) submitted that the primary objective of the ETS should be to educate the public, but not impose anti-competitive burdens on business. Carbon costs should be imposed as these emerge in sectors internationally. Achieve this by using free allocation.

DairyNZ (061) submitted that New Zealand is well placed to meet its first commitment period obligations under the Kyoto Protocol. Future obligations are theoretical.

Federated Farmers (137) submitted that international uncertainty suggests that the ETS has no role in preparing NZ for international obligations. The Government should consider whether the ETS settings are optimal for New Zealand's interests.

Fletcher Building (076) submitted that the role of the ETS is to introduce a marginal price on emissions and to increase awareness of the importance of reducing greenhouse gas emissions.

Greenpeace (085) submitted that the ETS should be one of a range of tools available to the Government to prepare New Zealand for future international obligations. The carbon price should act as a barrier to new emissions-intensive development.

Pastoral Farming Climate Research (131) submitted that the ETS should not prepare New Zealand for international obligations.

Holcim (112) submitted that the ETS is a necessary but not sufficient mechanism to prepare New Zealand for its obligations. Other complementary policies are necessary, such as home insulation and vehicle fuel efficiency standards.

Straterra (084) recommended that the ETS should be placed in a holding pattern. There are no functioning international markets to minimise costs of abatement.

Fonterra (120) submitted that the current objectives of the ETS are no longer appropriate because of the state of play in emerging international frameworks. The revised objectives of the ETS should set a price on emissions while avoiding emissions leakage, ensure New Zealand does not face larger economic costs than other developed nations, and ensure that policy to reduce global emissions does not have a negative impact on global food security. Fonterra (120) further submitted that there is no longer a need to reference the Kyoto Protocol in the objectives of the ETS.

## **Changes to the ETS to increase incentives for domestic abatement**

Twenty submitters provided views on this question. Fourteen submitters favoured increasing incentives for domestic abatement. Six submitters suggested that the ETS not be modified to strengthen incentives for domestic abatement.

### ***Summary of those submission favouring increased incentives for domestic abatement***

BusinessNZ (149) submitted that decoupling the ETS from the Kyoto rules could allow for more flexible arrangements around incentivising land use change. New forest plantings could be accelerated if land now in mature forestry could be deforested and converted to alternative land uses without incurring financial penalties. BusinessNZ suggested that under this decoupling scenario,

there could be increased international interest by some markets in forestry-linked NZUs because of the absence of competing AAUs.

The Environmental Defense Fund (095) submitted that New Zealand should take steps to guarantee the environmental integrity of units entering the scheme.

Federated Farmers (137) submitted that there is dissatisfaction among landowners that much of their efforts go unrewarded under the ETS, e.g. forest plantings that fail to meet the post-1989 threshold and definition of afforestation.

Greenpeace (085) submitted that the ETs should be modified by the establishment of a domestic emissions cap, and through auctioning NZUs and limiting the availability of international credits. It also submitted that there will be limits to the availability of international credits, even with new binding commitments. New Zealand should refocus the ETS on domestic reductions.

Richard Leckinger (096), Simon Johnson (063) and 350 Aotearoa (063) also submitted that there should be a cap on domestic emissions.

Similarly, WWF NZ (055) submitted that access to offshore credits purchases should be limited and that NZUs should be auctioned. There should be an emissions cap on sectors covered by the ETS.

Environment and Conservation Organisations of NZ (161) submitted that the ETS should be redesigned to promote domestic emissions reductions. The price cap and 2:1 rule should be abolished and agriculture brought into the scheme from 2012. Free allocations should be clawed back and replaced with auctioned NZUs. Another option that Environment and Conservation Organisations of NZ submitted was to issue all citizens with transferrable carbon credits.

The New Zealand Farm Forestry Association (039) submitted that the Government should monitor forestry planting rates to ensure that 20,000 ha are afforested annually.

Ballance Agri-Nutrients (048) submitted that complementary measures should be introduced for agriculture to increase the rate of uptake of on-farm mitigation measures.

### ***Summary of those submission opposing increased incentives for domestic abatement***

The Greenhouse Policy Coalition (114) and Fletcher Building (076) were opposed to adjusting the ETS to promote domestic abatement.

Carbon Farm (102) submitted that the design of the ETS is satisfactory now. It is the price signal that is important to determine the speed of abatement changes.

The Employers & Manufacturers Federation (070) submitted that incentives for domestic emissions reduction should not be increased as domestic demand for energy is inelastic.

Holcim (112) submitted that it was too early in the life of the ETS to make a judgement around stronger incentives for domestic abatement and that this question should await the next scheduled Review.

NZ Steel (135) submitted that the ETS should facilitate lowest cost compliance.

## **Importance of access to international carbon markets**

A majority of submitters who provided views on this question agreed that access to international carbon markets is important. Twenty submitters suggested that such access is important while seven submitters suggested that access was not important.

### ***Summary of those submission considered access to international markets is important***

Several submitters commented that access to international markets is important to keep compliance costs for liable New Zealand emitters as low as possible. [Holcim (112), Oregon Group (080), Environmental Defense Fund (095), Qantas (158), NZ Steel (135), Shell (157), Sothern Forestry (029), Synlait Milk (046), Ballance Agri-Nutrients (048), Craigmore Forestry (144)]

Notably, submitters that otherwise had diverse views on design aspects of the ETS held a shared view on the importance of international carbon market access.

The Greenhouse Policy Coalition (114) considered that access is important however it is concerned about the implications of the European Union's ban on CERs.

BusinessNZ (149) submitted that international access is important, but that the Government should decouple the ETS from the trading elements of the Kyoto Protocol. The Government should facilitate access to fungible units from a wider range of other schemes internationally. BusinessNZ suggested that formal linking of the ETS to other emissions trading schemes is not required in order to maximise the efficiency of emission reductions. What is important is access to a choice of market mechanisms. Formal linking would impose constraints on scheme design that would reduce New Zealand's welfare. What is important is the acceptability of units from other emission trading schemes.

A contrary view from [withheld] was that the Government should seek to establish greater linkages between the ETS and overseas emissions trading schemes. Linkages should allow increased market liquidity, better alignment of carbon prices, greater efficiency in emissions reductions.

Contact Energy (089) submitted that ETS participants should be able to access international markets. The price of NZUs should not be different from a prevailing international price.

Carbon Farm (102) submitted that international access is important. However a ban on poor quality credits, such as industrial CERs should be enforced to maintain the integrity of the ETS.

Motu Economic and Public Policy Research (139) submitted that it was important that New Zealand had access to developing countries that might sell to us. It further submitted that the CDM was seriously flawed because of problems with additionality. New Zealand should consider bilateral partnerships with Pacific Island States or Latin American nations.

Fonterra (120) submitted that linking to international carbon markets is very important to ensure that the ETS offers the lowest cost abatement and that New Zealand should allow all UNFCCC

endorsed emissions units to be surrendered against ETS obligations. However environmental integrity of the units is important. Fonterra submitted that a domestic price cap is preferable to a situation where cash is transferred to foreign firms selling emissions units without environmental integrity. Fonterra noted the ETS should be integrated with foreign schemes only once policy development has reached a settled phase.

Pure Advantage (162) submitted that consideration needs to be given to how the ETS may link with other international schemes in the future. International linkages should be assessed on the basis of considerations, such as their effects on the New Zealand businesses active in global markets, and should not just give rise to capital outflows.

Forest Management (075) supported linking New Zealand AAUs to overseas carbon markets, particularly those in Australia and the EU.

### ***Summary of those submission considered access to international markets is less important***

Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) submitted that access to international markets should only be relied upon if there is a stable international framework agreement. It also noted that voluntary carbon markets will not represent credible, long-term tools for emissions abatement.

Greenpeace (085) submitted that access to international markets is not very important. A domestic emissions cap is more important.

The NZ Business Roundtable (083) submitted that potential linkages to international emissions trading may not materialise.

Environment and Conservation Organisations of NZ (161) submitted that access to emissions units internationally should be limited to increase domestic prices. Access to international markets blunts the incentive to reduce domestic emissions.

Solid Energy (027) submitted that linking to the EU ETS is problematic as the price of NZ units will be distorted by the demand and coverage of the EU ETS. This would lead to higher prices in New Zealand.

## **The development of domestic and international carbon markets beyond 2012**

Of the submitters that commented on this question, 80 per cent submitted that carbon markets would be slow to integrate and/or remain fragmented beyond 2012. A small number of submitters considered that carbon markets would develop rapidly and become integrated.

### ***Summary of those submission that considered carbon markets would develop slowly***

BusinessNZ (149) submitted that a liquid global carbon market is unlikely in the near to medium term and noted:

- The CDM is likely to continue approving projects that will create new tradable units

- AAs are unlikely to be available
- The UN will continue to have an important role in the monitoring, reporting and verification rules.

Carbon Market Solutions (145) submitted that international carbon markets will become increasingly fragmented. New Zealand could be flooded by low cost CERs as these are restricted in the EU ETS. There may be a shift towards regionally focussed markets. It thought the Government should refocus its attention to how and why the ETS could link with emerging overseas emissions trading schemes outside of Australia. (Carbon Market Solutions [145])

The Environmental Defense Fund (095) submitted that if there is no multilateral agreement, carbon markets will develop in domestic jurisdictions. Each jurisdiction will need to decide on linking and acceptability of credits from other schemes. If New Zealand links to a larger scheme it may be required to adopt similar rules, such as restrictions on eligibility of certain types of units.

Federated Farmers (137) submitted that domestic markets will become more focussed on serving the needs of ETS participants and national circumstances.

Greenpeace (085) submitted that the future of the EU ETS is relatively certain. New Zealand is unable to link to the EU ETS because of its treatment of forestry. Other emissions markets are highly uncertain.

Holcim (112) submitted that international carbon markets are likely to develop slowly with differing sectoral and gas coverage. It also submitted that there was considerable uncertainty about whether a market with features of the present Kyoto arrangements would persist beyond 2012.

Qantas (158) submitted that carbon markets are most likely to develop in line with scenario 3 where trading exists between regional schemes.

Straterra (084) submitted that there are unlikely to be markets that New Zealand emitters can access in any meaningful way.

Fonterra (120) submitted that the domestic market will change with forestry moving from becoming a source of units to having a demand for units. Demand for NZUs will further increase at the end of the transition phase and the entry of agriculture. It noted that the NZU price has closely followed the CER price. NZUs will move closer to the price of CERs as the demand for units increases and the supply of units offered by forestry decreases.

Solid Energy (027) submitted that the liquidity of the international market has not changed since 2008. There should be no linkage with the EUETS.

Synlait Milk (046) submitted that regional emissions trading schemes and bilateral agreements are the most likely arrangements to frame the future.

***Summary of those submission that considered carbon markets would develop rapidly***

Carbon Farm (102) submitted that carbon markets will grow exponentially in the next decade.

Richard Leckinger (096) submitted that there would be rapid development of international carbon markets after the USA and the EU developed linked schemes.

Environment and Conservation Organisations of NZ (161) submitted that volatility will subside and markets will become more discerning with branding and assurance of quality.

Southern Forestry (029) submitted that there will be liquid markets after 2012. New Zealand will be able to export large numbers of surplus carbon credits into these markets.

## 5 Transition phase

### Scaling the ETS up to full obligation (Question 13)

#### Summary of those submissions arguing the transition phase should end in 2012

Some submitters were of the view that the ETS should scale up to a full obligation. Two provided no reasons [David Slack (008), Craigmore Forestry (144)], however others gave the following reasons:

- The transition phase delays investment and behavioural change amongst businesses, investors and consumers to reduce emissions [Motor Trade Association (052), Waikato Regional Council (072), WWF NZ (055), Imported Motor Vehicle Industry Association (100), Motor Industry Association (037), Contact Energy (089), Greenpeace (085), Carbon Farm (102), Forest & Bird (110), Environment and Conservation Organisations of NZ (161)]
- Extending the transition phase would widen the gap between our international commitments and our likely future emissions, increasing the carbon deficit [Parliamentary Commissioner for the Environment (143)]
- The transition phase is a significant cost to taxpayers [Parliamentary Commissioner for the Environment (143)]
- The true cost of emissions should be borne by the emitters to incentivise emissions reduction [Nelson Forests (098)]
- The transition phase is a significant subsidy to polluters [Environment and Conservation Organisations of NZ (161)]
- The transition phase deters new forest planting [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- The transition phase dampens investment signals, potentially leading to inefficient allocation of resources [Wellington City Council (058)]
- It is likely that countries will continue to incentivise emissions reductions, although there is uncertainty in the emergence or viability of an internationally binding agreement [Contact Energy (089)]
- Scaling up to a full obligation could help New Zealand contribute to global cooperation on emission reduction [350 Aotearoa (064)]
- The transition phase should be removed to allow a true carbon market to develop, as transition measure make the ETS a carbon tax in disguise [Richard Leckinger (096)]
- An open market means that the ETS is likely to be less subject to political pressure [NZ Anglican Church Pension Board (113)]

- Extending the transition phase prevents the ETS from introducing a market price for emissions [OraTaiao: NZ Climate & Health (146)]
- Market prices have now approached the price cap [Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Price controls have not been required to prevent a price blowout for carbon in New Zealand [Carbon Farm (102)]
- Having a NZU price that is separate and distinct from a prevailing international price is unlikely to be efficient [Contact Energy (089)]
- There is no basis for extending the transition phase after allowing for free allocation and the ability to reduce emissions intensity [Forest Owners Association (077)]
- The recession is diminishing as a threat [Carbon Farm (102)]

Reasons for removing the fixed price option and for removing the one-for-two obligation are summarised in the subsequent sections.

OraTaiao: NZ Climate & Health (146) thought there was a good case for scaling up to a full obligation by 31 December 2011, earlier than currently scheduled.

## **Summary of those submissions arguing the transition phase should be extended**

Some submitters argued that the ETS should not scale up to a full obligation in 2012. Their reasons include:

- The end of the transition phase could lead to a loss of competitiveness and carbon leakage given the lack of progress of introducing a carbon price overseas [Cavalier Wool Holdings (038), Wood Processors' Association (042), Synlait Milk (046), Ballance Agri-Nutrients (048), ALSCO NZ (057), Fletcher Building (076), Straterra (084), KiwiRail (086), [withheld] , Rio Tinto (094), NZ Sugar Company (103), Holcim (112), Greenhouse Policy Coalition (114), Fonterra (120), [withheld] (121)]
- The submitter has no or limited ability to pass through ETS costs to customers [withheld] , NZ Sugar Company (103), ALSCO NZ (057), Qantas (158)]
- The loss of competitiveness caused by the end of the transition phase is not offset fully for those businesses that receive allocation and is not offset at all for those that are not eligible for allocation [NZ Coal & Carbon (111), Sanford (156), Fletcher Building (076), [withheld]]
- High degree of uncertainty surrounding the pricing of carbon internationally and the absence of international agreement [[withheld] (121), DairyNZ (061), Fletcher Building (076), KiwiRail (086), Holcim (112)]
- There are only limited prospects for a reliable, deep and liquid international carbon market [Carter Holt Harvey Pulp & Paper (040), Greenhouse Policy Coalition (114), Beef + Lamb New

Zealand, Meat Industry Association and Deer Industry NZ (107), Genesis Energy (053), Holcim (112)]

- Weak economic conditions remain and an extension would allow more time for the economy to recover [Cavalier Wool Holdings (038); Fletcher Building (076), [withheld], Methanex (105), Greenhouse Policy Coalition (114), [withheld] (121), NZ Sugar Company (103)]
- Uncertainty over the future international agreements and rules [Federated Farmers (137)]
- Other countries are still considering how they might respond to their international obligations [Federated Farmers (137)]
- Australia has not yet introduced a carbon price and there is uncertainty if it will do so [Horticulture NZ (148)]
- Extending the transition period to 2015 would broadly fit in with the proposed Australian scheme [Greenhouse Policy Coalition (114)]
- The carbon price remains hostage to the vagaries of action outside our borders [Federated Farmers (137)]
- The ETS is not in sync with other schemes [Federated Farmers (137)]
- Negligible progress in other countries including many of our trading partners and competitors [Methanex (105), NZ Coal & Carbon (111), Horticulture NZ (148)]
- There are strong indications that any new schemes implemented in the next five years will be highly moderated [Methanex (105)]
- We are leading the world and no-one else is following [Steve Wrathall (018)]
- New Zealand should only do its 'fair share' [Employers & Manufacturers Association (070), Greenhouse Policy Coalition (114)]
- Alignment with other countries [ALSCO NZ (057)]
- Consistent with the Government's previously stated position that movement to full obligation in 2013 is conditional on progress in reaching international agreements [[withheld] (121)]
- There is a serious risk New Zealand industries could be exposed to a high carbon price [NZ Business Roundtable (083)]
- Flow-on effects of the ETS in increased input costs negatively affect businesses [Wood Processors' Association (042), Nova Trust (066), KiwiRail (086)]
- Industrial companies in most cases have energy costs much higher than one per cent of their revenue [Greenhouse Policy Coalition (114)]
- For many coal users, there is no viable alternative energy source, so the carbon price is simply a cost impost and does not incentivise abatement [Straterra (084)]

- The end of the transition phase will further disadvantage domestic freight forwarding and coastal shipping industries in New Zealand, as international ships are not subject to the ETS. [KiwiRail (086)]
- The end of the transition phase could create domestic market distortions [withheld]
- New Zealand will be better placed to establish links with international emissions trading schemes once the transition period ends, resulting in deeper and more liquid carbon markets and reduced price separation [withheld]
- This would provide sufficient time for global climate change policy and other countries' climate change policy to acquire some certainty [NZ Sugar Company (103), Cavalier Wool Holdings (038)]
- The transition phase provides certainty about costs [Cavalier Wool Holdings (038), Ballance Agri-Nutrients (048)]
- The current marginal carbon price under the transitional arrangements already provides sufficient incentive for abatement where technically possible [Rio Tinto (094)]
- A high emissions price in New Zealand, in the absence of an emissions price in other large emitting countries, is unlikely to elicit a technology response from technology developments [Fletcher Building (076)]
- Availability of abatement technologies is limited [NZ Sugar Company (103), KiwiRail (086)]
- It would take a carbon price well above \$100/tonne to make a significant cut in fuel consumption, but such a high carbon price would cause massive disruption to the economy [Climate Realists (050)]
- The ETS as it stands does not achieve anything in terms of mitigating climate change, so any money spent on the ETS would be a waste of money [Climate Realists (050)]
- People are increasingly becoming concerned about the costs and impact of climate change policies on their standard of living and jobs [Greenhouse Policy Coalition (114)]
- There is no justification to proceed with an ETS at this time [Arthur Thorstensen (009)]
- The submitter does not believe in climate change/global warming. [Simon Breeze (021)]

Some submitters argued that the ETS should not scale up to a full obligation unless:

- There is equivalent action by other countries [Fisher & Paykel (019), Hamilton City Council (028)]
- Either a second commitment period for the Kyoto Protocol is agreed or a new multilateral successor agreement to the Kyoto Protocol is agreed [Carbon Market Solutions (145)]

Some submitters proposed that the ETS should not scale up until:

- The 2014 ETS review at least [[withheld] (121), Methanex (105), Holcim (112), NZ Business Roundtable (083)]

- A transparent and robust carbon price emerges or at least the end of 2017 [withheld], Genesis Energy (053)]
- There is more certainty about the future of the carbon market after 2012 [DairyNZ (061)]
- There is greater certainty about international obligations [KiwiRail (086)]
- At least the end of 2022 or ‘until such time as suitable metrics on the extent of international effort and its comparability have been met’ [Employers & Manufacturers Association (070)]
- At least the end of 2022 or until our trade competitors are taking action of comparable effort [BusinessNZ (149)]
- Our trade competitors have operational emissions trading schemes or similar [Seafood Industry Council (065), Carter Holt Harvey Pulp & Paper (040), NZ Sugar Company (103), Beef + Lamb New Zealand, Meat Industry Association and Deer Industry NZ (107), Sanford (156), Fletcher Building (076)]
- New Zealand’s developed nation partners have implemented obligations equivalent to a one-for-one, uncapped price. The price cap will also be needed until full recourse to international climate markets is available. [Fonterra (120)]
- The New Zealand economy is robust and fully recovered from the Christchurch earthquake [Qantas (158)]

## **Fixed price option (Question 13a)**

### **Summary of those submissions arguing the fixed price option should end in 2012**

Some submitters supported the removal of the \$25 fixed price option in 2012, as currently planned under the legislation. [Bill Sayer (014), Marlborough Forest Industry Association (030), OMFinancial (047), New Zealand Farm Forestry Association (039), Motor Industry Association; Wellington City Council (058), 350 Aotearoa (064), Forest Management (075), NZ Forest Owners Association (077), Greenpeace (085), Richard Leckinger (096), Nelson Forests (098), Carbon Farm (102), NZ Institute of Forestry (119)]

Forest & Bird (110) said the fixed price option should be removed earlier, at the end of 2011.

