



New Zealand Emissions Trading Scheme Interim Auction Monitor Report

1 September 2021 auction



Ministry for the
Environment
Manatū Mo Te Taiao

Te Kāwanatanga o Aotearoa

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Contents

| | |
|--|----|
| Introduction and purpose of this report | 3 |
| Background | 4 |
| Auction monitor to provide information on auctions | 4 |
| (Interim) auction monitor's functions | 4 |
| Auction information: 1 September 2021 | 5 |
| Auction metrics | 5 |
| Commentary on the results of the auction | 5 |
| The auction clearing price | 5 |
| The confidential reserve price | 6 |
| Resolved tied bids | 6 |
| Cost Containment Reserve (CCR) | 6 |
| Commentary on the auction operation | 8 |
| General | 8 |
| Collateral and settlement | 8 |
| Feedback on the auction monitoring report | 9 |
| Appendix | 10 |
| References | 13 |

Tables

| | |
|--|---|
| Table 1: Metrics for NZ ETS auction held on 1 September 2021 | 5 |
|--|---|

Figures

| | |
|---|----|
| Figure A.1: Volume of NZUs bid for and Cover Ratio in each auction | 10 |
| Figure A.2: Total number of bids in each auction | 10 |
| Figure A.3: Participant numbers in each auction | 11 |
| Figure A.4: Bid volume (of thousands of NZUs) per participant and 'win' ratio | 11 |
| Figure A.5: Breakdown of successful bids by participant, September 2021 | 12 |
| Figure A.6: Breakdown of aggregated successful bids by 'Top 10' participants 2021 | 12 |
| Figure A.7: Proportion of Participants with mandatory compliance obligations under the NZ ETS | 12 |

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 third scheduled New Zealand Emissions Trading Scheme (NZ ETS) auction of 2021 held on 1 September 2021.

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 provide 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.

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 third auction of 2021, which occurred on 1 September 2021.

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 (MfE) will perform the function of the auction monitor, referred to in the document as interim auction monitor (IAM).

The IAM function is performed independently of the auction operator and of the MfE 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: 1 September 2021

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 1 September 2021

| | |
|--|---------|
| Number of participants | 43 |
| Number of successful participants | 31 |
| Average bid size | 42,855 |
| Average volume bid per participant | 432,544 |
| Average volume won per successful participant | 379,032 |
| Average number of bids per bidder | 10 |
| Total number of bids submitted (not including withdrawn bids) | 434 |
| Number of bids withdrawn | 49 |
| Number of successful bids | 191 |
| Largest participant (aggregated successful bids) as a percentage of total units sold | 37% |
| Herfindahl–Hirschman Index (measure of market concentration Top 10) | 0.205 |
| Percentage of bidders with mandatory compliance obligations | 58.5% |

Commentary on the results of the auction

The third quarterly auction of 2021 was held on 1 September. For the first time and as anticipated by the market, the cost containment reserve was triggered. Possibly less expected was that the entire CCR volume was purchased with a consequent increase in the clearance price above the \$50 trigger price.

The number of registered participants continues to increase (77) with 19 first-time participants in the September auction.

At 72%, the number of successful participants has rebounded from just above 40% in the previous auction.

There remain a small number of larger participants by volume purchased, however, the market concentration metrics suggest that the market has become more competitive – though the impact of the CCR volume may have been influential in this auction.

The auction clearing price

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

The IAM has calculated the clearing price using raw data provided by the auction operator and confirms that the clearing price of \$53.85 is correct.

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.

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 the confidential reserve price.

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.

There were two tied bids at the revised clearing price (i.e., at the price that all available NZU volume, including that of the cost containment reserve, was exhausted).

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

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 September auction was unchanged from the first two auctions at \$50.00 per NZU.

The available CCR volume to be shared across all four auctions in 2021 is 7.0 million NZUs.

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

The CCR trigger price was reached in the September auction and the full CCR reserve volume (7.0 million NZUs) was sold.

The 'interim clearing price' i.e., the price at which the full auction volume would have been sold in the absence of additional (CCR) volume, was \$57.00.

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.

Processing funds, including the return of unused collateral to participants as rapidly as practically possible post-auction (a function performed by MfE Finance personnel), continue to become further streamlined as participants, the auction operator and MfE become more familiar with the auctioning processes.

