



PROACTIVE RELEASE COVERSHEET

Minister	Hon Simon Watts	Portfolio	Climate Change
Name of package	Proactive release: Update to NZAS allocative baseline Cabinet paper and associated briefing notes	Date to be published	6 August 2024

List of documents that have been proactively released		
<i>Date</i>	<i>Title</i>	<i>Author</i>
6 August 2024	<ol style="list-style-type: none"> BRF-3944 Approval to issue call for data notice to NZAS Ltd. BRF-4093 Approval to issue drafting instructions for the annual update to the allocative baseline for NZAS BRF-4226: Approval to lodge: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 CAB-381 - Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 	Ministry for the Environment
<p>Information redacted YES / NO</p> <p>Any information redacted in the documents is redacted in accordance with the Ministry for the Environment's policy on proactive release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.</p> <p>No information has been redacted in the document "BRF-4226: Approval to lodge: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024".</p> <p>Summary of reasons for redaction</p> <p>Some information has been withheld for the reasons of maintaining legal professional privilege.</p>		

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Briefing: Approval to issue call for data notice to New Zealand Aluminium Smelters Limited

Date submitted: 14 December

Tracking number: BRF-3944

Security level: Policy and Privacy in Confidence

MfE priority: Urgent

Actions sought from Ministers		
Name and position	Action sought	Response by
To Hon Simon Watts Minister of Climate Change	Approve the publication of the attached Gazette notice	19 December
Cc Hon Nicola Willis Associate Minister of Climate Change	For information.	N/A

Actions for Minister's office staff
Forward this briefing to Minister Nicola Willis, Associate Minister of Climate Change. Return the signed briefing to the Ministry for the Environment (ministerials@mfe.govt.nz).

Appendices and attachments
1. Draft Gazette notice: Call for the Provision of Electricity Contract Related Information (Aluminium Smelting) Notice 2023

Key contacts at Ministry for the Environment			
Position	Name	Cell phone	First contact
Principal Author	Elliot Dunn		
Responsible Manager	Kate Whitwell	9(2)(a)	✓
General Manager	Melody Guy		

Minister's comments

Approval to issue call for data notice to New Zealand Aluminium Smelters Limited

Key messages

1. This briefing seeks your approval to publish the attached Gazette notice on 21 December 2023. The notice requests electricity contract related information from New Zealand Aluminium Smelters Limited (NZAS).
2. This information is needed as part of a routine annual regulatory process to update NZAS' final and provisional allocative baselines. The baselines are used to calculate NZAS' final and provisional (free) allocations of New Zealand Units provided via the New Zealand Emissions Trading Scheme (NZ ETS).
3. The update to NZAS' allocative baseline ensures that the amount of industrial allocation it receives reflects the actual emissions costs from its operation by taking into account electricity purchased through its contract with Meridian Energy Limited (Meridian).
4. NZAS must apply for its allocation by 30 April 2024 as required by the Climate Change Response Act 2002 (the Act). We need to issue the Gazette notice now so that the amendments to the Climate Change (Eligible Industrial Activities) Regulations 2010 (the Regulations) can be made ahead of this deadline (pending Cabinet approval).
5. If amendments are not made before 30 April 2024, it is estimated that NZAS' allocation would increase by 2.37 million NZUs which at current prices¹ is worth approximately \$170 million² to the Crown.
6. A separate piece of work is currently underway to update allocative baselines for all 26 eligible activities in 2024, including NZAS'. Additionally, any new electricity contract between NZAS and Meridian will prompt us to review and update estimates of emissions costs in future electricity purchases, which could also result in adjustment to NZAS' allocative baseline.

Recommendations

We recommend that you:

¹ \$71.90 as of 13 December 2023

² NZAS's allocation will be approximately 605,000 NZUs (\$40 million) with updates to its allocative baseline.

- a. **note** that updating the allocative baseline for New Zealand Aluminium Smelters Limited (NZAS) will ensure that its 2023 final allocation accurately reflects the emissions costs it faces through the price it pays for its electricity.
- b. **note** that NZAS must submit its application for an allocation by 30 April 2024 as required by the Climate Change Response Act 2002.
- c. **note** that without an update to its baseline, NZAS will receive approximately 2.37 million additional units valued at \$170 million at current prices.
- d. **note** that updates to all allocative baselines and a re-negotiated contract between NZAS and Meridian is likely to impact NZAS' baseline in 2024.
- e. **agree** to sign and publish the attached draft Gazette notice calling for electricity contract related information from NZAS by 21 December 2023.