Environment and Conservation Organisations of NZ (161) said the fixed price option should be removed as soon as possible.

These submitters supported the removal of the fixed price option because:

- The fixed price option causes significant distortions in the market [Blakely Pacific (154), NZ Forest Owners Association (077)]

- A price cap makes it less attractive to buy NZUs relative to CERs, as it prevents the price of NZUs rising. As a result, the cap works as a disincentive to forestry investment. [Lake Taupo and Lake Rotoaira Forest Trusts (142), NZ Forest Owners Association (077)]
- It would provide the right incentives for investing in forestry, renewable energy and more efficient generation technology [Mighty River Power (130)]
- The more prices rise above \$25 the faster supply meets demand [Southern Forestry (029)]
- The Government should not allow any price cap to be accessed by emitters whilst NZUs are available at a lower price. If not, taxpayers may unnecessarily bear a higher cost [NZ Forest Owners Association (077)]
- The \$25 price cap could provide an arbitrage opportunity for third parties effectively selling internationally-traded CER's at a capped price of \$25 (i.e. subsidising the world market) [NZ Forest Owners Association (077)]

### **Summary of those submissions arguing the fixed price option should be extended**

Some submitters proposed that the \$25 fixed price option should remain after 2012. [Rio Tinto (094), Cavalier Wool Holdings (038), Wood Processors' Association (042), Synlait Milk (046), Ballance Agri-Nutrients (048), Nova Trust (066), Fletcher Building (076), Straterra (084)]

Their reasons for extending the fixed price option included:

- The fixed price option provides business certainty [Escea (006)]
- The removal of the fixed price would lead to volatility in NZU price [Greenhouse Policy Coalition (114), Ballance Agri-Nutrients (048)]
- The fixed price option mitigates the cost impact on business after 2012 [Gelita (017), TA & DM Turner (127), Heaphy Mining (128), Coal Association (132)]
- Removal of the fixed price option would expose the New Zealand economy to the prevailing international price of carbon. Emission unit prices may therefore rise significantly beyond \$25 per unit, resulting in consequential increases in ETS-related costs [withheld], Rio Tinto (094), Greenhouse Policy Coalition (114), [withheld] (121), Ballance Agri-Nutrients (048)]
- The ETS places New Zealand among world leaders rather than being in line with major trading partners [Gelita (017), TA & DM Turner (127), Heaphy Mining (128), Coal Association (132)]
- The lack of international progress to a second commitment period [Solid Energy (027)]
- The lack of action overseas [Solid Energy (027)]
- The lack of development of liquid international market [Solid Energy (027)]
- The weak state of the New Zealand economy [Solid Energy (027)]

Some submitters argued that the \$25 fixed price option should continue beyond 2012 until:

- The 2014 review [Gelita (017), TA & DM Turner (127), Heaphy Mining (128), Coal Association (132)]
- The end of 2015, and the extension should be revisited in 2014 review [Greenhouse Policy Coalition (114)]
- At least 2015 [Escea (006), Solid Energy (027)]
- The end of 2022 unless a significant number of other jurisdictions have similar obligations on their producers at an earlier date [Horticulture NZ (148)]
- The economy is used to operating with a carbon price [Escea (006)]
- There is greater clarity on long term commitments by major emitting countries [BOC (032)]
- Our key trading partners (China, USA, Indonesia, Japan) impose a similar cost of carbon on their steel industries [NZ Steel (135)]
- The international community has pulled its weight [Catherine Harris (136)]

Fonterra (120) suggested that the \$25 fixed price option should remain after 2012 if restrictions are needed on the type of CER units New Zealand firms may import. The rationale is that a price cap is preferred to a situation that results in a transfer of cash from New Zealand to foreign firms who are gaining from the system through producing CER units that do not actually represent emissions reduction.

NZ Anglican Church Pension Board (113) suggested that, on the assumption that the Government will desire some control over the price of emission units, the price cap should remain permanently, but adjusted annually for CPI inflation. The advantage of this option is that both sellers and buyers of units know where they are. However, the submitter noted that the capped price probably will not relate to a free market internationally.

Some submitters suggested that while the fixed price option should remain, it should be amended after 2012. Their proposals included:

- The level should increase by 4 per cent per annum in real terms to provide certainty to emitters and incentives to forestry [Forest Management (015)]
- The level should be set lower as a lower price would make it more appropriate to our economy [Rockies Mining (024)]
- The cap should be set lower [Horticulture NZ (148)]
- Carbon prices should be fixed for moderate periods, such as a year at a time [Porirua City Council (129)]
- A modest price cap [Mobil (140)]

- If the cap is not removed, then it should be increased to \$30 [Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- If a fixed price option of \$25 does not continue beyond 2012, some kind of upper limit may be needed to avoid carbon prices being determined solely by the global market [Fisher & Paykel (019)]

Some submitters noted that if the fixed price option is continued, then this has implications on other ETS design settings:

- The banking provisions should be revisited [Motu Economic and Public Policy Research (139)]
- The restriction on exporting NZUs ends in 2012 and therefore the price cap should be increased to prevent risk of arbitrage [Lake Taupo and Lake Rotoaira Forest Trusts (142)]

NZ Institute of Forestry (119) noted forest owners effectively have to sell their units at or below the price cap because of limited acceptance of our forestry units by international carbon markets.

NZ Forest Owners Association (077) argued that, if the price cap remains, then the Government should be prepared to offer the same level of guaranteed inflation-adjusted price protection to foresters at harvest.

Some submitters provided some comments which are relevant to the fixed price option but are neutral as to whether the fixed price option should continue beyond 2012. These comments include:

- There should be a reassessment of the pricing. There is a need to ensure ETS participants remain competitive, but continuing the fixed price option of \$25 will not promote a significant change of behaviour to reduce emissions. [Origin Energy (122)]
- The Australian Framework for a Carbon Price Mechanism provides useful criteria for the transition from a fixed price to variable price cap and trade scheme. [Ballance Agri-Nutrients (048)]

## **One-for-two obligation (Question 13b)**

### **Summary of those submissions arguing the one-for-two obligation should end in 2012**

Some submitters supported the abolition of the one-for-two obligation in 2012. [OMFinancial (047), New Zealand Farm Forestry Association (039), Wellington City Council (058), 350 Aotearoa (064), Forest Management (075), NZ Forest Owners Association (077), Greenpeace (085), Richard Leckinger (096), Nelson Forests (098), Imported Motor Vehicle Industry Association (100), NZ Anglican Church Pension Board (113), Carbon Farm (102), NZ Institute of Forestry (119)]

Forest & Bird (110) argued the one-for-two obligation should be abolished earlier, at the end of 2011.

Environment and Conservation Organisations of NZ (161) said the one-for-two obligation should be abolished as soon as possible.

Most of these submitters provided reasons for supporting the abolition of the one-for-two obligation. Their reasons included:

- The one-for-two obligation reduces the effectiveness of the scheme [Bill Sayer (014)]
- Removing the one-for-two obligation would increase demand for units increasing carbon market liquidity [Forest Management (015), Mighty River Power (130)]
- The one-for-two obligation does not apply to liabilities arising from deforestation. It is unfair that the forestry sector faces such punitive measures. [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]

### **Summary of those submissions arguing the one-for-two obligation should be extended**

Some submitters proposed that the one-for-two obligation should continue beyond 2012. [Rio Tinto (094), Cavalier Wool Holdings (038), Wood Processors' Association (042), Ballance Agri-Nutrients (048), Nova Trust (066), Fletcher Building (076), Greenhouse Policy Coalition (114)]

Origin Energy (122) commented that the one-for-two obligation could be maintained in the interim.

The reasons for continuing the one-for-two obligation beyond 2012 included:

- The removal of the one-for-two obligation will at least double the ETS costs for New Zealand businesses. [NZ Sugar Company (103), Cavalier Wool Holdings (038), Ballance Agri-Nutrients (048), Fletcher Building (076), Sanford (156)]
- The one-for-two obligation reduces the effective price of emissions to a level which has less potential to be disruptive. [Fletcher Building (076)]

Some submitters argued that the one-for-two obligation should continue beyond 2012 until:

- There is greater clarity on long term commitments by major emitting countries. [BOC (032)]
- The international community has pulled its weight. [Catherine Harris (136)]

Some submitters suggested that the one-for-two obligation should be amended after 2012. Their proposals include:

- A one-for-four obligation until the 2014 review or until progress is made in international negotiations or until a global carbon price/international carbon market has emerged [Gelita (017), TA & DM Turner (127), Heaphy Mining (128), Coal Association (132), ALSCO NZ (057), GL Bowron & Co (074), Straterra (084), NZ Coal & Carbon (111)]
- A two-for-three obligation because there should be progressive movement towards a full obligation [Fisher & Paykel (019)]

Mighty River Power (130) commented on the consequences of extending the one-for-two obligation. It submitted that if the one-for-two obligation was extended for a couple of years, this would not have a materially detrimental effect on the build profile in the electricity market if there is a predictable step-up at the end of that period and the price cap is raised significantly higher.

## **Importance of certainty about the transitional phase**

Contact Energy (089) commented that there needs to be certainty about whether the transition phase will be extended or not. Regulatory certainty is needed to support investment decisions, and there needs to be a consistent signal to customers about the associated emissions impacts of their consumption decisions.

Two submitters commented that uncertainty around the application of the transition phase after 2012 influences commercial considerations surrounding alternatives to meet surrender obligations [Contact Energy (089), Origin Energy (122)].

## **Amendments to industrial allocation if the transition phase is not extended**

NZ Sugar Company (103) proposed that, if the transition phase expires at the end of 2012 as scheduled, the existing criteria for industrial allocation should be amended to ensure all persons who are materially trade-exposed are provided with assistance.

## **Price floor**

Genesis Energy (053) suggested introducing a carbon price floor. This could provide a level of protection to investors in mitigation projects from the risks of carbon price uncertainties.

## **Other comments about the transition phase**

Lake Taupo and Lake Rotoaira Forest Trusts (142) suggested that the Government should not sell NZUs to emitters if the market price is below the price cap.

Forest Management (015) considered that the ability to sell NZUs in international markets should be retained.

Greenhouse Policy Coalition (114) cautioned the Panel about the International Energy Agency (IEA)'s comment that 'New Zealand would be more likely to meet its domestic emissions reduction targets for 2020 and 2050 if the ETS had a firm cap and no fixed price'. The submitter said that the 2020 target is highly conditional and the IEA does not address this conditionality or the surrounding uncertain carbon pricing by our trading competitors.

Greenpeace (085) said subsidies to enable a transition should be separated from the price signal and should be aimed at vulnerable individuals and workers needing to transition to new employment.

## 6 Agriculture

### The extent of agriculture sector abatement options (Question 14)

#### Relevance of abatement options to the participation of agriculture in the ETS in general

This section summarises the generic comments submitters made about the relevance of abatement options to the level of sector participation. There were many more responses that related to specific sectors, and they follow in the next section.

Six submitters felt that the level of abatement options is relevant to the level of a sector's participation:

- Four submitters noted that the end goal has to be to reduce emissions so abatement options must be incentivised [Escea (006), Fisher & Paykel (019), Rockies Mining (024), Wellington City Council (058), GL Bowron & Co (074)], and that abatement options will become more attractive as the cost of carbon increases [Wellington City Council (058)].
- Two commented on the need to avoid 'carbon leakage' to our competitors [Hamilton City Council (028), Straterra (084)], with one adding that serious consideration should be given to ensuring New Zealand's EITE sector is adequately protected to prevent unnecessary harm to the national economy from carbon leakage [Straterra (084)].
- One noted that the levers within the ETS framework provide for variations in abatement capacity to be managed over time [Contact Energy (089)].

Six submitters said the level of abatement options is not relevant to the level of a sector's participation, and gave the following reasons:

- The full involvement of all sectors, all gases is important [Richard Leckinger (096), NZ Steel (135)] as do further submitters, as recorded in later sector-specific comments
- The two policy objectives are non-commensurate. The inclusion of a new gas might be justified by the easy availability of a low-cost abatement option, but not if this would breach the overriding 'fair share' principle [Employers & Manufacturers Association (070)]
- Abatement options will develop, and there are many available now in the energy sector [Environment and Conservation Organisations of NZ (161)]
- Free allocations distort the scheme and should stop [Bill Sayer (014), Steve Wrathall (018)].

Other comments included:

- It is the cost of abatement options that is really in question. It is always possible to abate, but the cost to do so may be prohibitive and result in leakage or closure [Holcim (112), Bank of New Zealand (124)].

- The ETS should be abandoned right now, so there are no future costs [[withheld] (081)].

## **Relevance of abatement options to agriculture sector participation**

### ***Summary of those submissions which thought it is relevant for agriculture***

Many submitters felt the level of abatement options is relevant for agriculture. [Talleys (007), Taranaki Regional Council (016), Taumarunui Sustainable Land Management Group (031), NZ Farm Forestry Association (039), Ballance Agri-Nutrients (048), DairyNZ (061), Forest Management (075), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Greenhouse Policy Coalition (114), Pastural Farming Climate Research (131), Origin Energy (122), Coal Association (132), Federated Farmers (137), Motu Economic and Public Policy Research (139), BusinessNZ (149), Qantas (158)]

Reasons included:

- The *lack* of abatement options (many stated this is a reason).
- Federated Farmers (137) submitted that significant time (i.e. beyond 2015) is required before research can be expected to deliver abatement technologies. Some of the difficulties faced are:
  - The complexity of biological systems
  - Agriculture emission reductions effects on other greenhouse gases
  - There is still a growing understanding of the processes that generate farming emissions
  - The challenge of applying unproven technologies across widely variable farm types and farming conditions
  - The uncertainty of the cost-effectiveness of technologies and the impacts they might have on product quality, quantity and consistency, and animal welfare.
- Some thought abatement options should not be the primary or only consideration. The sector's ability to remain competitive and the linkages with other sectors already participants must also be assessed, such as agriculture's reliance on fertilisers derived from petroleum products [Origin Energy (122)]. To over-weight this characteristic risks placing the Government in the position of second-guessing from where, and when, new technologies will come forward [BusinessNZ (149)].
- One noted, in response to this question, that agriculture overall does have a wide range of abatement options [Carbon Market Solutions (145)]. Several others make this point in response to later questions.
- One added that the agriculture sector needs certainty, and can't wait for the 2014 review [Pastural Farming Climate Research (131)].

Further reasons why abatement options are relevant to the agriculture sector are given later, in the context of submitters' views on when agriculture should enter the ETS.

### ***Summary of those submissions which thought it is not relevant for agriculture***

Eleven submitters' comments stated or indicated that they thought the level of abatement options is to some extent not relevant for agriculture for reasons including:

- The Panel and the Government should not be making judgments as to where abatement opportunities lie. The whole point of a market mechanism is to identify these in an efficient manner rather than to have some central authority 'pick winners'. If a 'winner picking' approach were to be taken to agriculture it should logically be applied to other industries with perceived limited abatement opportunities. Carve-outs would lead to generalised special pleading for exemptions and undermine the integrity of the scheme [NZ Business Roundtable (083)]
- Nor is the exclusion of agriculture by other countries a reason for exclusion by New Zealand. Liquid fossil fuels would also be excluded on that basis [NZ Business Roundtable (083)]. Others note that agriculture is not the only sector which has limited technological ability to reduce emissions [NZ Steel (135), Qantas (158)]
- Several submitted the lack of abatement options is perceived not real, that options to reduce emissions do exist, often appear to be understated or need to be encouraged by a price signal to drive investment in abatement options [Greenpeace (085), Nelson Forests (098), Forest & Bird (110), Sustainability Council (151), Carbon Farm (102), Lakes Taupo and Rotoaira Forest Trusts (142), Environment and Conservation Organisations of NZ (161)]. Some felt that existing opportunities are being insufficiently applied at present. One of them, Sustainability Council (151), submitted agriculture has more short-term options than other sectors, and that agriculture represents New Zealand's largest source of low cost abatement options
- One submitter added that where firms cannot reduce their emissions their costs relative to lower emission substitutes should rise so that people consume less of the higher emission products and services. This should then help drive investment decisions in favour of lower emission products and services. [Greenpeace (085)]
- The cost must be equitably levied across all sectors sooner rather than later, and this will make abatement more accessible if lower targets are available than trying to abate emissions steeply in the future. [Carbon Farm (102)]
- It's not relevant [Southern Forestry (029)]. All sectors can implement abatement by financing sequestration activities equivalent to their emissions [Euan Mason (108)]
- Agriculture and dairy are going to destroy the country's economy and environment [Phrenology Support Group (023)].

