

New Zealand Emissions Trading Scheme interim auction monitor report

16 March 2022 auction



Ministry for the
Environment
Manatū Mō Te Taiao



Te Kāwanatanga o Aotearoa
New Zealand Government

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Introduction and purpose of this report

This report is produced by the Ministry for the Environment (MfE) acting in the role of the interim auction monitor for the fifth scheduled New Zealand Emissions Trading Scheme (NZ ETS) auction, the first for 2022, held on 16 March 2022.

Auctioning of New Zealand Units (NZUs) is currently scheduled at quarterly intervals throughout the year as prescribed by the Climate Change Response (Emissions Trading Reform) Amendment Act 2020 and the Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020.

The purpose of this report is to record and provide details on the results of the auction, to present a comparison with previous auctions, and to provide an assurance that the auction was conducted properly and in accordance with the applicable rules and laws.

The remaining auction dates for 2022 are 15 June, 7 September and 7 December.

Background

Following the 2015/16 review of the NZ ETS, the Government agreed to introduce auctioning of NZUs to align the supply of units in the scheme with New Zealand's climate change targets.¹ Further public consultation on auctioning regulations took place between November and December 2019.²

Following extensive regulatory and legislative development and an open market procurement process, an auction operator was appointed to run regular scheduled auctions through the NZX Managed Auction Service.

The first auction occurred on 17 March 2021.

This report concerns the fifth scheduled auction which occurred on 16 March 2022.

Auction monitor to provide information on auctions

The appointment of an auction monitor requires regulations to be made prescribing the appointment process and the functions of the auction monitor.

Until the required consultations and regulation development have been concluded to appoint an auction monitor, the Minister of Climate Change has agreed that the Ministry for the Environment will perform the function of the auction monitor, referred to in this document as interim auction monitor (IAM).

The IAM function is performed independently of the auction operator and of the Ministry for the Environment policy team responsible for developing the regulations for the auction monitor and auctioning.

(Interim) auction monitor's functions

Based on feedback from the 2019 consultation, the Government agreed that the auction monitor should:

- publish certain information about each auction as soon as is practical following the auction
- publish a report on the outcome of each auction before the next auction occurs
- review the auctioning system after the first year and every subsequent two years.

Cabinet has agreed that the auction monitor must publish a report containing prescribed information from each auction and on the outcome of each auction prior to the subsequent auction occurring [DEV-20-MIN-0047].³

The auction operator [publishes information about NZ ETS auctions](#), which can be read in conjunction with this report.

¹ <https://environment.govt.nz/assets/Publications/amendments-to-ccra-tranche-1-cab-18-min-0606.01.pdf>

² <https://environment.govt.nz/publications/reforming-the-new-zealand-emissions-trading-scheme-rules-for-auctioning-summary-of-submissions/>

³ <https://environment.govt.nz/assets/Publications/DEV-20-MIN-0047-Minute.pdf>

Auction information: 16 March 2022

Auction metrics

Table 1 provides relevant metrics of the auction. Further details are presented graphically in the appendix.

Table 1: Metrics for NZ ETS auction held on 16 March 2022

Number of participants	32
Number of successful participants	30
Volume available at auction (including the CCR of 7 million NZU)	11,825,000
Volume of NZU sold	10,518,300
Volume of NZU Bid for	11,727,400
Average Bid Size	24,586
Average volume bid per participant	366,481
Average volume won per successful participant	350,610
Average number of bids per participant	11
Total number of bids submitted (not including withdrawn bids)	477
Number of bids withdrawn	9
Number of successful bids	350
Aggregate Top Five Participants (aggregated successful bids) as a percentage of total units sold	78
Herfindahl–Hirschman Index (measure of market concentration by volume purchased 'Top 10)	0.18
Percentage of bidders with mandatory compliance obligations	50

Commentary on the results of the auction

The NZ Emissions Trading Scheme auction for 2022 was successfully held on 16 March 2022. The first auction of the year, the full cost containment reserve volume of 7 million NZUs was available, adding to the 4.825 million units scheduled for sale as approved by Cabinet and as published in October 2021.

A relatively low number of new participants (eight) were registered by the auction operator though not all participated in the March 2022 auction. There are currently 92 registered participants.

Of the 32 entities who participated in the March 2022 auction, 30 were successful in their bids. This high success rate is likely attributable to the availability of the additional CCR volume of which 81 per cent was purchased.