Yes | No

Signatures



Melody Guy
General Manager
**Markets Unit, Climate Change Mitigation
& Resource Efficiency**
Date: 6 December 2023

Hon Simon Watts
Minister of Climate Change
Date:

Approval to issue call for data notice for New Zealand Aluminium Smelters Limited

Background

1. Industrial allocation is the provision of New Zealand Units (NZUs) to firms who carry out emissions-intensive³ and trade-exposed⁴ activities. This reduces the cost impact of the NZ ETS on those firms and the risk of emissions leakage.
2. The production of aluminium is an eligible industrial activity. New Zealand Aluminium Smelters Limited (NZAS) is therefore eligible to receive an industrial allocation. Historically, the majority of NZAS' emissions costs have been associated with its electricity use. However, as part of its main contract with Meridian which was renegotiated in 2021, it does not currently face emissions costs in the price it pays for the majority of its electricity.
3. The main NZ ETS cost impact on NZAS is due to direct onsite emissions from aluminium smelting as well as small amounts of natural gas and liquid fossil fuel use. NZAS also faces some emissions costs passed on for electricity purchased outside of its main electricity contract. These sources of NZ ETS costs are included in its allocative baseline.
4. The update to NZAS' allocative baseline is a routine regulatory process that has been carried out annually since 2010. The update ensures that NZAS' allocation reflects the actual emissions costs from its operation, which varies depending on how much electricity is consumed under its main contract with Meridian and how much is consumed outside that contract.

Analysis and advice

Allocation recipients receive a provisional allocation and an allocation adjustment

5. Allocation recipients receive an allocation of units in advance to cover their expected emissions costs for the current calendar year (ie, after applications close 30 April, a recipient receives its expected allocation for that entire calendar year based on its expected production). This is called a provisional allocation.
6. In this same application process, recipients have their provisional allocation from the previous calendar year 'trued-up' to take into account the final production that

³ A significant portion of their revenue is emissions costs that would be passed on to the consumer.

⁴ The activity is exposed to international trade.

occurred. This is called an allocation adjustment and determines the final allocation received for that previous calendar year.

NZAS' final allocation depends on its electricity consumption

7. NZAS is a special case because its annual emissions cost exposure is strongly coupled to its electricity purchases under its contract with Meridian. This electricity consumption changes from year to year, and hence its allocative baseline changes from year to year.
8. Therefore, NZAS' final allocation depends on both its final production and its final allocative baseline.

A Gazette notice must be issued to call for electricity contract related information to inform updates to the allocative baseline

9. The upcoming allocation applications are due by 30 April 2024.⁵ Updating NZAS' provisional 2023 allocative baseline to a final 2023 allocative baseline must be completed before this date to ensure that NZAS receives its correct allocation.
10. To do this we need to obtain information related to NZAS' purchases of electricity under their contract with Meridian for the 2023 calendar year. This is achieved through your issuing of a notice in the New Zealand Gazette that requests data on purchases of electricity under section 161D(1)(e)(ii) of the Act. A copy of the Gazette notice has been appended to this briefing.
11. Issuing the notice in the New Zealand Gazette in December will allow NZAS enough time to provide its 2023 electricity usage early in the new year. This means an update to its allocative baseline can be made ahead of the 30 April 2024 deadline (subject to Cabinet agreement).
12. The update to the allocative baselines involves finalising the baseline for the previous year in line with the actual emissions costs faced by NZAS for that year and updating the provisional baseline for future years.
13. Updates will:

- Finalise the baseline for 2023.
- Update the provisional baseline for 2024.
- Set a new provisional baseline for 2025.

Additional matters that will affect NZAS' allocative baseline in 2024

14. The electricity contract between NZAS and Meridian has a termination date in late 2024. Should a new contract be agreed, we will initiate a review to determine

⁵ The Act does not allow applications to be accepted after this date.

the emissions costs faced by NZAS in the new strike price for electricity purchases.

15. Officials will provide advice on this when more information is available. A first step will be to seek your approval to call for a complete copy of the new contract.
16. The Ministry is currently undertaking a data collection involving firms who are carrying out activities that are eligible for industrial allocation. This is part of the process to implement the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Act that was passed earlier in 2023. The data collection will close on 15 December and decisions from Cabinet will be sought in April/May next year.
17. The data collected will inform updates to the allocative baselines across all eligible activities including aluminium smelting and this is likely to impact NZAS' final 2024 allocations.

Te Tiriti analysis

18. No Tiriti issues are associated with the proposals in this briefing.

Other considerations

Consultation and engagement

19. We will engage with NZAS as part of the process to update its baselines.
20. Officials will contact NZAS to notify them of the upcoming Gazette notice ahead of its publication. NZAS will be anticipating this as part of the routine annual update.