### ***Examples provided of abatement for agriculture***

Some submitters noted opportunities that are immediately available or in development for the agriculture sector. [Hamilton City Council (028), NZ Forestry Owners Association (077), NZ Fertiliser Manufacturers' Research Association (091), Ecologic Foundation (090), Lake Taupo and Lake Rotoaira Forest Trusts (142), Carbon Market Solutions (145)]

These opportunities included:

- Nitrification inhibitors. One noted that they reportedly could reduce nitrous oxide emissions by 44-57 per cent [Sustainability Council (151)], another by 30-70 per cent [Fonterra (120)] and another noted it depended on region and conditions [Hamilton City Council (028)].
- Nutrient management planning advice and tools
- Best practice farming
- Stock management
- Dairy wintering pads and barns
- Dairy methane capture
- Lower-protein supplementary feeds
- Adding biochar to soil. Oregon Group (080) noted that biochar reduces Nitrous Oxide emissions from some soils under dairy pasture by up to 70 per cent.
- Biofuel use and biogas for energy. Oregon Group (080) noted that they are positioned to deliver both bio oil (as a liquid fossil fuel substitute) and biochar to markets.
- Renewable energy generation
- Afforestation and forest offsetting, and on marginal hill country a lot more could be planted [NZ Forestry Owners Association (077), Carbon Market Solutions (145)].

Others noted that the incentive is there and progress is being made, but that more time is needed:

- Current pressures on freshwater, particularly from intensive dairying, and the generally accepted call for limit setting through regulation will provide a parallel economic incentive or requirement to do agriculture differently over time [Forest & Bird (110)].
- The dairy industry has ambitious targets for research into developing mitigation technologies, and is confident that this research will result in the development of proven, practical, economically-viable tools to mitigate emissions of agriculture-based gases and lower the greenhouse gas intensity of dairy production. However, more time is needed for this research to produce results that are proven and farm-ready. [DairyNZ (061)]
- Investment in emissions reduction research equates to over \$1000 per dairy farm. Industry and Government have invested \$45 million in agriculture greenhouse gas mitigation research (half each) [Fonterra (120)].

- New Zealand's participation in international research on pastoral greenhouse gases is the appropriate means of addressing practicable abatement measures [Coal Association (132)].

## **Views on when the agriculture sector should enter the ETS**

### ***Exclude agriculture***

Six submitters suggested that agriculture should be excluded from the ETS, because:

- There are very limited abatement opportunities [Talleys (007)]
- It will not maintain our competitive advantage in the primary export industries [Talleys (007)]
- Taxing producers of fresh produce makes us trade exposed to importation and exportation of our produce [Tony Norton (036)]
- The calculation of the farming sector being responsible for 50 per cent of New Zealand's emissions is seriously flawed [Talleys (007)].
- The carbon cycle is balanced and methane production from animals and its heating value is flawed [Peter Foster (012), David Lloyd (026), Pastural Farming Climate Research (131)]
- Instead, duplicate Australia's proposed Carbon Farming Initiative [Pastural Farming Climate Research (131)].
- Remove or at least signal with some certainty within a specified timeframe the introduction of agriculture. The delayed entry of agriculture has contributed to significant distortions to market pricing of emissions [Blakely Pacific (154)].

### ***Delay or review agriculture***

Thirteen submitters suggested that agriculture's entry should be delayed, or reassessed at the 2014 review, for reasons including:

- Until proven and effective emissions reduction options are available [Taranaki Regional Council (016), Taumarunui Sustainable Land Management Group (031), Ballance Agri-Nutrients (048), DairyNZ (061), Greenhouse Policy Coalition (114), Bank of New Zealand (124)]. Otherwise the ETS acts more as a penalty than as a market incentive and this is inefficient at producing the desired outcome at least cost [Taranaki Regional Council (016)].
- Until the sector is proven to be able to financially meet the obligations [Taumarunui Sustainable Land Management Group (031)]
- Until there is an international accord [Bank of New Zealand (124)]
- Until three years after the completion of any post-Kyoto agreement. This sector has the lowest growth in emissions since 1990 of all sectors, and emissions intensities per kg of product are improving. [Climate Realists (050)]
- Until far beyond 2015 (if not excluded) [Federated Farmers (137)], because:

- New Zealand is the only country attempting to do so
  - Feeding a growing population is more important than reducing emissions
  - We are a more efficient food producer than other countries
  - Farming cannot reasonably reduce emissions without reducing production
  - There is too much emphasis on reducing temporary non-CO<sub>2</sub> gases
  - The burden of the ETS will put many farmers out of business
  - The cost to the New Zealand economy will be too great to withstand
- Until the start of 2018 with its inclusion in the scheme to be revisited at the 2014 review. It is not equitable for agricultural gases to come in without practicable abatement measures being available. No other countries are close to doing this. The only abatement option realistically available at present is to cut output, which will simply be picked up by other countries which have no carbon price. Allocation would surely have to be at 100 per cent to satisfy the requirements of fairness. [Greenhouse Policy Coalition (114)]
  - Until at least 2020 [Solid Energy (027)]
  - Flexibility is needed on an optimum date [Climate Change Iwi Leadership Group (159)]
  - Specify a variable date, depending on a number of factors relating to a clear transition path based on practical sectoral considerations [BusinessNZ (149)]. As an all-sectors, all-gases scheme, all sectors, should in principle, enter the ETS and face a price signal. This is important for inter-sector equity. At a minimum, it is important for the Government to send sectors a credible signal as to their inclusion in the ETS in order to spur action prior to actual inclusion and to make the entry of the sector more managed when it occurs. [BusinessNZ (149)]
  - Reassess it in the 2014 review, in line with other countries [Fonterra (120)].

### ***Keep agriculture on the current schedule***

Fifteen submitters suggested that agriculture's entry should proceed on schedule, or indicated the desirability of this, for reasons including:

- Stick to the announced plan; agriculture needs certainty more than almost anything else [Fisher & Paykel (019)]
- There should be no further deferral [Wellington City Council (058), NZ Institute of Forestry (119)]
- Since it makes up approximately 50 per cent of New Zealand's emissions and is such a key contributor to New Zealand's emissions profile it must be included [Forest Management (075), NZ Forest Owners Association (077), Lake Taupo and Lake Rotoaira Forest Trusts (142), Parliamentary Commissioner for the Environment (143)]

- It is important that agriculture faces a price signal from the ETS [NZ Forest Owners Association (077), Oregon Group (080), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. Reasons given were, because it comprises such a proportion of our emissions [NZ Forest Owners Association (077), Lake Taupo and Lake Rotoaira Forest Trusts (142)] and that it is very important to ensure uptake of abatement (especially for dairy) [Oregon Group (080)].
- The ETS is 'all gases and all sectors' [NZ Forest Owners Association (077), Vector (097), Kyoto Forestry Association (078), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Equity for other sectors [Forest Management (075), Seafood Industry Council (065)]. Forest Management (075) explained that if agriculture's entry is delayed further, the other sectors and New Zealand generally continue to subsidise agricultural emissions, and by 2020 this could be to a significant level if no inroads are made to reduce agricultural emissions. The Parliamentary Commissioner for the Environment (143) also noted that, if they are not met by emitters, liabilities will have to be met by the taxpayer.
- Excluding agriculture is material to forestry as a sector that competes on price for the same land base [Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- The sooner agriculture is brought into the ETS the sooner an effective free market for GHGs will be established and the better the cap and trade system will work to reduce the production of GHGs [NZ Farm Forestry Association (039)]
- Its effect on the availability of units in the local market [Vector (097)]
- Provide leadership and demonstrate commitment in this area, and send a signal that agriculture will be part of the ETS [Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Backtracking on bringing agriculture into the ETS would also send a negative signal to the international community. It would bring into question our commitment to carbon reductions and be likely to affect our clean green image. New Zealand's agricultural science is advanced by international standards and is in a good position to produce innovative emission-reducing technologies. Moving to a low-carbon agricultural model would further enhance our environmental credentials in the international marketplace [Parliamentary Commissioner for the Environment (143)]. Others including [Qantas (158)] expressed similar views.
- The co-benefits of bringing agriculture into the ETS would be large, especially accelerating the uptake of afforestation on erosion- and flood-prone hill country; and reducing nitrogen leakage from farms into water [Ecologic Foundation (090)]
- One added that the ETS should not treat agricultural sectors differently from others, when considering exempting agricultural activities [withheld]

Despite their stance, NZ Farm Forestry Association (039) submitted that there will be real difficulties in bringing agriculture in.

### ***Earlier inclusion for agriculture***

Five submitters suggested that agriculture's entry should, if anything, proceed ahead of schedule, for reasons including:

- As planned, however Carbon Market Solutions (145) proposes a 'voluntary opt-in' for agriculture prior to 2015, providing reporting is undertaken. This would mean farmers can earn units by undertaking projects within the ETS, such as activities related to methane capture and biogas to energy.
- A more rapid introduction would encourage sequestration through afforestation on marginal lands, potentially improve prospects for our agricultural exports, reduce erosion and make our hill country farms more profitable. All we lack is the conviction to make this happen. [Euan Mason (108)]
- Agriculture should be introduced earlier, in 2012, with a transitory period that phases out grand-parenting by 2020. The sector does have some current mitigation options and the price signal will create additional incentive to innovate to find other mitigation options. [Forest & Bird (110)]
- Agriculture should enter earlier than 2015, and assume full liability by 2015 [Environment and Conservation Organisations of NZ (161)]
- Urgent inclusion, with full exposure much earlier than scheduled because there is scope for abatement already in agriculture and we cannot afford to shield these sectors from reality and the necessary learning curve [OraTaiao: NZ Climate & Health (146)].

### **Alternatives or interim approaches to the inclusion of agriculture**

Submitters offered the following additional, alternative or interim approaches to the inclusion of agriculture in the ETS:

- Replace the ETS with legislated practices and actions to reduce emissions, e.g. energy standards [Talleys (007)]
- Consider alternative and more bottom-up market-based mechanisms to improve incentives for mitigation in the agriculture sector [Pure Advantage (162)]
- Complementary targeted policy measures are also needed. Good examples include the Global Research Alliance on Agricultural Greenhouse gases and the NZ Centre for Agricultural Greenhouse Gas Research [Mighty River Power (130)]
- Promote best practice solutions for agriculture to drive behaviour change (e.g. riparian plantings) [Taranaki Regional Council (016)]
- An adjustment scheme facilitating meat and wool farmers moving large parts of their properties into land retirement and/or afforestation. The SLUI model operated by the Horizons Regional Council should be expanded and speeded up to assist hill country farmers to adjust to their entry into the ETS. [Ecologic Foundation (090)]

- Some simple system like allowing farmers an exemption from paying for their emissions for a certain number of years if they plant an area of trees equal to a percentage of their total farm area. The European Union has an ‘agricultural set-aside programme’, which may provide a suitable model. [NZ Farm Forestry Association (039)]
- Incentives (e.g. through offsets, credits and subsidies) rather than penalties are provided by other countries (e.g. USA, Australia and EU) for their agriculture sectors to reduce emissions [Fonterra (120)]
- A mechanism to share the gains of reduced agricultural greenhouse gas emissions between state and farmer [NZ Fertiliser Manufacturers’ Research Association (091)]
- A carbon tax on urea or nitrogen based fertilizers (except eco nitrogen fertiliser) which are responsible for a variety of green house gases and pollute our waterways [M Dumbar (010)].

## **Comments on the agriculture point of obligation relevant to abatement**

### ***Farm-level point of obligation for agriculture***

Thirteen submitters, from both the forestry and agriculture sectors felt the agriculture point of obligation should be at the farm level, for reasons including:

- To incentivise farmers to take direct action to reduce emissions, and some added that it would allow them to benefit from reductions. [NZ Farm Forestry Association (039), Climate Realists (050), DairyNZ (061), NZPork (068), Waikato Regional Council (072), Forest Management (075), NZ Fertiliser Manufacturers’ Research Association (091), Pastoral Farming Climate Research (131)]
- Much greater chance of achieving the desired outcome [Kyoto Forestry Association (078)].
- It is where the abatement decisions are made [Greenhouse Policy Coalition (114)]
- Charging farm emissions via a processor means they will simply on-charge their supplier farmers with a tax, which would be blunt and inequitable [NZ Farm Forestry Association (039)]
- Processors will pass the carbon cost on to farmers by an average charge, which will not distinguish between inefficient and efficient farmers and will not provide incentives for them to reduce their emissions [Fonterra (120)]
- The pork industry’s emissions are sufficiently diverse that emissions profiles, mitigation measures, and carbon liabilities cannot be averaged and accounted for at any level except at the farm [ (068)]
- Most of agriculture emissions (85 per cent) are on-farm and only 10 per cent from processing [Fonterra (120)]
- One way of achieving this, suggested by Fonterra (120), would be to allow farmers to opt-in to farm level reporting in order to receive benefit for mitigation activities. Fonterra would offer to trade emission units on behalf of farmers

- The tools and processes already exist to measure and report on emissions at farm level (e.g. nutrient management services) [NZ Fertiliser Manufacturers' Research Association (091)].
- Others also mentioned wanting a farm level point of obligation [including Ballance Agri-Nutrients (048), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]

### ***Processor-level point of obligation for agriculture***

Motu Economic and Public Policy Research (139) preferred retaining the agriculture point of obligation at the processor level, at least in the meantime. They submitted that if the current processor based approach can be implemented in a simple way it might form a useful transition into a longer term policy. It should be designed to facilitate such a transition. However trying to create a more complex system may, at this stage, not be worthwhile particularly if it creates momentum away from a good long-run solution.

## **Conditions under which the agriculture sector should enter the ETS (Question 15)**

### **Conditions of sector entry to the ETS in general**

This section summarises the generic comments submitters made about what conditions should determine when sectors enter the ETS and incur surrender obligations. Conditions suggested included:

- If they are emitters [Rockies Mining (024), Environment and Conservation Organisations of NZ (161)]
- If they are significant emitters, otherwise they will be subsidised by taxpayers or low emitters [Carbon Farm (102)].
- As soon as feasible abatement options exist [Greenpeace (085), Methanex (105)]
- Assess sectors' supply chain especially, if a key link in that chain is already a participant [Origin Energy (122)]
- Proceed with caution, given New Zealand's relatively small economy and limited research and development potential in low carbon technologies [Hamilton City Council (028)]
- Only if a sector is already subject to comparable imposts with all major trading partner countries such as Australia, USA, China and Japan [Employers & Manufacturers Association (070), Seafood Industry Council (065) Hamilton City Council (028)]
- Not until international global warming is proven [David Slack (008)].

Some submitters thought there should be no conditions of entry, for reasons including:

- No special conditions, same rules for all emitters [Bill Sayer (014), Fisher & Paykel (019), Richard Leckinger (096), NZ Steel (135)]

- It is never obvious before the event, how a new sector might develop [Fisher & Paykel (019)]
- To let the market reveal where the response opportunities lie as politicians and officials are no better at picking who can and who cannot reduce their emissions [Sustainability Council (151)].

Two submitters were satisfied with the status quo [Holcim (112), Employers & Manufacturers Association (070)].

## Conditions of sector entry to the ETS

### *Conditions suggested*

Conditions suggested for the entry of the agriculture sector into the ETS included:

- When comparative actions are taken and prices on carbon are faced by other countries and our overseas trade competitors. [NZ Climate Science Coalition (003), Taranaki Regional Council (016), Fisher & Paykel (019), Ballance Agri-Nutrients (048), DairyNZ (061), Nova Trust (066), NZPork (068), NZ Fertiliser Manufacturers' Research Association (091), ExportNZ (104), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Greenhouse Policy Coalition (114), Bank of New Zealand (124), Pastoral Farming Climate Research (131), Coal Association (132), Catherine Harris (136), Federated Farmers (137)]. Reasons included:
  - To avoid distortions in the market place [Taranaki Regional Council (016)]
  - To maintain competitiveness [Ballance Agri-Nutrients (048)]
  - To avoid penalising one of the most efficient food producers in the world, in the face of rising food shortages [Taranaki Regional Council (016), Federated Farmers (137)]
  - To avoid eroding horticulture profitability further [Nova Trust (066)]
- In line with the availability and encouragement of uptake of affordable abatement options [Ballance Agri-Nutrients (048), DairyNZ (061), NZ Fertiliser Manufacturers' Research Association (091), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Greenhouse Policy Coalition (114), Bank of New Zealand (124), Coal Association (132), Federated Farmers (137), Motu Economic and Public Policy Research (139), BusinessNZ (149)]. The Climate Change Iwi Leadership Group (159) added the need for practical investment in research to find technology solutions.
- Furthermore these abatement options must be internationally recognised and reflected in the National Inventory or under international rules [Ballance Agri-Nutrients (048), Federated Farmers (137)]
- When it is an affordable and predictable scheme, and the benefit outweighs the cost (one submitter referred to NZIER's assessment that this is necessary to be net welfare enhancing) [ExportNZ (104), Fonterra (120)]
- Farmers cannot absorb the cost of the ETS [Catherine Harris (136)]

- When the administrative and compliance costs of inclusion is not high [Motu Economic and Public Policy Research (139)]
- When internationally recognised measurement, reporting and verification methods can be implemented at the enterprise level [Ballance Agri-Nutrients (048), Qantas (158)]
- When there is an effective set of rules for land use, land-use change and forestry (LULUCF) [Greenhouse Policy Coalition (114)]
- When there is greater certainty around the form and magnitude of any greenhouse gas emission reduction commitments in a legally binding multilateral agreement [DairyNZ (061)]
- When there is access to a broad and liquid international carbon market [Greenhouse Policy Coalition (114), BusinessNZ (149)]
- When there is support among the public [Greenhouse Policy Coalition (114)]. Their survey found last year found nearly 47 per cent of people thought farming should not be in the ETS, while just over 45 per cent thought it should be included.

Fisher & Paykel (019) noted, however, New Zealand might need to move ahead of countries that are dragging their heels. Waikato Regional Council (072) felt New Zealand should not lead or lag. Craigmore Forestry (144) felt that short-term shielding as new sectors enter is appropriate provided there is a very clear and defined period for the scaling up to full responsibility for emissions.

Fonterra (120) said that the ETS should be flexible on the method for including agriculture emissions, especially if integrating with different international schemes, as it would not be sensible for New Zealand farmers to purchase units/credits from overseas competitors with higher emission intensities. Ecologic Foundation (090) noted the need to obtain a marginal price signal.

Some submitters mentioned the need to do New Zealand's fair share with respect to emission reductions and because the agriculture sector accounts for 50 per cent of emissions the sector must be included [Waikato Regional Council (072), Vector (097), ExportNZ (104)].

Some also noted that it must be an all sectors, all gases scheme [OraTaiao: NZ Climate & Health (146), BusinessNZ (149), Climate Change Iwi Leadership Group (159)].

Southern Forestry (029) thought there should be no particular conditions of entry for agriculture, because 'the faster the better'. They thought that the agriculture sector, the largest emitter, has the greatest ability to respond and benefit from the ETS simply by changing land use.

### ***Satisfaction with current ETS implementation plan***

Nine submitters indicated that they were satisfied with the current ETS implementation plan [Escea (006), NZ Forest Owners Association (077), NZ Business Roundtable (083), Vector (097), Nelson Forests (098), NZ Institute of Forestry (119), Mighty River Power (130), Pure Advantage (162)].