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

Collateral and settlement

All of the potential participants who lodged collateral 'in cash' did so on or before T-5⁴ (25 August 2021). 83% of the cash was lodged on 25 August and 12.25% lodged on 24 August (T-6), with the remaining being lodged on T-7 or earlier.

All invoices for successful participants were processed and were settled by T+4 (7 September 2021). There were no invoice defaulters.

All NZUs were transferred to successful bidders' NZ ETS Registry accounts on T+4 (7 September 2021).

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

⁴ T-5 refers to the day five working days prior to the day the auction was held on.

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

| | |
|-------|--|
| March | 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, scheduled for 1 December 2021 |

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

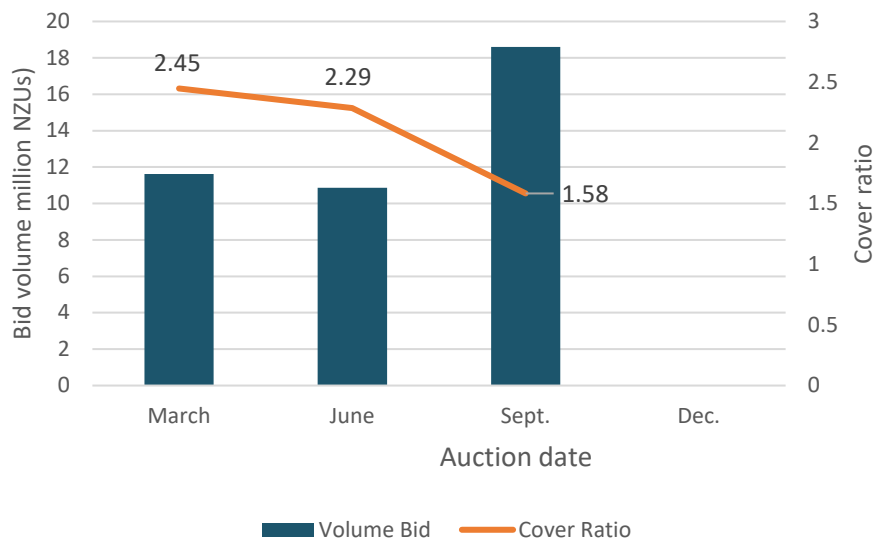


Figure A.2: Total number of bids in each auction

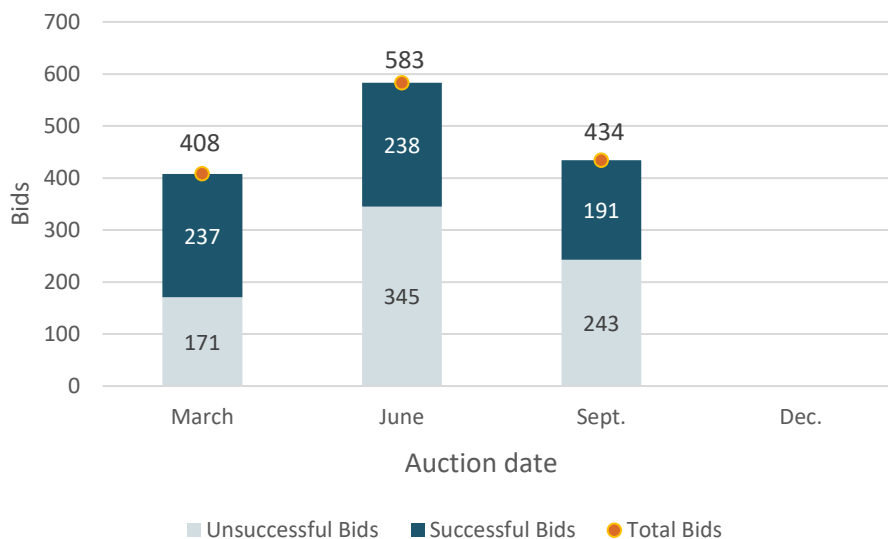


Figure A.3: Participant numbers in each auction

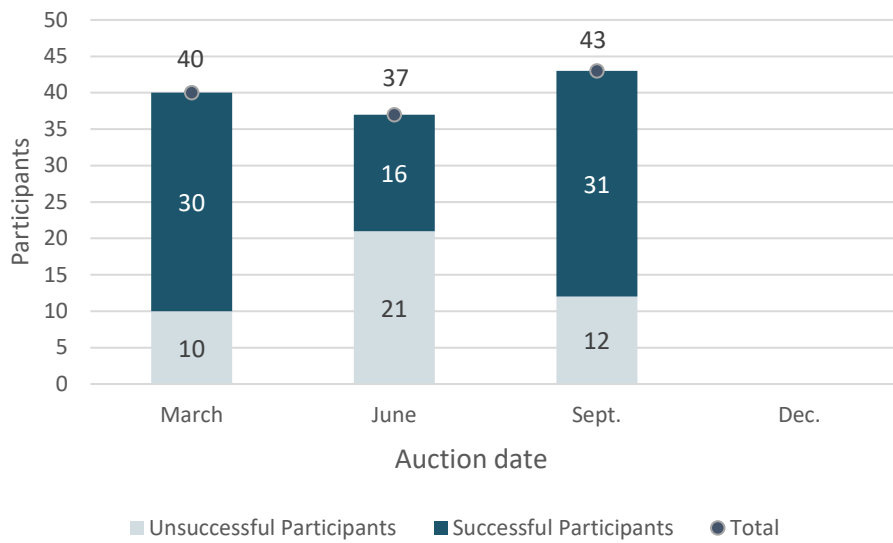
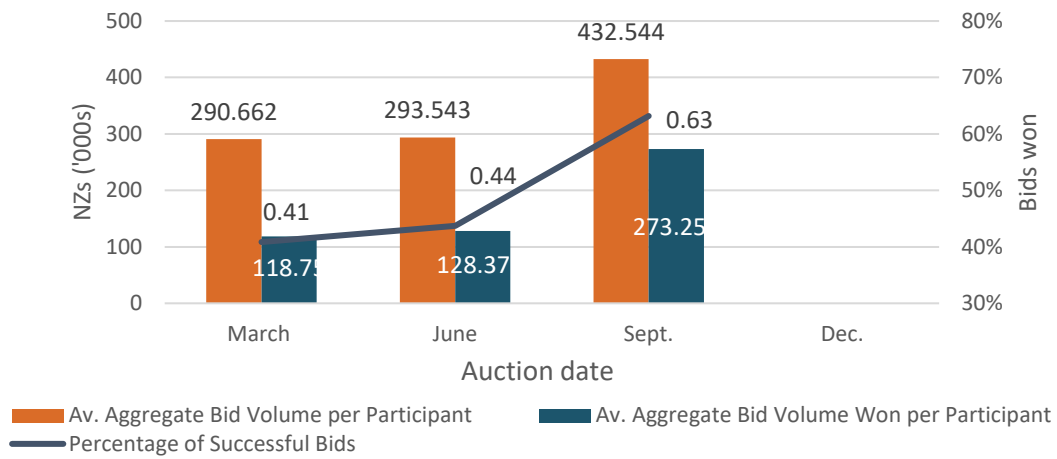