Risks and mitigations

21. There is a timing risk associated with this work. NZAS must submit its emissions returns report to the Environmental Protection Authority (EPA) before 30 April 2024 as required by the Act. Updates to NZAS' allocative baseline need to occur before this date so its previous year's allocation can be adjusted, and it can receive its correct provisional allocation for 2024.
22. If NZAS' 2023 provisional allocative baseline is not updated to a 2023 final allocative baseline this year, then the baseline used for NZAS' final allocation for 2023 would default to the prescribed 2010 baseline of 10.1304 in Schedule 2 of the Regulations. This baseline does not factor in NZAS' electricity contract and assumes a higher level of exposure to the emissions price through electricity purchases.

23. If updates to the baseline are made, NZAS will receive an estimated allocation of 594,000 NZUs. This will cost the Crown \$43 million at current NZU prices⁶. In contrast, if no updates are made to the baseline, NZAS will receive an estimated additional 2.37 million units⁷. This will cost the Crown approximately \$170 million at current prices.
24. The amendment regulations will require approval from Cabinet. Publishing the Gazette notice on 21 December allows time for the updates to be drafted and approval to be sought from Cabinet before 30 April 2024.

Legal issues

25. ^{9(2)(h)}

26.

Financial, regulatory and legislative implications

27. Updates to the allocative baselines for NZAS will require updates to the Regulations. These updates require Cabinet approval.
28. Once the new regulations have been drafted you will be provided with a draft Cabinet paper for review and approval ahead of Cabinet Committee.
29. The cost to the Crown of issuing units to NZAS following updates to the baseline is an estimated \$44 million. In contrast, if no updates are made NZAS' allocation will cost the Crown an estimated \$174 million.

Next steps

30. The Gazette notice will be published on 21 December, pending your approval.
31. Section 161D(4) of the Act requires the Gazette notice to be presented to the House of Representatives no later than 16 sitting days after publication in the NZ Gazette.
32. Cabinet has delegated to you, as Minister of Climate Change, the authority to issue drafting instructions for changes to NZAS' allocative baseline [ENV-18-

⁶ \$71.90 as of December 2023

⁷ This is approximate and assumes NZAS's production for 2023 is the same as its 2022 production.

MIN-0051 refers]. Once the allocative baseline is calculated following provision of the information from NZAS, we will provide you with further advice and seek your approval to issue drafting instructions to the Parliamentary Counsel Office for the amendment Regulations.

33. Following this we will provide you with a draft Cabinet paper for your feedback and request approval to circulate it for Ministerial consultation.
34. The draft amendment regulations will need to be considered by the Cabinet Legislation Committee early next year prior to submission to Executive Council and publication. The table below sets out the proposed timeline for this work.

Proposed timeline

Task	Date
Publish Gazette notice calling for data from NZAS	21 December 2023
Present Gazette notice to House of Representatives	Early February 2024
Calculate new allocative baselines	Early February 2024
Instruct the PCO to draft regulations	Early February 2024
Circulate draft LEG paper for Ministerial consultation	Early March 2024
Lodge LEG paper	Mid - March 2024
LEG considers regulations	Mid - Late March 2024
Cabinet and Executive Council	Late March 2024
Notification of amendment regulations in the NZ Gazette	Week of 29 March 2024
NZAS applies to EPA for its allocation of NZUs using new allocative baselines	By 30 April 2024

Approval to lodge: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Date submitted: 7 March

Tracking number: BRF-4226

Security level: Policy and Privacy [In-Confidence]

MfE priority: Urgent

Actions sought from Ministers		
Name and position	Action sought	Response by
To Hon Simon WATTS Minister of Climate Change	Approve lodgement of the attached Cabinet paper on 14 March Agree to allow officials to make minor editorial changes to the Cabinet paper prior to lodgement.	11 March
CC Hon Nicola WILLIS Associate Minister of Climate Change	N/A	N/A

Actions for Minister's office staff

Return the signed briefing to the Ministry for the Environment (ministerials@mfe.govt.nz).