Reasons given included:

- Agriculture is 50 per cent of New Zealand's emissions [Waikato Regional Council (072), NZ Business Roundtable (083)]
- For long term economic, competitiveness and marketing benefits, which have been understated [Waikato Regional Council (072)]
- The primary production sector represents a major opportunity for 'green growth' but the uncertainty around the agricultural sector and the ETS is an investment killer [Pure Advantage (162)]
- For equity with other industries and taxpayers [NZ Business Roundtable (083), Vector (097)].
- To incentivise investment in afforestation. Withdrawing agriculture will undermine investment in new forests [Nelson Forests (098), NZ Institute of Forestry (119)]
- Changes in land use management will not occur unless there are clear pressures to do so from a carbon market [Mighty River Power (130)]
- Early adapters should not be disadvantaged by changes that avoid or delay the ETS effects, for example, they could be unreasonably commercially disadvantaged if they have already made significant investments in new forestry [Mighty River Power (130)].

Motu Economic and Public Policy Research (139) advised to be very careful about making changes to policy when there is little new information. They explained that this only induces policy uncertainty. In particular, the agricultural emissions part of the ETS is an area where the solutions are still not clear and the best path is probably to make no changes until we can make a change with confidence.

### ***Dissatisfaction with current ETS implementation plan***

Six submitters indicated that they were not satisfied with other aspects of the current ETS implementation plan (over and above whether agriculture sector entry should be deferred or removed), as listed below:

- NZ Pork (068) sought to postpone the introduction of 'minor' agricultural industries to the ETS until an appropriate level of investigation into New Zealand-specific emissions factors has been completed. They submitted that there is uncertainty in the current IPCC values used to develop the New Zealand specific emission factors for pigs, so recommend to delay the inclusion of the industry into the ETS until the international review of the IPCC's 2006 guidelines are complete
- Two submitters sought to exclude the layer hen industry from the ETS. They said that it is not fair that an estimated 10 per cent of the hen flock may be in backyard or semi-commercial flocks that are not required to be participants. There is no fair measurement tool for all egg producers, for calculating emissions, and there is no signal to reduce or reward emissions reductions. It is unfair that horses are exempt, when they emit more emissions than the entire national flock of layer hens. The definition of 'poultry' (excluding layer hens) should use the term 'poultry meat birds'. [[withheld], [withheld]]

- Another, that other sectors should be kept out of the ETS because there will be less problems when it folds [Raymond Scampton (025)]
- BusinessNZ (149) suggested that there may be other ways of thinking about agriculture such as (i) raise the current level of allocation to 95 per cent, (ii) stagger entry of the different agricultural gases and/or (iii) include agriculture but reduce the \$12.50/tonne fixed price
- NZ Fertiliser Manufacturers' Research Association (091) noted that there is considerable uncertainty within the agriculture community that the ETS agriculture schedule will actually be adhered to. The consequence is the lack of an economic driver and discouragement of investment in the commercialisation and uptake of agricultural mitigation technologies, thereby hindering the sector to take timely and full advantage of the opportunities available to it
- Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) said the agriculture regulations will result in a significant wealth transfer from the red meat sector to the dairy sector because the regulated 'emissions factors' apply the emissions created through a cow or ewe's pregnancy and lactation to its offspring. As the red meat sector rears calves that originate on dairy farms, the rearer of the calf effectively assumes the responsibility for emissions from the dairy cow.
- Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) also commented that an ETS must assess individual farm business's emission performance, recognise the mitigation effect of all scientifically proven mitigation technologies, and properly shield agriculture from non-carbon costed overseas competitors. The current ETS does not meet any of these criteria.

## **Other comments about agriculture in the ETS**

Taumarunui Sustainable Land Management Group (031) submitted that current rules for agriculture mean there is no incentive to reduce emissions and therefore more efficient farmers will be penalised.

Greenpeace (085) considered that, in the case of agriculture, pollution subsidies simply create a rise in land prices.

Lake Taupo and Lake Rotoaira Forest Trusts (142) argued that emissions from food and fibre represent the least discretionary emissions on a global per capita basis.

Pure Advantage (162) suggested that there should be a significant increase in Government and industry funding for research into reducing emissions from livestock, fertiliser and land use change.

Horticulture NZ (148) noted that some of the grants available from the Energy Efficiency and Conservation Authority are not available to many greenhouse growers.

## 7 Waste

The ETS coverage of emissions from the waste sector was addressed by 37 submissions. Of the submitters who commented on the waste sector, 19 were in support of retaining the current arrangements, one advocated bringing forward full obligations a year, one thought the waste sector should be exempt from the ETS entirely, four thought the entry should be postponed until there was clarity on New Zealand's obligations post-Kyoto and action from trading partners, and four thought only small landfills should be exempted from the ETS. Additionally, five submitters sought the withdrawal of the ETS including any coverage of the waste sector.

### **Arguments for and against retaining current ETS entry date (Questions 14 and 15)**

The majority of submitters on ETS and the waste sector supported the current timetable and coverage. There were 12 submitters who considered it was important that the waste sector remained in the ETS as currently timed in order to incentivise emission reductions [Escea (006), Bill Sayer (014), Southern Forestry (029), Greenpeace (085), Richard Leckinger (096), Euan Mason (108), Porirua City Council (129), OraTaiao: NZ Climate & Health (146), BusinessNZ (149), The Sustainability Council (151), Mark Milke (152) and Qantas (158)]. For these submitters, abatement opportunities either existed or would be found.

Forest & Bird (110) argued that the entry of the waste sector into the ETS should be brought forward to as soon as possible.

Several submitters considered that ETS principles required the waste sector to enter the ETS as currently timed. Principles raised included market and policy certainty for participants [Mighty River Power (130)], and that an all sectors all gases ETS would be the most effective at reducing emissions [Richard Leckinger (096), Vector (097)].

NZ Forest Owners Association (077) stated that there was insufficient evidence to delay the entry of other sectors, such as waste.

Six submitters considered it was important that the waste sector enter the ETS as currently timed in order for equity of treatment with other ETS sectors [Rockies Mining (024), Wellington City Council (058), Richard Leckinger (096), Mighty River Power (130), OraTaiao: NZ Climate & Health (146), and BusinessNZ (149)].

There were three general arguments against the current timetable. Four submitters held that commonly accepted climate projections were incorrect [David Slack (008), Simon Breeze (021), David Lloyd (026), and [withheld] (081)]. Three submitters argued that no new costs should be taken up, including through the entry of the waste sector, until trading partners take up comparable costs [Steve Wrathall (018), Seafood Industry Council (065), Employers and Manufacturers Association (070)]. Similar to that position, two submitters considered no new sectors should enter the ETS until

there was a new international treaty that required binding emission reductions [[withheld] (121), ACT (141)].

The Greenhouse Policy Coalition (114) opposed what it considered a doubling-up of price incentives on the waste sector through application of the ETS on top of the current waste levy. It advocated the use of a single measure.

Three submitters considered that the waste sector should not be part of the ETS because it was a small source of emissions in the National Inventory, and that emissions from landfills had declined since 1990 [Hastings District Council (062), EnviroWaste Services (067), Central Hawke's Bay District Council (123)].

Several submitters also expected significant perverse environmental effects from ETS coverage of landfills, and argued the sector should be mandatory participants. The risk for illegal dumping of waste was mentioned by five submitters. [South Waikato District Council (044), Local Government New Zealand (099), Porirua City Council (129), Hastings District Council (062), Central Hawke's Bay District Council (123)]

Local Government New Zealand (099) also considered that compliance costs from the ETS would shift some local council funding away from waste minimisation programs.

EnviroWaste Services (067) argued that the ETS was not the best measure to reduce emissions from landfills; instead it argued that immediate expansion of the current National Environmental Standard controls on landfill gases to all landfills, and sufficient enforcement, would be a more effective and efficient measure.

## **Arguments on the coverage of the waste sector in the ETS**

Three submitters considered there should be temporary or permanent ETS exemptions granted to small landfills [Hastings District Council (062), Local Government New Zealand (099), Central Hawke's Bay District Council (123)]. These submitters generally held that the implementation and monitoring costs of mitigation activities, such as landfill gas systems and measuring changes to waste composition, would outweigh any benefit to them from reduced emissions.

## **Other comments about waste in the ETS**

Two submitters raised technical issues. Mark Milke (152) made a number of suggestions including different methodologies for estimating emissions from landfills, rewarding the sequestration of carbon from disposing of organic materials in landfills, and increasing research efforts on emissions from landfills. Wellington City Council (058) sought methodological changes so that direct measurement of landfill emissions was permitted, and so that a participant could use different assumptions about the rates of waste decomposition.

Mark Milke (152) also noted that wastewater conveyance, wastewater treatment, 'cleanfill' landfills and composting activities are not included in the ETS. There is a danger that including landfills and

not the other waste management systems will lead to the diversion of organics from landfills to these other systems. These alternative management systems should also be added to the ETS over time. In addition, he added that the ETS should be amended to charge for methane emitted from closed landfills and charge for the methane emitted in the future from waste disposed of in the past.

## 8 Synthetic greenhouse gases

The ETS coverage of synthetic greenhouse gases (SGG) was addressed by 50 submissions. Of the submitters who commented on the entry date, 18 were in support of retaining the current arrangement, two advocated bringing forward full obligations a year, 10 thought SGG sectors should be exempt from the ETS entirely, four thought the entry should be postponed until there was clarity on New Zealand's obligations post Kyoto and action from trading partners, two submitted argued for a postponement to 2018, and five thought sulphur hexafluoride should be exempted from the ETS but did not address the other SGGs. Additionally, five submitters sought the withdrawal of the entire ETS including any coverage of SGGs.

### **Arguments for and against retaining current ETS entry date (Questions 14, 15 and 17)**

Twelve submitters considered it was important that SGGs remained in the ETS in order to incentivise emission reductions. For these submitters, abatement opportunities either existed or would be found. [Escea (006), Bill Sayer (014), Fisher & Paykel (019), Wellington City Council (058), Greenpeace (085), Richard Leckinger (096), Nelson Forests (098), Electricity Networks Association (073), Euan Mason (108), Professor Don Cleland (117), OraTaiao: NZ Climate & Health (146), Qantas (158)]

This position conflicts with the opinions of nine submitters, who argued that because abatement opportunities did not exist or were too expensive or would lead to undesirable effects, then the sector should be exempt from the ETS and other policies explored. [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant Recovery NZ (045), Temperzone (054), Electricity Networks Association (073), [withheld], Transpower (118), Vector (097), Powerco (134)]

Six submitters considered that the principle of equitable treatment with other sectors meant that SGGs should enter the ETS on the current timetable [Rockies Mining (024), OraTaiao: NZ Climate & Health (146) and others]. Both Wellington City Council (058) and Richard Leckinger (096) argued that an all sectors all gases ETS is the most effective framework for reducing emissions. Similarly, the NZ Forest Owners Association (077) stated that there was insufficient evidence to change the ETS timetable for SGG.

Professor Don Cleland (117) supported the current timetable and ETS coverage of SGG, and argued that in most cases any subsequent costs would be passed onto consumers, and that any net costs to exporting firms would be outweighed by reputational benefits from ETS coverage.

Mighty River Power (130) also supported the current policy settings, as they argued consistent policy is important for investment certainty.

A number of submitters provided general arguments as to why the ETS coverage of SGGs should be delayed or removed entirely. Four submitters were dissatisfied with climate science and thought the

ETS was unnecessary [David Lloyd (026), [withheld] (081) and others]. Three thought no new sectors should enter the ETS until trading partners take up comparable costs [Seafood Industry Council (065) and others]. In a similar vein, two submitters thought any new sectors should not enter the ETS until a subsequent international treaty required emission reductions in New Zealand [[withheld] (121) and ACT (141)].

Many submissions cross-referred and supported points made by others. For the stationary refrigeration and air conditioning sector, submissions were made that argued ETS coverage is not the most effective measure at reducing emissions [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant Recovery NZ (045), Temperzone (054), [withheld], BusinessNZ (149)] as it did not consider:

- the effect on energy efficiency, resulting in uneconomic and poorer environmental outcomes
- the potential for theft of SGG because its value would increase under ETS coverage, which in turn creates new costs for businesses
- the effect on business costs from increased working capital requirements

The same submitters considered ETS coverage is out of step with the approach taken to managing SGG emissions in other countries such as Australia and in Europe.

The same submitters, supported by BusinessNZ (149) and Southern Forestry (029), argued that the small amount of emissions from the sector does not justify the cost imposition of the ETS. Similarly, three submitters argued that the costs of compliance were too high (Motor Industry Association (037), Imported Motor Vehicle Industry Association (100), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)) and different measures should be used.

Three submitters argued against ETS coverage on the basis that existing voluntary approaches were working to reduce emissions [BOC (032), Seafood Industry Council (065), Employers & Manufacturers Association (070)].

Refrigerant Recovery NZ (045) argued against ETS coverage because it would reduce its revenue from collecting and exporting waste SGG, when an incentive would be created for others to engage in the activity. The submitter was also concerned over possible end-of-life SGG ownership disagreements.

On technical matters, nine submitters raised a concern that the current methodological approach of assuming emissions as soon as the SGG was imported was inequitable, given the Government does not use the same methodology to estimate national emissions and therefore its own liability under international treaties [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant Recovery NZ (045), Temperzone (054), Electricity Networks Association (073), [withheld], Vector (097), Transpower (118), Powerco (134)]. Some of those submitters suggested methodological changes, while others used the issue as the basis for full ETS exemption.

Powerco (134) argued that there should be a threshold for users of sulphur hexafluoride so that small users would not incur ETS costs for small emissions.

## Alternative measures

The *Issues Statement* provided generalised outlines of policies that could be used to replace, or strengthen ETS coverage, either across all SGGs or for subsets of SGG importers and users. Some of those policies are in already place, such as the memorandum of understanding between the Crown and SF<sub>6</sub> users; others control to the import and use of alternative refrigerants. Exploring and weighing up alternative and complementary policies helped test if ETS coverage is the most equitable and efficient method to reduce SGG emissions and meet international obligations.

Submitters from the motor vehicle sector supported the use of a levy imposed at the customs point or on first registration, instead of ETS inclusion of the SGG contained in the imported vehicles. They argued that while they did not support any price imposition from climate change policies, they could support a levy instead of the ETS because it would guarantee coverage, and reduce compliance costs due to its 'simplicity'.

Many submitters from the stationary refrigeration and air conditioning sectors argued that a regulatory approach similar to that used to control ozone-depleting substances in New Zealand, and similar to the F-Gas regulations in Europe, would result in better environmental and economic outcomes than ETS coverage. Measures they supported included:

- banning wilful leakage of SGG from certain applications [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Motor Industry Association (037), Refrigerant Recovery NZ (045), Motor Trade Association (052), Temperzone (054), [withheld] , Imported Motor Vehicle Industry Association (100), Professor Don Cleland (117), BusinessNZ (149)]
- mandatory leak detection equipment and processes [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant Recovery NZ (045), Temperzone (054), [withheld] , BusinessNZ (149)]
- a mandatory levy on all imported SGG, at a low level, to fund recovery and education initiatives that would be managed by the sector [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Motor Industry Association (037), Refrigerant Recovery NZ (045), Motor Trade Association (052), Temperzone (054), [withheld], Imported Motor Vehicle Industry Association (100), BusinessNZ (149)]
- a legally enforceable code of practice for SGG handlers [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant Recovery NZ (045), Motor Trade Association (052), Temperzone (054), [withheld] , BusinessNZ (149)) possibly along with their mandatory licensing [Motor Trade Association (052), Seafood Industry Council (065), [withheld], Professor Don Cleland (117), Transpower (118), BusinessNZ (149)]
- mandatory licensing of all importers and exporters of SGG to enable levy collection and rebates [BOC (032), Refrigeration and Air Conditioning Industry Group (035), Refrigerant

Recovery NZ (045), Temperzone (054), [withheld], Professor Don Cleland (117)), but not supported by submitters from the motor vehicle industry [Motor Industry Association (037), Motor Trade Association (052), Imported Motor Vehicle Industry Association (100)]

Some submitters who import or use sulphur hexafluoride considered the existing voluntary memorandum of understanding could be continued, either as a voluntary or as a mandatory measure [BOC (032), Vector (097), Transpower (118)].

## **Allocation issues for SGG**

Temperzone (054) said that if SGG enter the ETS then manufacturers of SGG equipment should be acknowledged as a distinct group from other SGG participants and receive special treatment, such as allocation or an exemption from the ETS. It noted that the SGG sector had been excluded from allocation, without consultation, on the incorrect assumption that importers of SGGs will be able to pass their costs on to their customers.

## 9 Forestry

### ETS incentives for forestry investment (Question 7)

#### The ETS incentives are too strong

Some submitters argued that the ETS perversely incentivises the plantation of arable land. They said that this has detrimental impacts on social and economic factors and on global food availability, and is depriving New Zealand of export earnings and jobs [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Bryan Leyland (001), Talleys (007), Raymond Scampton (025), Climate Realists (050)]. Talleys (007) elaborated that forestry exports unprocessed logs, whereas agriculture processes added-value products with its associated benefits of domestic production.

Other comments included:

- It results in market distortions [David Slack (008), ACT (141)]
- Land use should be determined by market demand for the products produced, and the ETS reduces this flexibility [Steve Wrathall (018)]
- Pastural Farming Climate Research (131) argued that forestry only receives rewards for sequestration from the atmosphere but is not penalised for carbon released from soils. He claims that this amounts to an over allocation of \$4262 per hectare (based on a \$25 carbon price)
- Other concerns expressed were that the revenues available to landowners from 'carbon farming' are over-stated [Pastural Farming Climate Research (131)], and downplay the fact that those revenues are short-term and must be repaid if trees are ever felled [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]. Once all suitable land is planted in forests, New Zealand will need new abatement opportunities [Straterra (084)].

#### The ETS is providing the right incentives

Other submitters' thought the incentive for forestry investments was right or about right. Some submitters partially agreed and outlined some provisos and areas where the treatment of forestry in the ETS could be improved. Other comments included:

- Several submitters noted the importance of including other sectors, such as agriculture, in the ETS [Southern Forestry (029), Northland Regional Council (069), Mighty River Power (130), BusinessNZ (149), NZ Forest Owners Association (077)]
- Some submitters provided examples of increased forest plantings, such as farmers who are planting trees in their marginal land and the conversion of farms to forestry in the central North Island [Escea (006), Taumarunui Sustainable Land Management Group (031), Simon Breeze (021)]

- Several submitters said foresters expect future carbon price rises which should provide on-going incentive for planting [Carbon Farm (102), Greenhouse Policy Coalition (114), Coal Association (132), BusinessNZ (149)]
- Some submitters felt the ETS provides the right incentives but noted some words of caution:
  - Hamilton City Council (028) said too much reliance on forestry could delay the development of emission reduction technologies
  - Greenhouse Policy Coalition (114) said there is a risk that international forestry rules may change after 2012, leaving the Government without new units to devolve to foresters after 2012 and that Government should investigate the least expensive way of promoting forest planting if this occurs
  - Bill Sayer (014) noted that wind and fire losses are likely to increase as a consequence of global warming, and special assistance may be necessary later.