Figure A.4: Bid volume (of thousands of NZUs) per participant and 'win' ratio



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, September 2021

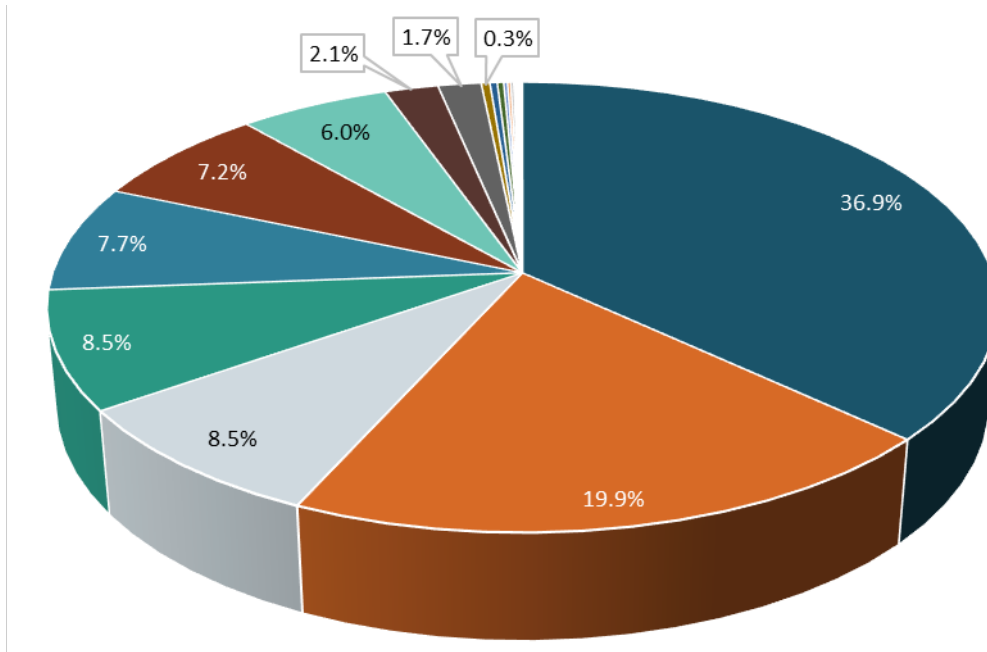


Figure A.6: Breakdown of aggregated successful bids by 'Top 10' participants 2021

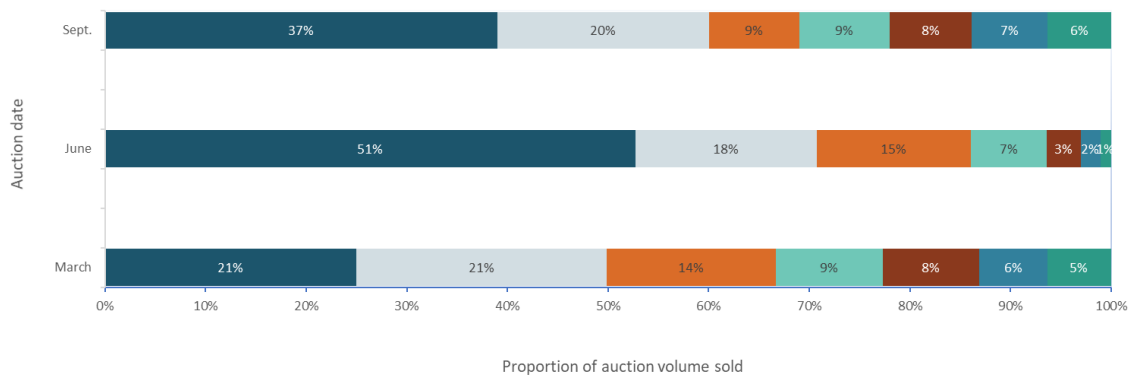
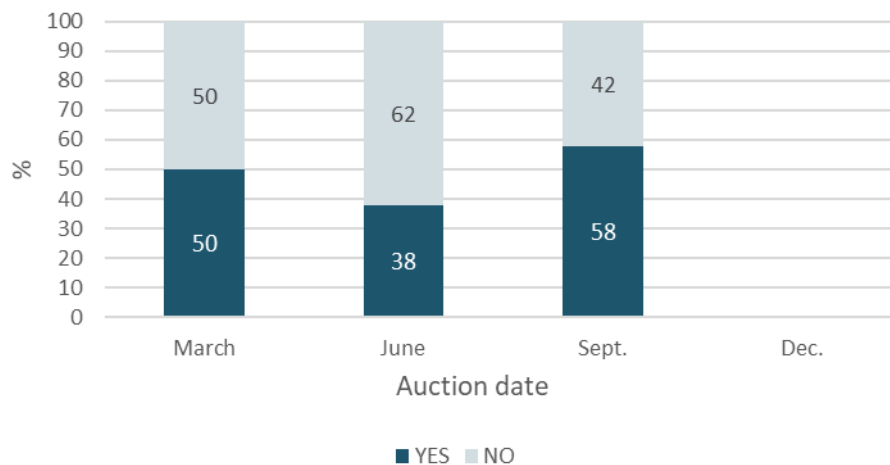


Figure A.7: Proportion of Participants with mandatory compliance obligations under the NZ ETS



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