The market concentration index reveals an overall increase in the 'competitiveness' of the auction although the top five participants still purchased over 78 per cent (top 10, 94 per cent) of the sold volume.

As noted over the last year, it is very likely that several of the larger players represent a number of third-party bidders. This is also germane in considering the fifty percent of participants in the auction who have obligations under the NZ Emissions Trading Scheme.

The early months of 2022 saw a significant increase in the secondary market prices for NZU. Global political and economic influences precipitated a sharp drop in international carbon prices in early March, recovering somewhat and stabilising in the days immediately preceding the 16 March auction.

The auction clearing price

The auction operator is required to publish the clearing price following the auction.

The IAM notes that the CCR trigger price was breached and as the CCR volume was not exhausted in this auction, the auction clearing price was correctly interpreted as \$70 per NZU (the CCR trigger price).

The confidential reserve price

The Climate Change Response Act enables the Minister of Climate Change to set a methodology for calculating a confidential reserve price for NZ ETS auctions. The confidential reserve price has the purpose of preventing NZUs from being sold at auction at a price significantly below the secondary market price. If the auction clearing price is less than the confidential reserve price, the auction will not sell any NZUs. Unsold NZUs will be rolled forward to be sold at the next auction in the same calendar year.

As was the case in the March 2022 auction, the legislation requires that the confidential reserve price cannot exceed the trigger price(s) for the cost containment reserve.

The auction operator has robust procedures and checks in place to ensure that the confidential reserve price is correct. The IAM is satisfied that these checks are sufficient and that the clearing price was above or equal to the confidential reserve price.

The IAM independently confirms that the calculated confidential reserve price did not have an impact on this auction.

Resolved tied bids

If more than one bid sets the clearing price, those bids are referred to as tied bids. If all tied bids together bid for more units than are left, each tied bid is allocated a proportional share of the remaining units, subject to rounding rules. Bids are only accepted in multiples of 100 units from 500 units (the lot size and minimum bid respectively). Units are allocated to bids in multiples of lot size. Therefore, when tied bids occur and the operator calculates proportional shares, they apply the following rounding rules:

- the number of units allocated to a tied bid, if not a multiple of the lot size, is rounded down to the nearest 100 units (this may include being rounded down to zero)
- if unallocated units remain after tied bids are awarded their proportional share (rounded to the nearest 100 units), any remaining lots are randomly allocated to the tied bids, but only up to their original bid amount.

The IAM has examined how units have been allocated among bids and confirms that the auction operator has correctly applied the allocation and rounding rules.

There were no tied bids requiring consideration in the March 2022 auction.

Cost Containment Reserve (CCR)

The cost containment reserve (CCR) mechanism provides for an additional volume of NZUs to be added to the auction volume if the auction clearing price is equal to or exceeds the CCR trigger price. Currently, there is only one trigger price level in an ETS auction. The cost containment reserve trigger price for the March 2022 Auction was set at \$70 per NZU, as previously published.

The available CCR volume to be shared across all four auctions in 2022 is 7.0 million NZUs.

Both the CCR trigger price and available volumes are set by regulation, though both may be reviewed and are subject to change. The available annual auction volumes and auction dates are published in October of the preceding year by the Ministry for the Environment.

The CCR trigger price was breached in the March 2022 auction and the full CCR reserve volume (7.0 million NZUs) was available of which 5.7 million units were sold.

Commentary on the auction operation

General

The auction operator has confirmed that the auction ran smoothly with no outages or delays. New participants continue to register as interest in the auctions increases.

The IAM has no reason to believe that the auction rules were not followed.

Collateral and settlement

There were no significant issues noted with the receipt of collateral or the timely payment of invoices for settlement notwithstanding the administrative challenges of 'last-minute' payments and international time zones. All invoices for successful participants were settled within four working days of the auction.

Uncommitted collateral was returned to participants promptly.

Standby Letters of Credit (SBLC) were the preferred instrument for lodging non-cash collateral for six of the participants, though continuing the trend, most buyers deposited cash as collateral. Again, the value of cash and SBLC received was about the same.

All NZUs were transferred to successful bidders' NZ ETS Registry accounts on the same day as the invoice settlement date.

The IAM notes that all participants lodged collateral within the prescribed timeframes, and all successful participants received their allocated units within the prescribed timeframe.

Feedback on the auction monitoring report

Please send any information about the ETS auctions to the interim auction monitor at etsconsultation@mfe.govt.nz for consideration in future reports.