Submitters expressed a range of views about the level of investment that was occurring. Some submitters gave examples of investments they or others were making in forest:

- Forest Management (015) are overseeing the establishment of over 1000 hectares of new forest in 2011, and potentially at least this in 2012, and they have negotiated agreements to supply and purchase units on a long term basis. They also see areas of native regeneration to gain credits, and significant reinvestment and new forest investment by foresters and hill country farmers
- Craigmore Forestry (144) has 3,500 hectares of new land planting scheduled in winter 2011 and plans to plant a further 4-5,000 hectares in 2012 and more beyond this point. They noted that the ETS is a major contributor to their new planting investment decisions, in combination with potential timber revenues
- BusinessNZ (149) was aware of new forestry investments in land being made as a direct result of the ETS. It also was aware of much larger land purchases on the East Cape by new overseas players who are intending to join the ETS
- Pure Advantage (162) commented on a marked pick-up in new forestry plantings
- Carbon Farm (102) noted the incentive to farmers in steep hill country to retire areas to regenerate in indigenous forest.

### **The ETS is providing too little incentive**

Some submitters argued that the ETS was not having the desired effect on new planting, and others indicated that they thought the incentive for forestry investments was insufficient:

- There is little sign that the ETS is leading to new forest investment [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142), Nelson Forests (098)]. Wairakei Pastoral (056) noted there has been very little new planting except where funded by the Afforestation Grant Scheme (AGS) and East Coast Forestry Project (ECFP)

- Several expressed uncertainty about the longevity of the ETS which does not provide confidence to invest in new forests, and that there is no confidence in receiving carbon credits for more than a couple of years [OMFinancial (047), Wairakei Pastoral (056), [withheld] (081), Origin Energy (122), Carbon Market Solutions (145), Blakely Pacific (154)]
- Carbon credits must be paid back when the trees are harvested in the 2020s [Sustainability Council (151), Environment and Conservation Organisations of NZ (161)]
- Potential investors were concerned that if they cash-up on early-sequestered carbon they will have to face the liability of major future increases in the price of carbon [NZ Farm Forestry Association (039)]
- Land prices are too high, even on marginal hill country [Marlborough Forest Industry Association (030)]
- The delay in bringing agriculture into the scheme so that land-use is still tilted disproportionately towards dairy [OraTaiao: NZ Climate & Health (146)]
- Impacts of market interference and transition phase measures and that foresters expect more extensions and exclusions [Marlborough Forest Industry Association (030), Richard Leckinger (096), Origin Energy (122)]
- The ETS has been too complex and too risky to stimulate a planting boom [Piers Maclaren & Associates (034)]
- The pre-1990 land conversion liability [Lake Taupo and Lake Rotoaira Forest Trusts (142), Carbon Market Solutions (145), OraTaiao: NZ Climate & Health (146)]
- The costs of pollution do not equal the costs of sequestration because of the gradual introduction of the ETS and some sectors are treated differently [Euan Mason (108)]
- There are insufficient incentives to plant and retain, or allow to regenerate, native species. This should be remedied [Environment and Conservation Organisations of NZ (161)]
- The rural sector is very likely to be over-represented amongst those that believe anthropogenic global warming is a 'con' and this is limiting afforestation on their land [Euan Mason (108)]
- The fact that the EU ETS does not accept forestry credits may reduce the incentive to invest in forestry [Qantas 158].

## Other comments

Submitters raised the following other issues with the current ETS forestry incentives:

- Two submitters argued that a viable domestic wood processing sector remains an important pre-requisite for investment in afforestation. There is little evidence as yet of carbon forestry replacing solid wood processing as the primary driver of afforestation. The ETS should incentivise growth in New Zealand's forestry industry more broadly, particularly in relation

to wood processing and using wood residues for renewable energy. [Carter Holt Harvey Pulp & Paper (040), Carter Holt Harvey (133)]

- Oregon Group (080) supported current incentives but added that changes to the treatment of forestry in the ETS would allow them to invest in more afforestation, such as risk sharing arrangements with the Crown (force majeure)
- Motu Economic and Public Policy Research (139) suggested that although the international carbon price is almost certainly our best estimate of the appropriate level of reward, we should look at methods of providing greater incentives up front and scaling back more distant incentives
- Several submitters noted that forestry is a long-term investment which needs certainty that the ETS has a longer life span to encourage investment [Forest Management (015), NZ Forest Owners Association (077), Oregon Group (080), Origin Energy (122), Bank of New Zealand (124), Carbon Market Solutions (145)]. One noted that past policy uncertainty impacted on new planting/investment and deforestation [NZ Forest Owners Association (077)]
- Nelson Forests (098) said there are risks that if the Government excludes agriculture from the ETS and/or allows very cheap CERs into the ETS after 2012, causing the carbon market to be oversupplied, carbon prices slump and afforestation stops
- IFS Growth and Craigpine Timber (106) the ETS unfairly disadvantages owners of forests established before the 2008 start date of ETS due to the requirement to surrender units for residual decay following harvest
- Two submitters noted the decision to plant trees must be supported by positive economics, stable legislation and consistent ETS policy, specially given the long-term nature of forestry investment [Forest Management (075), Kyoto Forestry Association (078)]
- WWF NZ (055) noted that the influence of the ETS is hard to quantify.

## **Options suggested to increase forestry incentives**

The NZ Farm Forestry Association (039) noted that it is highly desirable that as many hectares of new forest are planted as possible. This will help reduce New Zealand's burst of emissions in the 2020s, maintain the national yield of timber with all its associated socio-economic benefits, and reduce soil erosion and flood damage, improve water quality, increase biodiversity, improve the landscape and provide recreational opportunities. It also thought that about one million hectares of erosion prone/low productivity pastoral land is suitable for afforestation. New planting needs to be immediately stepped up to at least 20,000 hectares per annum.

Piers Maclaren & Associates (034) thought New Zealand has up to 5 million hectares of marginal land. If this was planted in trees at 50,000 hectares per annum (as was achieved between 1992 and 1998) this would constitute more than a century of positive carbon sequestration by forestry.

Two submitters added that an increase in the pool of domestic credits from forestry would assist in raising liquidity in the market for emissions units, which would be beneficial to those with surrender obligations [Contact Energy (089), Origin Energy (122)].

Other options suggested to increase the incentives for forestry investments included:

- Provide stability. Stable, long term policies and regulation are needed [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)] as is a belief that the price of carbon has stabilised [NZ Farm Forestry Association (039)]
- Equitable treatment with other land uses [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. Greenpeace (085) submitted that the ETS needs to be supported by changes to other land-use policy settings that presently favour competing land uses, such as agricultural production having free access to water, subsidies for irrigation, inadequate environmental regulations and support in export promotion.
- Foster a strong and competitive domestic wood processing sector, which has historically driven afforestation [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Increase the use of wood and wood products in New Zealand. Recognise the advantages of wood compared with other building products. Increase innovation and product development based on wood [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Facilitate forestry exports [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Explore mechanisms for local authorities and community groups to earn additional bonus 'eco' credits for indigenous forest entered into the ETS, over and above the usual credits earned for post-1989 forestry, to increase participation rates and better align the ETS with national environmental objectives [Hamilton City Council (028)]
- Cover the risk of having to buy back more expensive units upon harvesting. This may be obtained by insurance, risk pooling, delay of harvest, physical swap contracts, and price hedging and other mitigation options, but they are complicated and will certainly reduce the financial incentive to plant. [NZ Farm Forestry Association (039)]
- Change the tax rule known as the 'cost of timber' [NZ Farm Forestry Association (039)]
- Increase Government finance for forestry schemes like the AGS, the ECFP and the Sustainable Land Management Hill Country Erosion Programme [NZ Farm Forestry Association (039)]. The Climate Change Iwi Leadership Group (159) noted the critical role of forestry in New Zealand international obligations and added that policy design must include ongoing afforestation incentives like the ECFP.

- Euan Mason (108) drew attention to a study underway to look at ‘reserve pricing’ of afforestation on farms in New Zealand, including how the rural sector might respond to incentives provided by the ETS and the AGS.
- Provide recompense for the many benefits forests provide society, such as clean water, flood protection, erosion protection and biodiversity, not just carbon storage [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- The key is to ensure afforestation continues whether wood values are high or not [Carbon Market Solutions (145)].

## **Other suggested changes for forestry in the ETS**

Other suggested changes to the treatment of forestry in the ETS are outlined below.

### ***Change the definition of post-1989 forest land to include smaller plantings***

A number of submitters said woodlots and forests under 30m in width (such as shelter belts and riparian planting) should be included in the ETS and earn credits. The associated soil and water protection benefits were also noted. [Taranaki Regional Council (016), Wairakei Pastoral (056), NZPork (068), Fonterra (120), Max Hill (155)]. Fonterra (120) cited the example of 4,500 kilometres of river bank riparian plantings in Taranaki which are expected to sequester 4,000 units of carbon by 2013. Wairakei Pastoral (056) suggested allowing such planting to have a title-specific definition that allows an area of trees without being specific as to location.

### ***Allow pre-1990 forest land offset planting***

A number of submitters sought the ability to plant a new area of forest elsewhere instead of paying deforestation emissions liabilities, with some suggesting that this be a New Zealand-specific solution [South Waikato District Council (044), Wairakei Pastoral (056), Forest Management (075), NZ Forest Owners Association (077), Kyoto Forestry Association (078), Federation of Māori Authorities (109), Fonterra (120), Bank of New Zealand (124), Craigmore Forestry (144), BusinessNZ (149), Blakely Pacific (154), Climate Change Iwi Leadership Group (159)]. If not in the first Kyoto Protocol commitment period, then offsetting could be implemented after 2012 [South Waikato District Council (044)]. Reasons given for offset planting included:

- flexible land-use is important to avoid emissions leakage, economic costs in excess of other countries’ and reducing global food security
- The ability to offset plant would address the current issues of reduced pre-1990 forest land value, loss of economic and long-term community benefits from halted conversion of forest to pasture, and the flow-on impacts on council rates.

Suggested implementation included:

- Plant an equivalent area of forest in another location, or alternatively, to treat all plantation forests as post-1989 forest [South Waikato District Council (044), Fonterra (120)]

- Allow offset planting within the same or contiguous properties [Western Bay of Plenty District Council (088)]
- Fund the deforestation liabilities by withdrawing the second tranche of the Forestry Allocation Plan (FAP) units and using those, along with the FAP units not applied for in the first tranche [Wairakei Pastoral (056)]
- Apply for a permit to offset plant and be required to show that it contributes to net national benefit, and funded as above [Wairakei Pastoral (056)]
- Issue carbon loans to landowners that deforest pre-1990 areas, which are then repaid from the new planting [Craigmores Forestry (144)]
- NZ Forest Owners Association (077) suggested as an alternative, to remove the 9 year rule

Lake Taupo and Lake Rotoaira Forest Trusts (142) noted that offset planting is not realistic for many Māori forest owners as they have no opportunity, financial resources or desire to invest in planting land elsewhere in order to open up opportunities on their forested lands.

### ***Force majeure***

Several sought protection for foresters from force majeure losses that can be considered beyond reasonable risk management provisions, such as a pest invasion [Forest Management (075), NZ Forest Owners Association (077), Kyoto Forestry Association (078), Oregon Group (080), Lake Taupo and Lake Rotoaira Forest Trusts (142), Blakely Pacific (154)]. The added certainty it would give the industry would be invaluable. Some of the submitters recommended that, like Australia, a national scheme be provided utilising a small percentage of the credits to provide insurance cover [NZ Forest Owners Association (077), Kyoto Forestry Association (078), Lake Taupo and Lake Rotoaira Forest Trusts (142) and Blakely Pacific (154)].

### ***'Averaging'***

Some submitters called for the ability to receive credits up to the long-term average carbon stock level, rather than the full carbon stock level of the forest [Piers Maclaren & Associates (034), NZ Forest Owners Association (077), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. Reasons included to remove the long-term risks associated with an unknown price of carbon at harvest.

### ***Harvested wood products***

Some submitters sought accounting for emissions from harvested wood products (the carbon in wood removed from forests), which removes the assumption that all carbon is instantly emitted the moment the wood is harvested [Escea (006), Forest Management (075), Kyoto Forestry Association (078), Craigmores Forestry (144), Marlborough Forest Industry Association (030)].

### ***Increase the 2 hectares pre-1990 deforestation exemption threshold to 50 hectares***

Several submitters sought an increase in the 2 hectare pre-1990 deforestation exemption threshold for equity with owners of less than 50 hectares who can apply for a 50 hectare exemption [Carter Holt Harvey Pulp & Paper (040), NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. Others reasons included that, at 2 hectares, the threshold imposes an unreasonable

compliance cost on larger forestry estates, incurred from deforestation liabilities and from efforts to avoid it on large, geographically diverse holdings. There are numerous regulatory and natural processes which can cause deforestation of over 2 hectares.

### ***Post-1989 field measurement approach***

Several submitters sought either reversal of the decision not to allow owners of less than 100 hectares to use the field measurement approach (as this is unfair and reduces the incentive to afforest), or enable forest owners to choose whether to use the field measurement approach or the look up tables [NZ Farm Forestry Association (039), Forest Management (075), NZ Forest Owners Association (077), Kyoto Forestry Association (078), Oregon Group (080)].

### ***Specific exemptions from pre-1990 deforestation liabilities sought***

The following specific exemptions were sought by certain submitters:

- A requirement to increase forest setback areas which should rest with the authority requiring it [NZ Forest Owners Association (077), Lake Taupo and Lake Rotoaira Forest Trusts (142)]
- Landowners who did not get the return from the timber [Grahm Kehely (020)]
- Harry Mowbray (160) explained how he had been caught unaware by the less-than-50 hectare exemption applying to total landholdings (rather than individual titles) and by one of the partners owning more than 50 hectares and thus preventing any of the others from applying for a less-than-50 hectare exemption. This has had perverse effects on their land use decisions and future dairy conversion plans. They are also concerned about their understanding that the Central North Island Māori forestry treaty settlement included the Government agreeing to pay the deforestation liabilities.
- Tree clearance around power lines [Electricity Networks Association (073)]
- Replacing pre-1990 scrub with fast growth forest species [Craigmore Forestry (144)]
- Deforesting areas better suited to public recreation [Western Bay of Plenty District Council (088)]
- Energy crops such as miscanthus, grown in place of pre-1990 forest [Proprietors of Taharoa C Block (051), Bioenergy Association (138)].

## **Other comments about forestry in the ETS**

The tree weed exemption should be maintained for two more Kyoto Protocol commitment periods [Local Government New Zealand (099)].

New Zealand should mirror the approach other nations have taken in relation to forestry, and there is no indication that they intend to mirror the Kyoto Protocol rules like NZ has [Fonterra (120)].

Consideration needs to be given to how soil carbon can be included into the ETS [Horticulture NZ (148), Environment and Conservation Organisations of NZ (161)].

Consideration needs to be given to horticulture being able to offset emissions by accounting for carbon in fruit trees and vines, soils and shelterbelts [PlusGroup Horticulture (147)].

Payment of credits to foresters must be delayed or repealed because we cannot afford it and a direct trading link with the EU is unlikely [Basil Walker (071)].

Forestry to be harvested should not be included in emissions accounting [350 Aotearoa (064)].

Pastoral Farming Climate Research (131) considered that forestry is a carbon store but not a sink, nor a solution to the problem of climate change.

Marlborough Forestry Association (030) believed there is a disconnect between the ETS (specifically the encouragement of forestry expansion of permanent forest sinks) and Resource Management Act (RMA) constraints that may act to discourage forestry.

The Proprietors of Taharoa C Block (051) considered that the definition of tree or forest in the ETS should be changed but remain consistent with the Kyoto Protocol.

## **The impact forestry's inclusion in the ETS has had on biodiversity**

Five submitters commented on the following positive effects on biodiversity resulting from the ETS encouraging afforestation:

- cleaner and healthier environments [Forest Management (015)]
- a reduction in chemical use from the transition from agriculture [NZ Forest Owners Association (077)]
- soil stability increased and erosion reduced in hill country land that follows destocking and planting [Forest Management (015), Southern Forestry (029), NZ Farm Forestry Association (039), Oregon Group (080)]
- water quality protection and reduced flooding [Forest Management (015), Southern Forestry (029), NZ Farm Forestry Association (039), Oregon Group (080)].
- improved biodiversity habitat and biodiversity measures [Southern Forestry (029), NZ Farm Forestry Association (039), Oregon Group (080), NZ Institute of Forestry (119)]
- improvements to the landscape [NZ Farm Forestry Association (039)].

Examples were provided:

- in North Canterbury over 100 hectares of regenerating native bush and one of the largest lowland natural wetlands in North Canterbury are now registered in the ETS and have been retired from grazing and are regenerating

- a large number of rural landowners are controlling weeds due to afforestation and income flow [Forest Management (015)]
- native forest regeneration is increasing as landowners are letting their land regenerate to native forest to gain carbon credits [Forest Management (015)]

NZ Forest Owners Association (077) submitted that the risks to biodiversity from ETS-driven forestry are small and overall the impact will be beneficial. New forest planting will typically occupy marginal farm land that has a lower level of biodiversity than the plantation forest that will succeed it. They noted that potentially, there may be a limited number of areas where planted forestry could replace native forest and not contravene either the Forests Act or the Resource Management Act. NZ Forest Owners Association and Farm Forestry Association members are bound by a 'Forest Accord' signed 20 years ago with the key environmental groups in New Zealand that prevents this, but it is possible that this could take place legally on rural land.

A couple of submitters were unsure of the extent of impacts on biodiversity, given that the rate of afforestation of pasture and other low-biodiversity lands is at historically low levels [NZ Institute of Forestry (119), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. The NZ Institute of Forestry (119) also pointed out that the afforestation incentive in the ETS is directed at fast growing species, whereas a different choice of species, but a slower growing one, would provide greater biodiversity benefits. It also felt that the ETS acts against more afforestation using indigenous species for timber production.

Three submitters had concerns about the negative effects of forestry and the ETS on biodiversity. Climate Realists (050) were concerned that pines are the dominant species planted for carbon farming, and that large areas of monoculture carry biodiversity risks. They noted that some species will adapt to the environment, e.g. tree ferns and kiwis, but that should a lethal disease arrive in our pine forests vast areas will be at risk. Two other submitters said that afforestation in some places for carbon benefit can also bring a very high environmental cost through the impact of wilding trees on local ecology and other economic activities, and can create a snowballing wilding-spread risk in some areas [Forest & Bird (110), Environment and Conservation Organisations of NZ (161)].

