



Cabinet

Minute of Decision

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New Zealand Emissions Trading Scheme Settings: Consultation Document

Portfolio **Climate Change**

On 16 December 2019, following reference from the Cabinet Environment, Energy and Climate Committee, Cabinet:

- 1 **noted** that the New Zealand Emissions Trading Scheme (NZ ETS) is a key tool to support meeting New Zealand's climate change targets and transitioning to a low emissions economy;
- 2 **noted** that proposals for NZ ETS settings will support the effective operation of the NZ ETS;
- 3 **noted** that consulting on NZ ETS regulations at the same time as the select committee stage of the Climate Change Response (Emissions Trading Reform) Amendment Bill (the Bill) will enable the public to consider the proposals together;
- 4 **noted** that the Bill specifically empowers consultation on regulations to take place prior to the Bill coming into effect;
- 5 **agreed**, for the purpose of consultation, that the proposed provisional emissions budget for 2021 - 2025 be 354 Mt CO₂-e;
- 6 **noted** that the proposed provisional emissions budget for 2021 – 2025 requires 13 Mt CO₂-e of emissions reductions or sequestration beyond current forecasts;
- 7 **agreed**, for the purpose of consultation, that the proposed NZ ETS emissions cap for 2021-2025 be 151 million units, made up of these key sources of emission unit supply:
 - 7.1 the expected volume of units to be freely allocated (44 million New Zealand Units (NZU));
 - 7.2 the volume of units to be auctioned (80 million NZUs);
 - 7.3 the import of international units (zero);
 - 7.4 the use of units already in participants' accounts (27 million NZUs);
- 8 **noted** that price controls are mechanisms that help manage unacceptably low or high prices in the NZ ETS and limit the risk of prices falling outside of a range needed to meet an emissions budget;

- 9 **agreed**, for the purpose of consultation, that the proposed price control settings are:
- 9.1 a price floor of a value of \$20 per NZU for 2020-2025;
- 9.2 a price ceiling, implemented through a ‘cost containment reserve’, of \$50 per NZU for 2020-2025;
- 10 **noted** that, although the price ceiling is the upper extreme of expected and acceptable prices in the NZ ETS, it will not be the key driver for the market price, which will be ultimately determined by unit supply and demand;
- 11 **noted** that provisional emissions budget settings will cap emissions in the NZ ETS for 2020 and 2021;
- 12 **noted** that the government will make emissions budget settings decisions for the years 2022–2025, 2026–2030, and 2031-2035 following consideration of advice from the Climate Change Commission in early 2021;
- 13 **noted** that the government will make subsequent decisions about future NZ ETS settings, including price controls, based on these emissions budgets and advice from the Climate Change Commission;
- 14 **authorised** the Minister for Climate Change and the Minister for the Environment to approve changes to the consultation document to reflect the above decisions;
- 15 **noted** that under the current drafting of the Bill, the fixed price option will be replaced by the cost containment reserve from the first auction;
- 16 **noted** that the arrangement, referred to in paragraph 15 above, has a high risk of market instability due to the market power this gives to sources of supply over 2020, should the first auction be held at the end of 2020, as is planned;
- 17 **noted** that a continuation of the fixed price option available for 2020 emissions will provide certainty of emission unit supply for participants until government auctions are fully operational in 2021;
- 18 **noted** that an increase of the fixed price option to \$35 per NZU to apply for surrender obligations arising from activities in 2020 signals the government’s intention to accelerated emission reductions in the economy, while providing for market stability and predictability;
- 19 **agreed**, for the purpose of consultation, to a policy change that will allow the continuation of the fixed price option to meet surrender obligations for 2020 activities;
- 20 **agreed**, for the purpose of consultation, that the rate of the fixed price option be \$35 per NZU for all surrender obligations arising from 2020 activities;
- 21 **agreed**, for the purpose of consultation, that the volume of units available annually within the cost containment reserve will be based on 90 per cent of the difference between forecast net emissions and the volume of units added to the scheme;
- 22 **noted** that market impacts of releasing different cost containment reserves is a particularly challenging area to forecast, and that the Ministry for the Environment will convene a group of industry experts to discuss this area further during consultation before final regulation recommendations are made;

- 23 **agreed** to release the consultation document attached to the paper under ENV-19-SUB- 0073 (the consultation document) to support public consultation from mid-December 2019 to late-February 2019 on proposals for NZ ETS settings, **subject to** any changes to the document to reflect the above decisions;
- 24 **noted** that the Minister for Climate Change and the Minister of Energy and Resources will consider releasing the discussion document, attached under ENV-19-SUB-0073, together with the consultation document *Accelerating renewable energy and energy efficiency*, attached under ENV-19-SUB-0072;
- 25 **authorised** the Minister for Climate Change to make minor editorial, design and technical and minor policy changes to the consultation document as needed;
- 26 **noted** that the Minister for Climate Change will report back to Cabinet by mid-2020 with final policy recommendations;
- 27 **noted** that the proposals in the paper under ENV-19-SUB-0073 and its attached appendices are commercially sensitive, and that the release of this information will have implications for the NZ ETS market;
- 28 **noted** that considerations around public release of information need to be managed carefully;
- 29 s 9(2)(j) 
- 30 **noted** that the Framework for International Carbon Markets Cooperation provides guidance to officials in discussions with potential international carbon market partners;
- 31 **agreed** that the Framework for International Carbon Markets Cooperation be publicly released alongside the consultation document on NZ ETS settings;
- 32 **noted** that a formal negotiating mandate would be needed from Cabinet before any formal negotiations on international carbon market cooperation could begin;
- 33 **directed** officials to undertake further work on what emission reductions would occur at different price points and report back to ENV in due course.

Michael Webster
Secretary of the Cabinet

Hard-copy distribution:

Prime Minister
Deputy Prime Minister
Minister of Energy and Resources
Minister for the Environment
Minister for Climate Change