Appendix

Graphical presentation of historical auction metrics

Legend for graphs in this report

Mar. 21 Auction 1, held on 17 March 2021

June Auction 2, held on 23 June 2021

Sept. Auction 3, held on 1 September 2021

Dec. Auction 4, held on 1 December 2021

Mar. 22 Auction 1, held on 16 March 2022

The most recent auction and four trailing auctions will be presented in this appendix.

Figure A.1: Volume of NZUs bid for and Cover Ratio in each auction

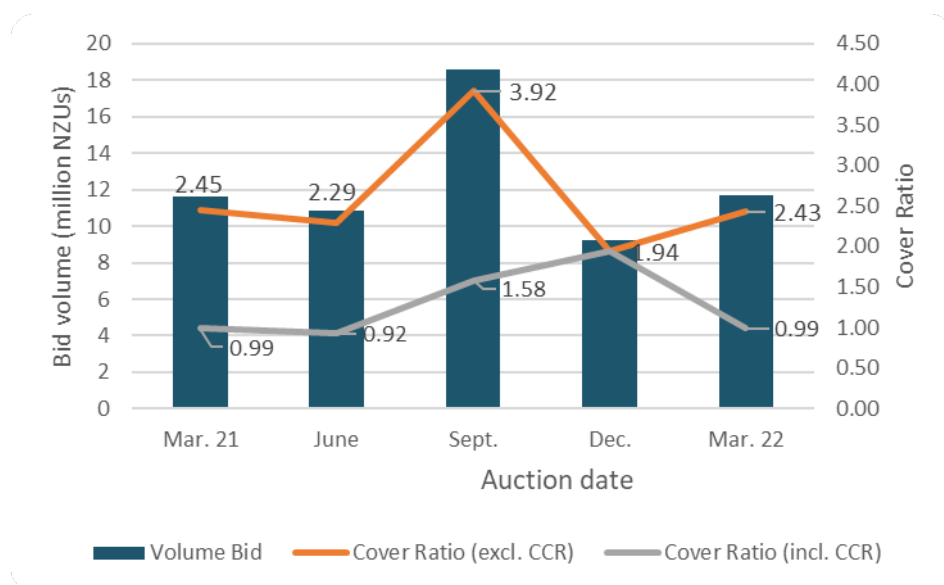


Figure A.2: Total number of bids in each auction

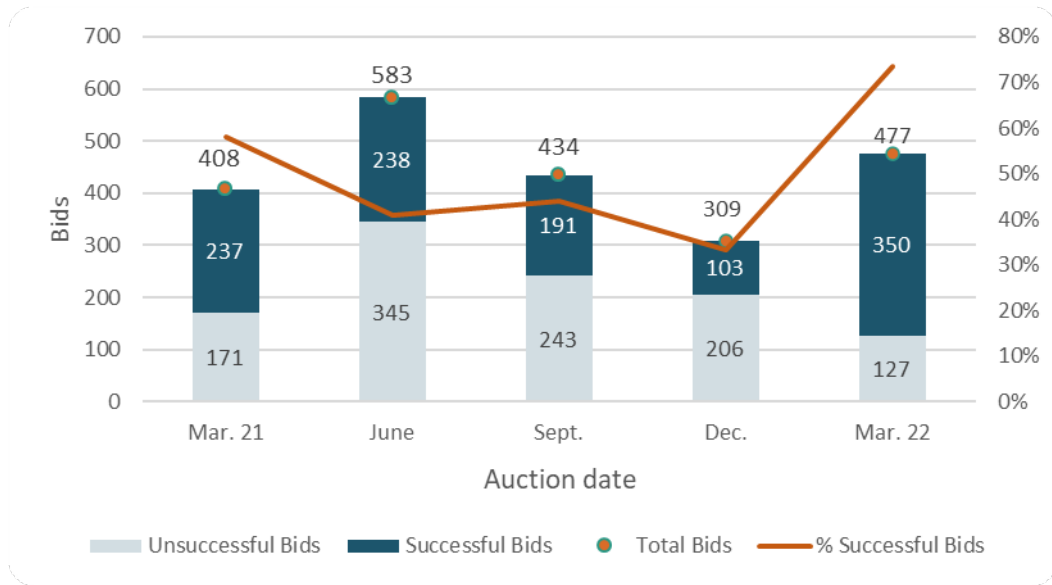


Figure A.3: Participant numbers in each auction

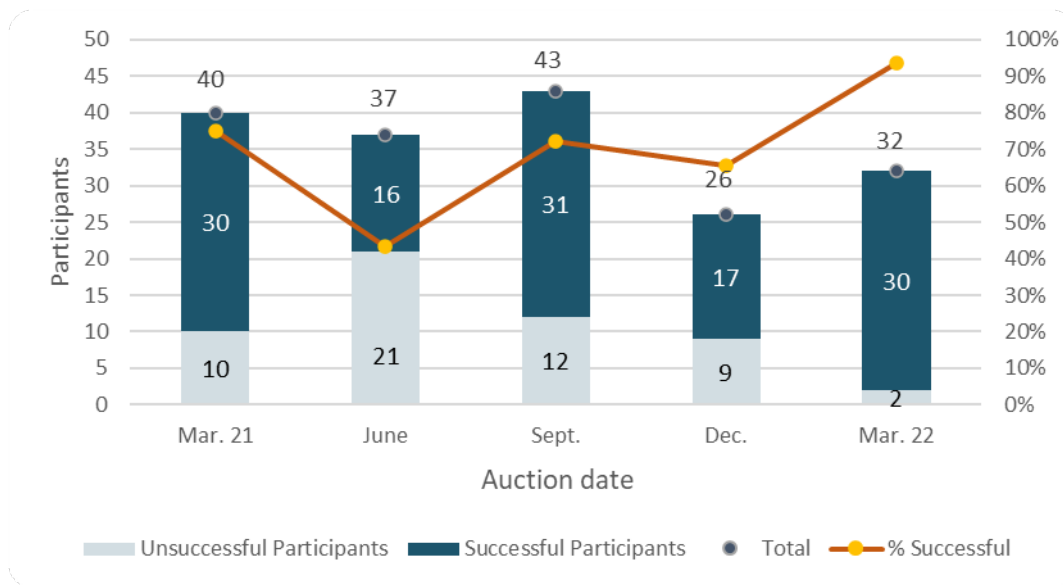
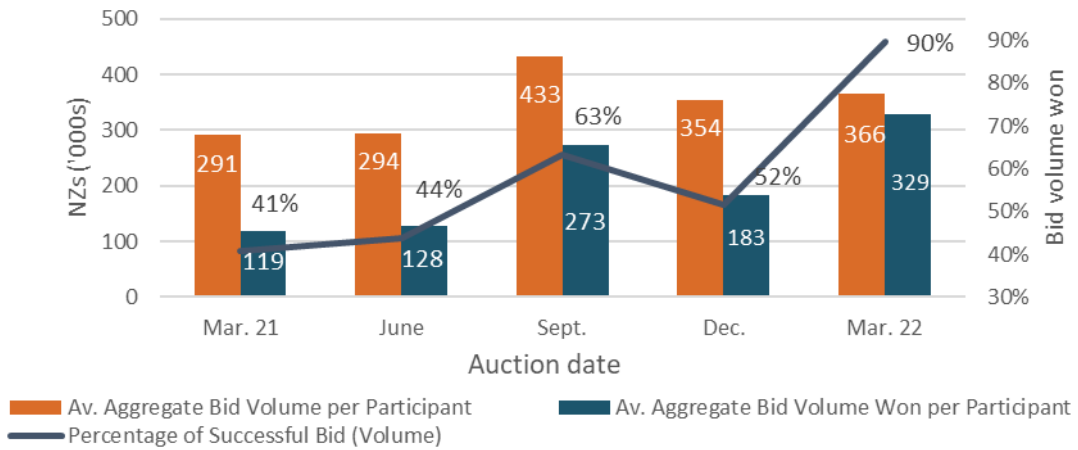


Figure A.4: Bid volume (of thousands of NZUs) per participant and 'win' ratio



Note that many participants submitted multiple bids and there may be multiple bidders representing a single participant.