Climate Change Iwi Leadership Group (159) suggested, in recognition of indigenous forests for both their carbon and biodiversity roles, the creation of new biodiversity units that attribute a cash value to indigenous forests. These units would be traded within both the ETS and Internationally.

Forest & Bird (110) noted that New Zealand's biodiversity is ill-equipped to adapt to the likely impact of climate change. Mitigation policies have both risks and opportunities for biodiversity, particularly those involving land-use change. They promote policies that protect both carbon stores and biodiversity.

# 10 Allocation

## Allocation settings after 2012 (Question 16)

Some submitters commented directly on whether allocations should continue as planned under the current design settings after 2012. However, many more submitters addressed this issue in their responses to the sub-questions, which are summarised in the sections below.

### Continue allocation as planned

Several submitters did not want any change to the current allocation settings [Horticulture NZ (148), Carter Holt Harvey Pulp & Paper (040)].

### Discontinue allocation

Some submitters said that free allocation should end. Reasons included:

- It erodes trust in both business and the Government, by unfairly distributing the burden of the liability for GHG emissions, from those responsible for emissions to those who pay but cannot adjust the pollution causing the emissions [Environment and Conservation Organisations of NZ (161)]
- It weakens incentives to abate emissions [350 Aotearoa (064), Bill Sayer (014), Environment and Conservation Organisations of NZ (161), WWF NZ (055)]
- It distorts carbon markets [Bill Sayer (014)]
- Emitters should face full costs of their emissions and should stop emitting greenhouse gases altogether [Bill Sayer (014)]
- The costs of the ETS are so low relative to other factors affecting fuel prices and competitive risk [Southern Forestry (029)]
- It is counter to the OECD-agreed Polluter Pays Principle [Environment and Conservation Organisations of NZ (161)]

Some submitters objected to allocation because they did not believe in climate change or global warming.

### Redesign the approach to allocation

Some submitters suggested alternative approaches to free allocation. Alternatives included:

- There should be a cap on the amount of allocation [Parliamentary Commissioner for the Environment (143)]

- Emission units should be auctioned as this would distribute costs more flexibly, provide more incentives for innovation and lessen political arguments over allocation of economic rents [350 Aotearoa (064), Simon Johnson (063)]
- A carbon tax might be a more appropriate mechanism than allocation, particularly given Australia's recent decision to impose a carbon tax [Hamilton City Council (028)]
- Claw back a proportion of free allocation and then reissue them by auctioning. This will remove the windfall gains to those who get the free allocation and raise money for the Crown [Environment and Conservation Organisations of NZ (161)]
- Retire free allocation and issue every citizen with transferable carbon credits on, say, a carbon credit card. Businesses and other emitters can then purchase such credits from citizens on a secondary carbon market. [Environment and Conservation Organisations of NZ (161)]
- If the Government wishes to maintain employment then consideration should be given to directly assisting workers rather than firms, such as start-up support to clean technology firms where they are able to employ workers from polluting activities [Greenpeace (085)]
- The Minister should have more discretion over the threshold tests for industrial allocation [NZ Sugar Company (103)].

## Considerations on allocation settings

Some submitters made comments on the current allocation settings and suggested other considerations. These included:

- The state of the economy is relevant to the appropriate level of free allocation [[withheld] (121)]
- Free allocation is an important tool in ensuring the economic effects of the ETS are not unduly burdensome [Contact Energy (089)]
- Many agricultural producers, including many small, family-run farms, are particularly sensitive to sudden economic changes. As such there is a good case for allocating some free allocation to the sector for a transition period [Parliamentary Commissioner for the Environment (143)]
- Allocation should err on the point of being too generous rather than less generous as over-allocation does not affect economic efficiency, but under-allocation risks reduced investment and loss of production overseas [BusinessNZ (149)]
- The Australian Productivity Commission study on the relative carbon prices in different countries will be an important source of information. If this study suggests New Zealand has taken on a disproportionate burden relative to its per capita income level then the impacts of the ETS should be reduced [NZ Business Roundtable (083)]

- Free allocation to specific sectors should be based on evidence of need [Forest & Bird (110), WWF NZ (055)]
- New Zealand's competitive advantage should be treated as dynamic, with the potential to change over time, rather than as static and in need of preservation in its current form [WWF NZ (055)]
- Free allocation should be monitored to ensure it does not undermine the intention of the ETS, that is to reduce carbon emissions [Hamilton City Council (028)]
- There should be no free allocation to new areas of investment which produce high greenhouse gas emissions from coal, lignite, oil and methane (such as would appear to be supported by the Government's draft Energy Strategy) [Environment and Conservation Organisations of NZ (161)]
- Criteria should be provided for deciding which new activities are eligible to receive allocation, including a requirement that the new activity will reduce New Zealand's national net greenhouse gas emissions [Parliamentary Commissioner for the Environment (143)]
- A sector-by-sector assessment is important when considering allocation as it is necessary to compare the policies in place in those countries with which particular sectors compete [Methanex (105)]
- Some supply contracts do not allow for the pass-through of ETS costs [[withheld] (121)]
- The use of the methodology for the proposed Australian CPRS is inappropriate for the ETS:
  - As New Zealand has a different emissions profile than Australia, NZ should not be locked in with Australia [Parliamentary Commissioner for the Environment (143)]
  - Activities eligible for allocation should be defined and threshold levels set to retain the competitiveness of New Zealand businesses [Coal Association (132), ALSCO NZ (057)].

## Phase out of allocation

A number of submitters commented on the current phase-out rate for allocation with some arguing it was too slow and others it should be delayed. One, NZ Fertiliser Manufacturers' Research Association (091), said the allocation phase-out rate for agriculture was appropriate at this time.

### ***Summary of those submissions arguing for a faster phase out of allocation***

Some submitters objected to the slow phase-out of allocation because it would reduce the incentive for emission reductions over the longer term, and argued for a faster phase out. Comments included:

- The phase out rate of 1.3 per cent per annum from 2012 for eligible industrial activities and from 2016 for agriculture was overly generous and would mean that some sectors will effectively receive allocations forever [Hamilton City Council (028), Parliamentary Commissioner for the Environment (143)]

- The increasing exposure to the ETS is so gradual that agriculture will still be mostly shielded from the ETS by 2050, when emissions need to be closer to zero [OraTaiao: NZ Climate & Health (146)]
- WFF NZ (055) said (quoting the European Commission) ‘a less ambitious pathway could lock in carbon intensive investments, resulting in higher carbon prices later on and significantly higher overall costs over the entire period’
- The Parliamentary Commissioner for the Environment (143) said the slow phase-out rate is inconsistent with the Government’s target to reduce emissions by 50 per cent on 1990 levels by 2050 and recommended that the phase-out rates for allocation be increased
- Forest & Bird (110) said agriculture should be introduced with a transitional period that phases out allocation by 2020
- Environment and Conservation Organisations of NZ (161) said allocation should be cancelled after 2012

***Summary of those submissions arguing for delaying phase out of allocation***

Some submitters said allocation should be delayed. Suggestions on how long phase-out should be delayed included:

- to 2016 [Greenhouse Policy Coalition (114)]
- to 2018 [BusinessNZ (149)]
- until the next ETS review [Ballance Agri-Nutrients (048), NZ Business Roundtable (083), Coal Association (132)]
- until evidence of international progress and domestic action by our key trading partners [Straterra (084)]
- until there is a fixed international price of carbon and we trade in an equitable international market [NZ Coal & Carbon (111)]
- until competitors face a carbon cost [NZ Steel (135), Horticulture NZ (148), Holcim (112), Solid Energy (027)]
- until 80 per cent of global emissions are covered by a comparable cost of carbon [Rio Tinto (094)]
- the rate at which phase-out reduces could have significant impacts on the regional economy which relies heavily on the primary and secondary sectors [Northland Regional Council (069)].

The main reasons given for delay included New Zealand’s competitors are not facing a price of carbon [BusinessNZ (149), Greenhouse Policy Coalition (114), Ballance Agri-Nutrients (048)], and uncertainty over the future availability and price of emission units [Ballance Agri-Nutrients (048)].

Rockies Mining (024) noted that if carbon prices increase, allocation should be maintained.

## **Fiscal cost of allocation**

A number of submitters objected to the high cost allocation imposed on Government, society or taxpayers. Comments included:

- Allocation creates a major fiscal risk because it is not capped and is made on an intensity basis. [Sustainability Council (151), Parliamentary Commissioner for the Environment (143), Environment and Conservation Organisations of NZ (161)]
- Allocation imposes an opportunity cost relating to the revenue forgone [Parliamentary Commissioner for the Environment (143), Environment and Conservation Organisations of NZ (161) Ora Taiao: NZ Climate & Health (146)]
- Allocation is a subsidy with taxpayers subsidising big polluters [Parliamentary Commissioner for the Environment; Sustainability Council (151), Ora Taiao: NZ Climate & Health (146)]
- Allocation unfairly transfers the majority of the costs of New Zealand's Kyoto Protocol obligations onto future taxpayers [Sustainability Council (151), WWF NZ (055)].

## **Equity of allocation**

Some submitters felt that the free allocations raised equity issues, due to the distribution of the costs of allocation:

- The costs incurred by New Zealand should be shared fairly between emitters and taxpayers, but the current set-up of the ETS favours emitters at the expense of taxpayers [Carbon Farm (102)]
- Allocation imposed costs elsewhere in the economy, typically on consumers, who do not invest in renewable energy [Simon Johnson (063)]
- All sectors of the economy need to reduce their emissions and no sector should be given favourable treatment [Seafood Industry Council (065)]
- Any elements of the agricultural sector that are trade-exposed should be treated in the same way as other trade-exposed industries [NZ Business Roundtable (083)]
- Producers and consumers should both pay and this sharing of the cost of greenhouse gases is essential to the effectiveness and efficiency of the price instrument [Environment and Conservation Organisations of NZ (161)].

## **The effectiveness of allocation in reducing competitiveness risks or carbon leakage (Question 16a)**

Some submitters commented that the current settings for free allocation have been effective in reducing the competitiveness risks of the ETS. These comments included:

- Allocation is an effective and appropriate mechanism to reduce competitiveness risks [Fletcher Building (076), NZ Refining Company (043)]
- Allocation is an effective mechanism to reduce competitiveness risks if the level of allocation and any phase-out is appropriately set [Ballance Agri-Nutrients (048), Methanex (105)]
- Allocation has been important in helping to reduce competitiveness risks [Horticulture NZ (148), Carter Holt Harvey Pulp & Paper (040), Holcim (112)]

One submitter commented that the most effective way to reduce competitive risk is to cap the carbon price at zero until the future shape of global emissions policies becomes clear [Climate Realists (050)].

A number of trade-exposed, energy-intensive submitters said free allocation was necessary to off-set the potential loss of international competitiveness and of the risk carbon leakage. This was because businesses which export a large proportion of their output or compete against importers are trade-exposed and therefore prices for their products are determined internationally rather than domestically. This means they are unable to pass on the ETS costs as their overseas competitors do not face a similar cost on their products. It was also noted that a loss of competitiveness impacts on the long-term survival and the future expansion of those businesses. [Rio Tinto (094), Holcim (112), Carter Holt Harvey Pulp & Paper (040), ALSCO NZ (057), [withheld], Seafood Industry Council (065), [withheld] (121), Sanford (156), Horticulture NZ (148)]

Some submitters said free allocation was necessary because their international competitors receive financial incentives, such as large energy efficiency capital expenditure grants and for biofuels [Carter Holt Harvey Pulp & Paper (040), Wood Processors' Association (042), Sanford (156)].

The Environment and Conservation Organisations of NZ (161) did not think free allocation was an effective or efficient way of reducing competitiveness risks. It thought that as long as there is tradability of permits, such allocations are simply windfall gains to polluters.

Some submitters said current free allocation did not fully offset the costs associated with the ETS and therefore risks of competitiveness loss remain [Fletcher Building (076), NZ Steel (135), Ballance Agri-Nutrients (048)]. Other comments included:

- Competitors do not face a price on carbon, and trade-exposed industries and agriculture are not being properly shielded by free allocation [NZ Business Roundtable (083), ExportNZ 104]
- Some trade-exposed and energy-intensive businesses receive no allocations or inadequate allocations because of the way eligible activities are defined, the eligibility thresholds, the firm's scale of operation and/or the design of the proposed Australian scheme. Those sectors specifically identified included:
  - Greenhouse growers of fresh tomatoes, capsicums and cucumbers [Horticulture NZ (148)]
  - Wool scourers [Cavalier Wool Holdings (038)]

- Production of yarns [Qualityarns (033)]
- Dairy food processing sector [Coal Association (132), NZ Business Roundtable (083), Fonterra (120)]
- Meat processing sector [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]
- Coal mining [Coal Association (132)]
- Commercial fishing industry [Seafood Industry Council (065), Sanford (156)].
- Free allocation does not cover some areas of business operation (such as, wood chipping operations), even where they are an integral and on-site part of the manufacturing process [Carter Holt Harvey Pulp & Paper (040)]
- 100 per cent assistance would be in line with the assistance provided in other countries [ALSCO NZ (057), Cavalier Wool Holdings (038), Methanex (105)]
- While free allocation covers a significant proportion of production-related direct energy emissions costs, it does not cover price increases of local goods and services as a result of the ETS [Carter Holt Harvey Pulp & Paper (040), Wood Processors' Association (042)]
- Coal users receive insufficient or no allocation [Heaphy Mining (128), Rockies Mining (024), Coal Association (132), Cavalier Wool Holdings (038), Nova Trust (066)].

## Activity definition

Several submitters commented on how activities are defined under the ETS. Fonterra (120) considered that the definitions of activities (for the purpose of industrial allocation) should be broadened to ease the administrative burden of application for such allocation. Fletcher Building (076) disagreed with officials on some interpretations about emissions on the boundary of an activity definition for the purpose of industrial allocation.

The Coal Association (132) said this concept, which refers to the transformation of inputs into saleable product, and is based on an untested Australian proposal, was inappropriately interpreted to exclude coal mining as an eligible activity. The concept of an activity should be refined to enable a mining activity to include processes from extraction of raw materials at the mine face, though chemical or physical transformation to the creation of the final saleable products. This point was also made by a number of other submitters [Straterra (084), NZ Coal & Carbon (111), Heaphy Mining (128), NZ Business Roundtable (083), Gelita (017)].

Forest & Bird (110) rejected claims by the mining industry for extended allocation coverage. Mining activity generates its own emissions (e.g. fugitive emissions) and uses inputs that generate emissions or have emissions embedded and the industry must take responsibility for these emissions.

## **Allocation to compensate for loss of asset value**

### ***Pre-1990 forests***

Several submitters comments on the adequacy of allocation to compensate for the loss of asset values. Lake Taupo & Lake Rotoaira Forest Trusts (142) commented that the effect of the ETS has been to render land-use change from forestry established before 1990 significantly uneconomic, with high consequential impacts on the capital value to the land. The allocation provided in compensation was insignificant relative to the impost. Southern Forestry (029) said the inadequacy of the forestry allocation for pre-1990 forest owners had a greater impact on Māori, as the largest owners of pre-1990 forest land.

### ***Fishing***

The Seafood Industry Council (065) said that quota owners were offered an allocation of 750,000 emission units to offset the loss of value in quota prices, but that not all quota-owners applied for their entitlements. Environment and Conservation Organisations of NZ [161] disagreed with allocation to the fishing industry because they were not given to those who run the boats and emit greenhouse gases, but to the fisheries quota holders.

## **Impact of allocation on incentives to reduce emissions (Question 16b)**

### **Free allocation reduces incentives to reduce emissions**

A number of submitters said free allocation erodes incentives to reduce emissions [Wellington City Council (058), 350 Aotearoa (064), Bill Sayer (014), Environment and Conservation Organisations of NZ (161), WWF NZ (055), Parliamentary Commissioner for the Environment (143) Carbon Farm (102), ALSCO NZ (057), Forest & Bird (110)]. Some submitters believed that free allocation had reduced incentives for emission reductions because it had been too generous [Parliamentary Commissioner for the Environment (143), Carbon Farm (102)].

Some submitters said that allocations reduce incentives for emission reductions because they were intensity-based and uncapped [Wellington City Council (058), Carbon Farm (102), WWF NZ (055), Simon Johnson (063), Parliamentary Commissioner for the Environment (143), Environment and Conservation Organisations of NZ (161)].

Greenpeace (085) noted that providing free allocation to emissions-intensive industry where lower emission alternatives exist is counter-productive to the purpose for the scheme because it provides a competitive advantage for emissions-intensive firms.

### **Free allocation slows the transition to a low carbon economy**

Some submitters said free allocation reduced the incentives to transition to a low-carbon economy [Greenpeace (085), Parliamentary Commissioner for the Environment (143), OraTaiao: NZ Climate &

Health (146), WWF NZ (055), Forest & Bird (110), Environment and Conservation Organisations of NZ (161), Sustainability Council (151)].

The Sustainability Council (151) noted the ETS does not position the New Zealand economy, or the New Zealand public, to respond to broader shifts in the big picture of global policy. Southern Forestry (029) noted there could be huge advantages to the New Zealand brand by being carbon compliant. OraTaiao: NZ Climate & Health (146) said free allocation to the agriculture sector in particular risks locking the sector into outdated practices and technology.

## **Allocations maintain or increase incentives to reduce emissions**

Some submitters said that the allocations had not reduced incentives to reduce emissions. This is because free allocation is provided on an intensity-basis (i.e. based on production rather than energy usage) which means the same opportunity/marginal cost of abatement remains. [Horticulture NZ (148), Carter Holt Harvey Pulp & Paper (040), Ballance Agri-Nutrients (048), Rio Tinto (094), Fletcher Building (076), NZ Steel (135), Holcim (112), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Oregon Group (080)]. Other comments included:

- Free allocation results in a better outcome in terms of global emission as it ensures production remains in New Zealand rather than moving to more emissions-intensive countries [Methanex (105)]
- Businesses still face significant costs under the ETS even with an allocation [Horticulture NZ (148)].

Some submitters argued that it was not allocations but lack of abatement options and other barriers that prevented emission reductions, including the practicality of alternative fuels and the lack of new energy efficiency technologies [Horticulture NZ (148), Rockies Mining (024)].

Carter Holt Harvey Pulp & Paper [040] said free allocation supported the transition to a low-carbon economy by supporting a sustainable manufacturing sector (that is, wood manufacturing) and a producer of renewable energy.

Horticulture NZ (148) submitter said greenhouse vegetable growers would like to access future allocations to fund investments in low-carbon technologies and energy efficiency measures.

## **Impact of uncertainty on incentives for abatement**

General Electric (150) commented on the importance of providing certainty in relation to free allocation as this would provide greater confidence to invest in generation, transmission and distribution for new clean energy.

## Allocation thresholds (Question 16c)

### Allocation thresholds should be lowered

Some submitters argued they had been substantially and inequitably affected by the allocation thresholds [Coal Association (132), Qualityarns (033)].

A number of submitters proposed lower allocation thresholds and/or higher levels of assistance associated with these thresholds. Proposals and reasons for them included:

- A sliding scale of thresholds to avoid major break points, to assist small businesses [BusinessNZ (149)]
- Lower thresholds as many SMEs have extremely thin margins currently and even those with relatively small energy use are adversely affected [GL Bowron & Co (074)]
- Lower thresholds (whether on revenue or value-added basis) so that genuinely trade-exposed industries are not competitively disadvantaged [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]
- Levels of assistance should increase to 80 per cent and 95 per cent for each of the current thresholds [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]
- To ensure sectors that are of critical importance to New Zealand's future prosperity, such as food processors like Fonterra, receive increased allocation to reflect the competitiveness risks these sectors face [Greenhouse Policy Coalition (114), BusinessNZ (149)]
- Because they were based on an Australian scheme that was never implemented and therefore it is possible that they are not appropriate for New Zealand [Straterra (084), Methanex (105), NZ Coal & Carbon (111)]

### Current allocation thresholds are acceptable or it is too soon to say

Holcim (112) expressed satisfaction at the thresholds applying to their core business.

Oregon Group (080) said it was too soon to say whether the current thresholds are acceptable and recommended not to revisit the thresholds for at least 5 years.

### Use of revenue to determine emissions intensity

Some submitters commented that while they were impacted by the ETS because they did not qualify for free allocation because emissions intensity is based on revenue rather than 'value-added'. This was a particular issue for businesses that provide an emissions-intensive service for part of the production process. A number suggested either amending the revenue rule and/or including a 'value-added' assessment as well. One submitter noted that value-added allows for a more informative assessment of the cost impact on a firm's competitiveness. [Cavalier Wool Holdings (038), NZ Sugar Company (103), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]

## **Early actor disadvantage**

Two submitters said some activities fell outside the eligibility thresholds because of early action taken to reduce emissions, such as by increasing the use of biofuels. The submitters argued that, for this reason, there were parts of the industry that should receive allocation through more flexible eligibility rules, a lower threshold for eligibility and a greater allocation percentage. [Carter Holt Harvey Pulp & Paper (040), Wood Processors' Association (042)].

BusinessNZ (149) proposed having a choice over which years are used as the base years for determining eligibility. The Wood Processors' Association (042) proposed treating biofuels in the same way as fossil fuels for eligibility purposes which would enable an innovative, engineered wood product such as laminated veneer lumber to go from zero to 90 per cent allocation.

## **Environmentally sustainable production**

Two submitters said it was a significant flaw in the current allocation of NZUs, including where they occur on an emissions-intensive basis, that more environmentally-sustainable business operations, such as engineered wood product manufacturing and laminated veneer lumber, do not qualify for assistance when more polluting industries do [Carter Holt Harvey Pulp & Paper (040), Wood Processors' Association (042)].

Carter Holt Harvey (133) argued that consideration should be given to extending allocation to the solid wood processing sector on a basis that it 'assumes emissions from established biofuel use were from a logical fossil fuel'.

Fletcher Building (076) argued that output from eligible activities using either primary materials or recycled/recovered materials as inputs should get the same rate of assistance so that plants using recycled materials are not competitively disadvantaged.

## **Inclusion of liquid fossil fuels**

A number of submitters suggested liquid fossil fuels (LFF) should be included for determining eligibility and allocative baselines, although in different ways:

- Specifically heavy fuel oil used in the provision of industrial heat to make it consistent with the treatment of gas and coal used for this purpose [BusinessNZ (149), Rio Tinto (094), Carter Holt Harvey Pulp & Paper (040)]
- For coal mining, as LFF is used as a process input rather than for transport purposes [Straterra (084), NZ Coal & Carbon (111), Heaphy Mining (128), Gelita (017), Coal Association (132)].

Several submitters noted that LFF are a source of liable emissions under the ETS but are inexplicably and unjustifiably not included in the assessment of a businesses' emissions intensity or as a source of emissions for which allocation can be provided [Coal Association (132), ALSCO NZ (057)]. Rio Tinto (094) noted that if LFF were included then the New Zealand treatment of LFF would be consistent

with that proposed under the Australian CPRS and if it would mean that allocation would cover a greater proportion of the ETS costs incurred.

## **Inclusion of waste fuels**

Holcim (112) expressed disappointment at the ‘unusual and irregular’ treatment of waste fuels in the ETS, and strongly urged that the combustion of waste fuels be treated in exactly the same manner as combustion of coal or other ‘traditional’ fuels, specifically that such fuels should be included as eligible fuels for the purposes of allocation. As it was, the beneficial act of fuel-switching to waste fuels was effectively penalised in the ETS relative to coal or other eligible fuels.

## **Fugitive emissions of methane from coal mining**

Numerous submitters said fugitive emissions of methane from coal mining are a significant liability for mining companies and should be made eligible for allocation (or these emissions should be zero-rated) [Straterra (084), NZ Coal & Carbon (111), Coal Association (132) ALSCO NZ (057), Solid Energy (027), NZ Business Roundtable (083), Greenhouse Policy Coalition (114)]. Comments included:

- Fugitive emissions of methane are a significant cost under the ETS for coal producers, particularly from underground mines, and cannot be passed on (Coal Association (132), Solid Energy (027))
- The management of fugitive emissions of methane is fundamentally a safety issue, which should be given priority and treated separately to emission reduction. The only currently available way to reduce the ETS charge for fugitive emissions of methane is to reduce efforts to vent it, which is contrary to good safety practice and if taken to an extreme would impact on miner safety [Coal Association (132), ALSCO NZ (057), Solid Energy (027)]
- The current treatment of fugitive methane emissions under the ETS will create a strong encouragement in favour of importing coal, and will discourage exports, increasing global emissions and impacting on the New Zealand economy [Coal Association (132), Solid Energy (027)]
- It is inconsistent and illogical to treat fugitive emissions of methane as a liable source of greenhouse gas emissions but not allow such emissions to be included in the calculation of a businesses’ emissions intensity, or as a source of emissions for which allocation can be provided [Coal Association (132), ALSCO NZ (057)]
- It doesn’t make sense that a trade-exposed company is entitled to allocation for the coal it uses but does not receive allocation in respect of the fugitive emissions of methane associated with that coal [Solid Energy (027)]

## **Allocation for lignite or low-grade brown coal**

Parliamentary Commissioner for the Environment (143), supported by Forest & Bird (110), recommended that new industries that use lignite on a large scale are specifically excluded from receiving allocation for the following reasons:

- All uses of lignite (low grade coal) have high carbon footprints
- Companies that develop products from lignite, such as diesel, may be eligible for free allocation worth millions of dollars per year but this will significantly increase the gap between our promise to reduce emissions and the current path we are on.

### **Allocation for intermediate crude oil products**

The NZ Refining Company (NZRC) (043) said that even though they were currently covered by a Negotiated Greenhouse Agreement and were therefore exempt from the ETS, future arrangements for industrial allocation to petroleum refineries is very important for investment decisions. Under current legislation, NZRC would not be eligible for industrial allocation. The legislation needs to be amended urgently so that it is appropriate and operable for the activity of refining petroleum, and so NZRC has certainty to make investment decisions.

### **The process for determining allocative baselines (Question 16d)**

A number of submitters commented on the allocative baselines or suggested changes to the way they are calculated:

- Electricity emissions factor should not be determined theoretically by Government but be based on either (i) the emissions of the highest cost electricity generator, or (ii) a survey of actual electricity price increases [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]
- Baseline calculations may need to be reconsidered to ensure appropriateness of allocation in future [Bank of New Zealand (124)]
- The process needs to be regionally-based as a grower in the South Island may use more energy to grow a crop than a North Island one due to climatic factors. Also, allowance needs to be made for alternative energies that are available [Rockies Mining (024)]

Others said that no change was required because the current process is pragmatic or robust [Oregon Group (080), Holcim (112), Ballance Agri-Nutrients (048), Fletcher Building (076)]

### **Efficiency of allocation to SMEs (Question 16e)**

Some submitters commented on the efficiency of allocation to small and medium-sized enterprises (SMEs). These comments included:

- BusinessNZ (149) proposed that the Panel recommends an independent review of the administrative and compliance regulations, such as those in relation to the establishment and implementation of the allocative baselines, with a view to reducing compliance costs for small businesses
- Horticulture NZ (148) said the application process for industrial allocation was cumbersome and complex, and that there was also a time gap between growers paying the carbon tax

and receiving allocation. This impacted on cash flow, a financial cost carried by business. It also noted that many small growers are unable to sell small bundles of units at a reasonable price compared to larger businesses

- Rockies Mining (024) said small coal mining businesses found the administrative burden of all aspects of the ETS very difficult to manage and that the most effective way to reduce the burden would be to reduce the price of carbon
- The Coal Association (132) said there should be a review of the complex and costly administrative burden faced by small companies
- GL Bowron & Co (074) said the system is not easy to understand, especially for SMEs, and it would be better to develop a simpler system
- It was questionable whether the allocation of units to SMEs is the most administratively or economically efficient way for protecting affected sectors [Steve Wrathall (018), Oregon Group (080)]
- The Employers & Manufacturers Association (070) said the needs of trade-exposed SMEs would be more efficiently met by blanket exemptions or refunds, rather than by allocation.
- Straterra (084) said that the size of the business is irrelevant. If they are emissions-intensive and trade-exposed then they should get allocation.

Besides SMEs, one large business said it had incurred significant administrative costs to obtain and present the information necessary to secure an allocation for their energy-intensive, trade-exposed (EITE) activities - a cost not borne by their competitors [Carter Holt Harvey Pulp & Paper (040)].

## **Other comments about allocation**

Several other issues in relation to allocation were raised and these are summarised below.

### **2014 review of allocation**

Greenhouse Policy Coalition (114) proposed a review in 2014 to see if circumstances remain the same and the transitional measures should continue.

### **Transparency of allocation**

Several submitters criticised the lack of transparency around the allocation of units under the ETS. Comments on the importance of transparency included:

- These units are worth considerable taxpayer money so it should be clear who gets them and why [Carbon Farm (102)]
- It builds public confidence in the system - a lack of transparency can cloak unfairness and dramatic transfers of wealth [Sustainability Council (151)].

Carbon Farm (102) added that arguments against transparency on the basis of commercial sensitivity should be ignored and that if participants wished to maintain that sensitivity, they should refuse to take the credits.

# 11 Operation of the ETS

The *Issues Statement* asked for views on the administrative efficiency of the ETS. In particular the questions were about the compliance costs associated with the ETS (including brokerage fees), complexities of ETS reporting requirements (such as accounting methodologies), penalties for breaching ETS obligations and the organisation of this administration across Government.

The administrative efficiency of the ETS was addressed by 55 submissions.

## Compliance costs associated with the ETS (Question 3a)

There were a range of views on the compliance costs associated with the ETS, from those who expressed that the costs were too expensive, to those who felt that the costs were reasonable.

There were 24 submitters (of which 19 were businesses) who expressed the view that the compliance costs were too high. For some this is a direct cost to the business [Rockies Mining (024), Horticulture NZ (148) and others] and they have passed this increased cost onto the consumer or supplier [Pacifica Shipping (041), GL Bowron & Co (074)]. Carter Holt Harvey Pulp & Paper (040) noted that this increased cost is also seen as a disadvantage to businesses as this cost is not faced by international competitors. The costs are considered high, particularly when assessed on a cost per unit reduction in emissions [NZ Business Roundtable (083)] and this high cost is one of the main reasons for parties deciding not to opt in, and purchase a pass on emissions instead [[withheld] (121)]. The Coal Association (132) said many small coal producers and wholesalers are struggling with the complexity and costs involved in calculating their liabilities.

There were 16 submitters (of which 9 were businesses) who expressed the view that the compliance costs were reasonable. For some the costs were considered minor relative to the benefits received [Southern Forestry (029)], the compliance issues were relatively straightforward [Pacifica Shipping (041)] and the registry is easy to use [Employers & Manufacturers Association (070)]. Some submitters expressed the view that the brokerage fees are comparable to the costs of brokerage in other markets overseas [Fonterra (120), Origin Energy (122)].

Twelve submitters have found that in addition to the costs to register and trade, there has been a significant increase in resource requirements and there will be ongoing resource input. The increase in resources was needed:

- Because the system is very complex [Simon Breeze (021), Rockies Mining (024), Nelson Forests (098), Coal Association (132), Horticulture NZ (148), Sustainability Council (151), Straterra (084)]
- For creating new inventories [NZ Farm Forestry Association (039), Wairakei Pastoral (056)] and maps [Climate Realists (050), Wairakei Pastoral (056)]
- For completing audits, reviews, reports and system improvements [Wairakei Pastoral (056), Ballance Agri-Nutrients (048), NZ Steel (135)]

- For obtaining information necessary to secure allocations [Carter Holt Harvey Pulp & Paper (040), Fletcher Building (076), Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)]
- For assisting with the eligibility and definitions of activities [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107), Greenhouse Policy Coalition (114)]
- For assisting with the collection of trading units [withheld]
- For on-going policy advice, tracking and development [Ballance Agri-Nutrients (048), Wairakei Pastoral (056), Iwi Leaders Group (159)].

Others lack the necessary resources and technical expertise to understand and engage in the ETS [Federation of Māori Authorities (109), Climate Change Iwi Leadership Group (159)].

Some perceive that the process should become easier [Greenhouse Policy Coalition (114)] and that compliance costs are falling as competition increases, greater choice of providers is available, a wider range of services, and more transparency around fees [Carbon Farm (102)]. For example, OMFfinancial (047) charge 10 cents a tonne in brokerage fees, and this is about to drop to 5 cents a tonne. Holcim (112) thought transaction costs had the potential to be significant.

Oregon Group (080) noted there was only a significant one-off registration cost.

A few submitters thought lower transaction costs could be achieved by replacing the ETS with a carbon tax [NZ Business Roundtable (083), Sustainability Council (151), Environment and Conservation Organisations of NZ (161)]. Fonterra (120) noted that to reduce the advent of significant legal costs, a standard emissions purchase agreement should be published and price transparencies should be aided by displaying a weighted price average for all transactions on the unit register. Craigmore Forestry (144) stated that to avoid delays in issuing NZUs, which have caused financial costs to participants, there should be a restructure of the compliance system.

## **Complexities of ETS reporting requirements (Question 3b)**

There were a range of views on the reporting requirements of the ETS, from those who expressed the view that the reporting was very complex, to those who felt that there were no major issues with the reporting.

There were nine submitters (of which eight were businesses) who expressed the view that the reporting was very complex. Rockies Mining (024) stated that the website is difficult to grasp and therefore unhelpful. Small businesses find the issue of trading in credits daunting [[withheld] (049)].

Taumarunui Sustainable Land Management Group (031) expressed concern at lack of transparency in the method of passing on of agricultural ETS costs from processor to producer. Oregon Group (080) stated that owners of less than 100 hectares of post-1989 forest are 'short changed' by not having the option of being able to use the Ministry for Agriculture and Forestry's field measurement approach. NZ Pork (068) questioned the accuracy in reporting and how on-farm liability can be reasonably assessed given the high range of uncertainty surrounding these emission factors.

Wairakei Pastoral (056) stated that the issue is more to do with gaining an understanding of the requirements placed on their business by the ETS, and how they are to be interpreted.

There were also concerns raised by submitters about the time it has taken to have applications processed [Wellington City Council (058)]. Blakely Pacific (154) stated that there have been long delays associated with concluding the regulations around the measurement approach. Bank of New Zealand (124) stated that some of their clients have noted that units are processed faster for PFSI forests and have opted into the PFSI scheme partially to avoid delays in awarding allocations. NZ Steel (135) noted that there are issues with the lack of international accounting standards (taxation etc) for units, which are expected to take 2-3 years to resolve.

There were nine submitters (of which eight were businesses) who expressed that there were no major issues with the reporting. A few submitters stated that they find the Ministry for Agriculture and Forestry's website simple to use [Escea (006), NZ Steel (135)], however the necessary logins took a while to get [Escea (006)]. Some submitters noted that the ETS reporting requirements are well defined, appropriate, and operating smoothly and successfully [[withheld] (049), Genesis Energy (053)].

Genesis Energy (053) also noted that the institutions that support the carbon market, including brokers and other intermediaries, exchange platforms and price discovery tools remain in their infancy, which is to be expected at this early stage of market development.

Carbon Farm (102) stated that all Government agencies involved put a significant amount of effort into consulting on regulations and explaining the rules, however Rockies Mining (024) felt that there was very little training about the scheme in the South Island.

Suggested changes to the reporting requirements are:

- The current default factors chosen for fugitive emissions of methane from coal mines pose a substantial business risk as they are double Australian emission factors and while the unique emission factor process will help to narrow this gap, the required monitoring is complex and costly [Coal Association (132), NZ Coal & Carbon (111)]. NZ Steel (135) also considered that the coal emission factor is inappropriate.
- The present guide on allocating CO<sub>2</sub> emissions from CHP plant mandates the use of default emission factors. The guide clearly states that these emission factors should only be used if actual source-specific efficiency factors are not available. The applicable regulations should be altered to allow the use of source-specific efficiency factors for combined heat and power plants, where these are available [Carter Holt Harvey Pulp & Paper (040)]
- Carter Holt Harvey Pulp & Paper (040) said it is not clear whether the regulations on the obligation thresholds for geothermal steam and waste oil mean that the ETS liability applies only to the emissions over the threshold, or for all emissions when those emissions exceed the threshold

- A system similar to the monthly royalty payments where you pay a percentage of the capped rate as you go, with the funds to be held in a Government secured fund and the miner for example can either top up the difference and pay cash or buy credits and surrender them as they wish [[withheld] (049)]
- The point of obligation for monitoring, mitigating and accounting for agricultural emissions must be at the farm [NZ Pork (068)]
- The use of self-entered electronic mechanisms (audited as necessary) could achieve administrative efficiency for other agricultural gases [Waikato Regional Council (072)]
- The point of obligation should sit at the individual business level, not the sector level [Waikato Regional Council (072)]
- Participants should be encouraged to use more accurate or efficient tools [Oregon Group (080)]
- There should be a standard fee per hectare for participating forests and use LiDAR capture, which quantifies the carbon volume but adds useful forest management data such as contour information [Nelson Forests (098)]
- Determine the extent to which these regulations can be simplified and stream-lined without materially adversely affecting the overall integrity of the ETS [BusinessNZ (149)].

Origin Energy (122) noted a few suggestions including:

- Specify the number of decimal places required for reporting
- Provide a definition of venting
- Provide default factors for flare gas value and flare gas density
- Provide oxidation factors
- Provide guidance of carbon farming initiative and a carbon offset calculation methodology.

A couple of submissions noted that too much weight has been given to the consideration of 'reporting simplicity' in the design of the ETS, which could undermine the integrity of the scheme [Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107)].