Figure A.5: Breakdown of successful bids by participant, March 2022

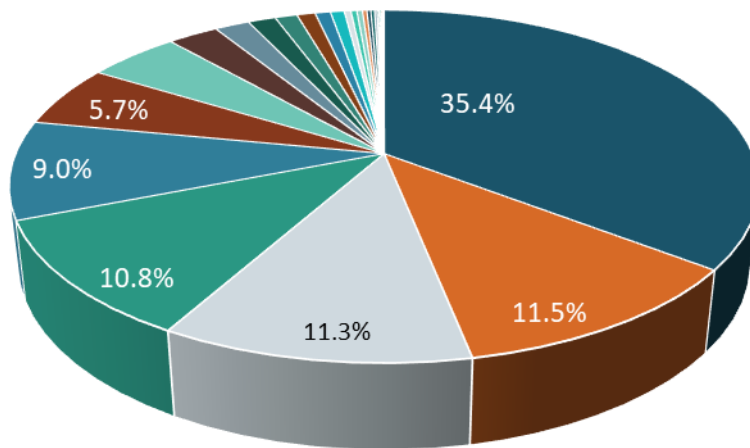


Figure A.6: Breakdown of successful bids aggregated by participants

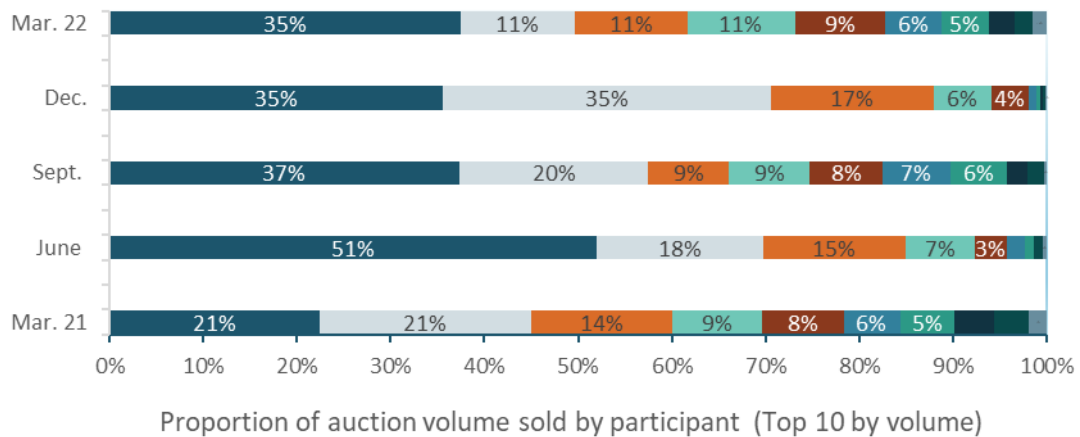


Figure A.7: Proportion of Participants with mandatory compliance obligations under the NZ ETS

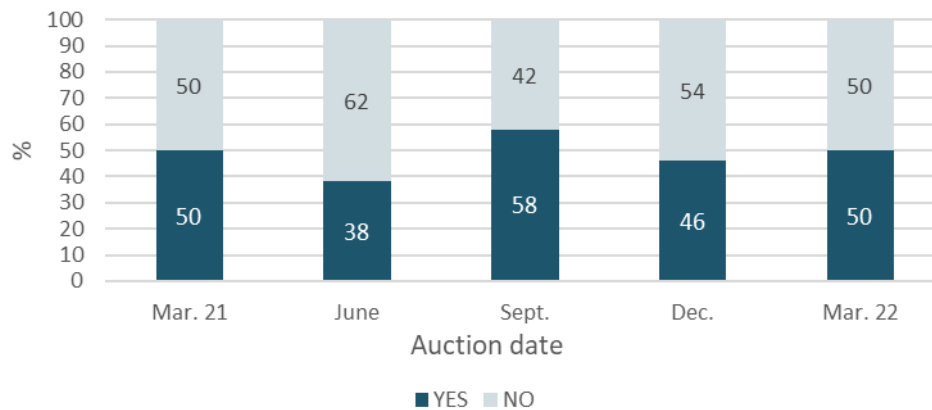


Figure A.7 represents the number of participants that are registered as having mandatory compliance obligations on the ETS Register. ‘Larger volume’ participants not necessarily registered as having compliance obligations, may be purchasing NZUs on behalf of ‘smaller’ third parties that do have compliance obligations.

References

New Zealand Cabinet. 2018. *Amendments to the Climate Change Response Act 2002: Tranche One*. Cabinet Committee Minute of Decision CAB-18-MIN-0606.01. Wellington: Cabinet Office, Department of the Prime Minister and Cabinet.

Ministry for the Environment. 2019. *Reforming the New Zealand Emissions Trading Scheme: Rules for auctioning*: Technical consultation document. Wellington: Ministry for the Environment.

New Zealand Cabinet. 2020. *New Zealand Emissions Trading Scheme: Regulatory Decisions on the Rules for Auctioning*. Cabinet Economic Development Committee Minute of Decision DEV-20-MIN-0047. Wellington: Cabinet Office, Department of the Prime Minister and Cabinet