### **Penalties for breaching ETS obligations (Question 3c)**

There were a range of views on the penalties for breaching ETS obligations, from those who expressed the view that the penalties are excessive and disproportionate, to those who felt that the penalties needed to be significant enough to encourage compliance.

There were eight submissions (of which seven were businesses) that expressed the view that the penalties are excessive and disproportionate. Reasons stated for this were:

- That it is beyond the perspective of small business [Rockies Mining (024)]

- That it is excessive for what is a self-assessment based system where there is a significant learning curve for both Government and affected parties [Ballance Agri-Nutrients (048)]
- It penalises the introduction of carbon abatement solutions which have advantages over commercial forests in terms of CO<sub>2</sub> sequestration [Bioenergy Association (138), Proprietors of Taharoa C Block (051)]
- It is disproportionate when compared to other statutory requirements and taxation legislation [Holcim (112), NZ Steel (135)].

The Greenhouse Policy Coalition (114) argued that this shows an unwarranted lack of trust in ETS participants and the Coal Association (132) stated that for many smaller coal producers and wholesalers, their greatest fears are that they may inadvertently misinterpret the regulations and find they have huge liabilities because they inadequately charged their customers.

There were three submissions that expressed the view that the penalties needed to be significant to encourage compliance [Oregon Group (080), Carbon Farm (102), OraTaiao: NZ Climate & Health (146)]. Oregon Group (080) also stated that the penalties are comparable with penalties under the Health and Safety in Employment Act, or for breaches of the Resource Management Act.

Craigmore Forestry (144) suggested that there should be greater policy dissemination regarding where the liabilities lie for all scenarios under forest rights, leases, and future sale and purchase transactions.

Horticulture NZ (148) has required management systems to be put in place to cope with deadlines and claim accuracy.

BusinessNZ (149) submitted that businesses should have a grace period in which they have a greater ability to 'learn by doing' and transition to the full compliance regime for 2013 and beyond. Federated Farmers (137) suggested the grace period for penalties upon a sector's entry to the ETS should be retained, albeit with a more general period tied to the flexible entry of new sectors, rather than the legislated dates of entry.

## **Government administration of ETS and the role of the Environmental Protection Authority (Question 3d)**

There were 13 submissions (of which nine were businesses) that expressed the view that the administration of the ETS should come under one agency. Reasons stated for this are that it would be more efficient and simple under one agency [New Zealand Farm Forestry Association (039), Carter Holt Harvey Pulp & Paper (040), Fletcher Building (076), Rockies Mining (024), Climate Change Iwi Leadership Group (159)], and compliance costs should be further constrained if transferred to the Environmental Protection Agency [Contact Energy (089)]. NZ Business Roundtable (083) and BusinessNZ (149) suggested an independent allocation agency should be established, while Richard Leckinger (096) suggested that it should be performed by an existing independent agent. NZ Steel (135) stated that there would be a concern if there was a separation of policy and administration.

Origin Energy (122) supports moving the administrative accountability for the management of ETS across to the newly formed Environmental Protection Authority, and Holcim (112) would like to see administration of the ETS defined as a key priority for the Environmental Protection Authority. Craigmore Forestry (144) states that the role of a future Environmental Protection Authority would be vital to reduce uncertainties around future liabilities lying with the land. Carter Holt Harvey Pulp & Paper (040) and Fletcher Building (076) felt the Environmental Protection Agency's functions do not yet go far enough.

Others support the Ministry for Agriculture and Forestry maintaining its role in the forestry sector, with the administrative role under one agency [Wellington City Council (058)]. Oregon Group (080) stated that names of contact people are more important than Ministry affiliations.

## **Other comments about ETS administration**

There were four submissions that raised concerns about the current security arrangements prevailing in the ETS Registry and suggested that improvements are needed to reduce the risk of unauthorised or fraudulent access to holding accounts [Steve Wrathall (018), [withheld] (081), Methanex (105), Holcim (112)].

Methanex (105) also suggested that a clearer period for the transfer of units is needed, allowing compliance traders the opportunity to operate a 'white list' in order to limit the parties with which transfers from their account can be made.

Solid Energy (027) stated that the Act should be amended so that it operates as a self-contained domestic scheme based solely on NZUs issued by the Government after 31 December 2012.

NZ Forest Owners Association (077) considers that it would be more administratively efficient to dispense with the two-for-one subsidy and simply provide the desired level of subsidy through the free allocation process.

The Greenhouse Policy Coalition (114) stated concern over regulatory hazard presented by any failure to meet deadlines on applying for allocations, i.e. the threat of having allocation stripped.

Qantas (158) stated that there should be regulations that provide transparency of administration fees that fuel suppliers can apply for managing the carbon liability, a transparent carbon price index, an undertaking by the Government to review legislative impediments to carbon reduction across the economy (for example in the areas of airspace management), and the reduction of the time locked in to the decision to 'opt-in' to the New Zealand scheme to two years (six months notice to opt-in, six months notice to exit, one year locked in).

## 12 Other issues (Question 18)

### Climate change science

Climate Realists (050) considered it inappropriate that the issue of climate change science is not within the scope of the ETS Review 2011.

Some submitters expressed their scepticism about global warming [Terry Dunleavy (002), NZ Climate Change Coalition (003), David Slack (008), Steven O'Connor (011), Peter Foster (012), John Adams (013), Steve Wrathall (018), Simon Breeze (021) and ACT (141)]. Raymond Scampton (025) submitted that humans cannot control nature.

David Lloyd (026) argued that pastoral or animal production at a constant rate is carbon-neutral, while Bryan Leyland (001) pointed out that there is uncertainty in the calculation of greenhouse gases absorbed by plant life and the like.

### Measurement of New Zealand's emissions position

The Sustainability Council (151) is concerned that the accounting methodology under the Kyoto Protocol has led to a misleading picture of New Zealand's emissions position, understating the need to reduce emissions. Similarly, 350 Aotearoa (064) disagreed with the Government's emissions accounting practices and considered that the statement that New Zealand is 'expecting to exceed its Kyoto Protocol commitments' is misleading.

### Public interest in climate change

Greenhouse Policy Coalition (114) submitted that, according to a survey, New Zealanders seem less committed to climate change as an issue and are less interested in doing something about it if it costs them.

### Climate change negotiations

350 Aotearoa (064) submitted that young people are often left out as a legitimate stakeholder group in climate change negotiations.

### General comments on the ETS

Some submitters expressed support for the ETS [Richard Leckinger (096), Vector (097)]. Some believed an ETS is the best vehicle for New Zealand to reduce emissions [BusinessNZ (149), Wellington City Council (058), Carbon Farm Limited (102)]

Some other submitters were less enthusiastic about the ETS. Escea (006) considered that the public does not believe the ETS is here to stay. Steve Wrathall (018) raised the issue as to whether the ETS

is an appropriate solution to a non-problem. Rosemary Adams (022) and Raymond Scampton (025) are of the view that the ETS is a hoax.

The NZ Climate Change Coalition (003) suggested that the ETS legislation should remain in place, but its effect should be nullified until climate change science is confirmed or enough trading partners have emissions trading schemes. Arthur Thorstensen (009) considered that any further development of an ETS should be deferred indefinitely. Federated Farmers (137) preferred not having the ETS. A number of submitters argued that the ETS should be abandoned [Bryan Leyland (001), John Newsham (005), Simon Breeze (021), [withheld] (081), ACT (141)].

ACT (141) also submitted that the ETS should be structured to take full advantage of the relative strengths of Government and the private sector. It believes that the private sector is better at allocating scarce resources.

Fletcher Building (076) considered that sharing of emission costs within New Zealand should be determined by the principle of avoiding disruptive and disproportionate economic change. It is not a question of the split between emitters and taxpayers.

## **Purposes of the ETS**

ACT (141) submitted that the purpose of the ETS is unclear, as it has multiple purposes. It suggested that the purposes of the ETS should be ordered in priority, and that a purpose should only be assigned to the ETS if it is achievable by the ETS. ACT (141) believed the only purpose of the ETS should be to signal to the international and domestic communities that New Zealand intends to participate in any meaningful international agreement. It also suggested that there should be clear benchmarks against which the achievement of the purposes of the ETS is measured.

Waikato Regional Council (072) suggested that the ETS should be designed to encourage the development of innovative emissions-reducing solutions, rather than the purchase of offsets. Similarly, Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) considered that New Zealand's policy tools should have the objective of driving emission mitigation innovation and adoption, and not be designed as a mechanism for devolving a Crown liability.

## **Fair share**

WWF NZ (055) suggested that the Panel should undertake an assessment of New Zealand's 'fair share' contribution to emissions reduction and an assessment of how much 'help' the ETS should be providing to meet this fair share.

A few submitters considered that New Zealand's share of global emissions is small [NZ Climate Change Coalition (003), W Newsham (005)].

Some submitters believe that unilateral reduction of emissions does not have long-term benefit; rather, global action is required [Ballance Agri-Nutrients (048), Horticulture NZ (148), NZ Steel (135)].

## Emission reduction targets

Greenpeace (085) considered that New Zealand's 2050 emission reduction target is unlikely to be tenable. Environment and Conservation Organisations of NZ (161) suggested that the 2050 target should be more stringent, and there should be two-yearly milestones of emissions reductions from 2012.

WWF NZ (055) submitted that it is unclear whether the ETS alone is sufficient to deliver the aspirational policy target of 90 per cent of electricity generation from renewable sources by 2025. The Government should therefore consider what grid investments or what electricity market modifications may be required to support a system with 90 per cent of electricity generation coming from renewable sources.

## Overseas action

Some submitters discussed the climate change policies or renewable energy policies in other countries [Carter Holt Harvey Pulp & Paper (040), NZ Forest Owners Association (077), Greenpeace (085), Environmental Defense Fund (095), Greenhouse Policy Coalition (114)].

Beef + Lamb NZ, Meat Industry Association and Deer Industry NZ (107) submitted that an ETS that simply collects revenues for Government or drives a hollowing-out of certain sectors, such as the EU ETS, will lack credibility.

Greenhouse Policy Coalition (114) suggested that we should not pay too much attention to the carbon pricing mechanism currently proposed in Australia.

Straterra (084) and Greenhouse Policy Coalition (114) commented that the summary of mitigation measures in other countries presented in the *Issues Statement* is misleading and largely irrelevant.

## Eligible emission units

Some submitters commented on whether or what overseas units should be acceptable in the ETS. A submitter suggested that all Kyoto units should be admissible in the ETS. Shell (157) submitted that the right to accept equivalent overseas units should remain. BusinessNZ (149) suggested that priority should be given to facilitating access to fungible units from other schemes that meet minimum acceptability standards. BP (079) considered that approved international units must continue to be eligible for use in meeting obligations under the ETS. Origin Energy (122) considered that restriction on surrender of AAUs under the Kyoto Protocol for post-2012 emissions should be removed, and that Australian AAUs should be allowed to be surrendered for compliance in the ETS. Environmental Defense Fund (095) considered it would be good to open the ETS to Reducing Emissions from Deforestation and Forest Degradation (REDD) credits. BusinessNZ (149) thought offsets from HFC 22 and adipic acid CDM projects should not be banned from the ETS, even though the EU ETS does.

On the other hand, Southern Forestry (029) commented that there are huge risks to admitting low-priced offshore SGG units that cannot be admitted in the EU ETS. Some submitters submitted that

industrial gas CERs should be banned from the ETS from 2013 [OMFinancial (047), Forest Management (075), NZ Forest Owners Association (077), Kyoto Forestry Association (078), Oregon Group (080), Carbon Farm (102), Lake Taupo and Lake Rotoaira Forest Trusts (142)]. Nelson Forests (098) submitted that CERs from low environmental integrity projects must be banned after 2012. Some submitters suggested that un-greened hot air units should not be allowed to directly enter the ETS [NZ Forest Owners Association (077), Kyoto Forestry Association (078), Carbon Farm (102), Lake Taupo and Lake Rotoaira Forest Trusts (142)].

Escea (006) considered it likely that international carbon markets will be able to manage dubious carbon credits created by countries with high levels of corruption and weak Governments.

## **Fossil fuels**

Gelita (017) considered that fossil fuels will continue to be a vital energy source in the foreseeable future. Nova Trust (066) noted that, in Canterbury, there are very few alternative energy sources to coal. John Newsham (005) advocated the use of Southland coal for power generation.

Employers & Manufacturers Association (070) suggested that diesel fuel should be excluded from the ETS. On the other hand, M Dumbar (010) was of the view that fossil fuels causing more greenhouse gas should be taxed more.

Mobil (140) made the following suggestions regarding ETS-exempt fuel:

- The Government should provide clear guidance in regulations on what evidence is required to be provided by a fuel consumer to an ETS participant (who is a fuel company) in support of a request to be sold ETS-exempt fuel
- The Government should have a mechanism to monitor the activities and records of fuel consumers who have purchased ETS-exempt fuel, such as a registration system
- Fuel consumers, who on-sell fuel for ETS-exempt use at a later date, without having been charged the ETS costs by fuel companies in the first instance, should be allowed to become voluntary ETS participants. Alternatively, fuel consumers, who on-sell fuel for ETS-exempt uses, should periodically report such sales to the Government and should be eligible for an allocation in respect of these sales.

Linfox Logistics (093) supported the point of obligation for the transport sector at the distributor level.

KiwiRail (086) would like to be able to manage pricing risks associated with carbon directly, however the ETS does not allow it to become a voluntary participant.

## **Other transition measures**

Federated Farmers (137) also suggested the payment of money instead of emissions units should be retained to mitigate the risks associated with low liquidity in the ETS and difficulties in securing overseas units. In addition, the ability for the Government to issue NZUs where money is paid by ETS

participants in lieu of emissions units should be retained. It also commented that prohibition of export of NZUs needs to be reviewed.

## **GST treatment of NZU transactions**

Rockies Mining (024) was of the view that charging GST on top of the ETS costs is not fair. It also commented that there is no assistance from Inland Revenue regarding GST treatment of NZU transactions.

## **Relief from the ETS costs in certain circumstances**

Rockies Mining (024) submitted that an ETS participant should be relieved from the ETS costs in circumstances where its customer's business fails.

## **Information issues**

A number of submitters raised the following information issues:

- There is no assistance from accountants or lawyers regarding the ETS [Rockies Mining (024)]
- Businesses need a list of legitimate buyers and sellers of carbon credits [Rockies Mining (024)]
- Businesses need information on what types of carbon credits can be bought for ETS compliance [Rockies Mining (024)]
- There were not enough ETS workshops for businesses before the implementation of the ETS [Rockies Mining (024)]
- There is not enough ETS education for the farming sector [Wairakei Pastoral (056)].

## **Entering contracts with private actors**

Motu Economic and Public Policy Research (139) suggested that the Government should enter into contracts with private actors to buy NZUs in the future at fixed prices. This would provide more price certainty and make efficient investments possible. Alternatively, the Government could invest now in sequestration or emissions reduction projects and in exchange the company could contract to receive fewer free NZUs in future.

## **Offset mechanism**

BusinessNZ (149) submitted that there should be an expansion of the offset mechanism to include both ETS participants and non-participants.

## Complementary measures and alternative policies

Bill Sayer (014) considered that a strategy is needed to plan, direct and monitor how we reach the 2050 emissions reduction target. Wellington City Council (058) believes alignment is needed across all Government policies, strategies and funding. Currently, there are inconsistencies between the ETS and other key Government policies, such as the Energy Strategy. Mighty River Power (130) also suggested that a holistic and complementary approach is needed in other areas of policy development, for example, in the anticipated National Policy Statements on Renewable Energy Generation and Freshwater Management.

General Electric (150) believes a price on carbon pollution can and should be supported by complementary measures. Motor Trade Association (052) and Wellington City Council (058) also support the introduction and expansion of complementary measures. Some submitters suggested that the following complementary measures should be considered:

- Adaptation measures [BusinessNZ (149)]
- Special transition arrangements for encouraging the development of carbon capture schemes [Shell (157)]. The Coal Association (132) supported the Government's commitment to carbon capture and storage research
- 'No regrets' measures, policies that are justified in their own right but also contribute to emissions reductions, such as road pricing policies [Business Roundtable (083)]
- Other measures to target non-price barriers to change, such as measures that address attitudinal changes, information gaps, capital barriers, technology development, and the international competitiveness of low-carbon industries [Wellington City Council (058), BP (079) and Greenpeace (085)]
- Technology and research grants for clean and green technologies [Climate Change Iwi Leadership Group (159)]. ALSCO NZ (057) commented that the Government provides very little assistance in terms of technology grants.
- Support for the clean technology sector, such as a contestable fund for low-cost equity or debt finance, if the transition phase does not end from 2013 [Pure Advantage (162)]
- Changes to the building code [Escea (006)]
- Subsidise carbon-neutral or nearly carbon-neutral energy sources [M Dumbar (010)]
- Improve public transport and promote other low-carbon options [Environment and Conservation Organisations of NZ (161)]
- Educate and subsidise businesses and households to lower emissions [OraTaiao: NZ Climate & Health (146)]
- Cut income tax and impose a tax on petrochemicals [Harry Mowbray (160)].

Some submitters suggested alternative policies to the ETS. New Zealand Business Roundtable (083) and ACT (141) considered that a carbon tax is preferable to the ETS. The Campaign for Better

Transport (153) suggested that the ETS component on petrol should be replaced with a direct tax on petrol. Revenue from this tax should be ring-fenced for mitigation projects and be available to local Councils.

Southern Forestry (029) thought the funding for the Energy Efficiency and Conservation Authority would be well spent elsewhere.

## **Using NZUs to pay for increased electricity costs**

One submitter [withheld] said it had been unable to meet the ETS-related costs of stationary energy by surrendering its allocation directly to electricity retailers as part payment for electricity charges. This had been rejected by electricity retailers because of the perceived difficulties in determining the ETS-related component of electricity prices. It recommended that the Act be amended to require electricity retailers to accept NZUs as part payment for electricity charges, where the component of the electricity charge attributable to the ETS can be reasonably determined.

## **Market liquidity**

[withheld] (121) noted there was limited market liquidity, with the result that a ready forward market for carbon, around which participants would be able to plan and develop their businesses, had not eventuated. The consequences of this were a lack of transparency (inability to discern price trends), the need to do less than robust or complex 'deals' with third parties, such as foresters and traders, and higher transaction costs.

## **Process for the ETS Review**

Some submitters made comments on future ETS reviews. The Climate Change Iwi Leadership Group (159) considered that the next ETS review should be held by 2014. On the other hand, BusinessNZ (149) was of the view that scheduled ETS reviews should be removed to provide greater long-term predictability of policy settings.

Some submitters made the following suggestions on how the ETS should be conducted:

- The Panel should issue a summary of its conclusions before issuing its draft report to the Minister [BusinessNZ (149)]
- A robust, detailed economic analysis (in consultation with energy users) is necessary before making any recommendations on future ETS settings [Coal Association (132)]