Appendices and attachments

- Draft Cabinet paper: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024
- Draft Emissions Trading Scheme Climate Change (Eligible Industrial Activities) Amendment Regulations 2024
- Next steps timeline

Key contacts at Ministry for the Environment

Position	Name	Cell phone	First contact
Principal Author	Elliot Dunn		
Responsible Manager	Kate Whitwell		✓
General Manager	Mark Vink		

Minister's comments

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Approval to lodge: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Request for approval to lodge Cabinet paper

1. This briefing seeks your approval to lodge the attached Cabinet paper: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 (Appendix 1) on the 14 March for consideration at the Cabinet Legislation Committee (LEG) meeting on 21 March 2024.
2. On 19 February you approved the issuing of drafting instructions for the annual update to allocative baselines used to calculate industrial allocation for aluminium smelting by NZAS [BRF-4093 refers].
3. Cabinet approval to authorise the submission of the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 to the Executive Council is needed.
4. These regulations will update the allocative baselines used in calculating industrial allocation for the New Zealand Aluminium Smelter Limited (NZAS).
5. The Parliamentary Council Office (PCO) has completed the drafting of the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 (appendix 2). These will be lodged by PCO on 14 March for consideration at Cabinet Legislation Committee on 21 March. Talking points will be provided next week.
6. These regulations need to be in force by early April 2024 to enable NZAS to apply for its industrial allocation by the 30 April deadline using accurate allocative baselines.
7. Ministerial consultation commenced on 27 February and will run until 11 March. No feedback has been received to date but any feedback we do receive will be addressed in the Cabinet paper and forwarded to your office for approval prior to lodgement.
8. The Ministry of Business Innovation and Employment, Ministry of Primary Industries, and the Treasury were consulted on the Cabinet paper. The Environmental Protection Authority and Department of the Prime Minister and Cabinet were informed. There have been minor updates to the Cabinet paper to incorporate agency feedback.
9. NZAS has been consulted on the updates to the allocative baselines and agrees with them. NZAS will be advised of the expected Gazettal date once Cabinet has agreed to the regulations.

10. These regulations need to be in force by early April 2024 to enable NZAS to apply for its industrial allocation before the 30 April deadline using accurate allocative baselines.
11. The amendment regulations will amend the Climate Change (Eligible Industrial Activities) Regulations 2010.

Recommendations

We recommend that you:

- a. **Note** that on 19 February you approved issuing drafting instructions to Parliamentary Counsel Office to update allocative baselines for aluminium smelting by NZAS in the Climate Change (Eligible Industrial Activities) Regulations 2010.
- b. **Note** that the Parliamentary Council Office has completed the drafting of the amendment regulations and these need to be made before the end of March 2024 to ensure that NZAS can apply for its correct allocation.
- c. **Note** that feedback from Ministerial consultation will be addressed in the paper and forwarded to your office prior to lodgement.
- d. **Agree** to allow officials to make minor editorial changes to the Cabinet paper prior to lodgement.

Yes | ~~No~~

- e. **Approve** lodgement of the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 Cabinet paper on 14 March subject to incorporation of feedback from Ministerial consultation.

Yes | ~~No~~

- f. **Note** that we will provide you with talking points next week to take to Cabinet Legislation Committee.

Signatures



Mark Vink

General Manager

**Markets Unit, Climate Change Mitigation
and Resource Efficiency**

6 March

Signed: SG Watts (electronic)

Hon Simon WATTS
Minister of Climate Change

Date 10/3/2024

Appendices

Appendix 1: Draft Cabinet paper: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Appendix 2: Draft Emissions Trading Scheme Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Appendix 3: Next steps timeline

Task	Date
Lodge LEG paper	14 March
LEG considers regulations	21 March
Cabinet and Executive Council	25 March
Notification of amendment regulations in the NZ Gazette	Week of 25 March
NZAS applies to EPA for its allocation of NZUs using new allocative baselines	By 30 April 2024

Policy and Privacy

In-Confidence

Office of the Minister of Climate Change

LEG - Cabinet Legislation Committee

Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Proposal

- 1 I propose the Cabinet Legislation Committee (LEG) authorise submission of the attached Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 to the Executive Council.
- 2 The amendment regulations prescribe the New Zealand Aluminium Smelters Limited final allocative baseline for 2023 and provisional allocative baselines for 2024 and 2025 under the New Zealand Emissions Trading Scheme (NZ ETS).

Relation to government priorities

- 3 This is a routine operational adjustment that requires Cabinet approval.

Executive Summary

- 4 The NZ ETS prices emissions across the economy, with emitters surrendering an emissions unit (New Zealand Unit or NZU) for every tonne of emissions. Some industries are more impacted by the NZ ETS where they have high levels of emissions costs compared to revenue and operate in international markets (referred to as emissions intensive and trade exposed industries, or EITE).
- 5 The Government provides allocations¹ of New Zealand Units (NZUs) to EITEs to help meet some of their emissions costs. Free allocation mitigates the risk that EITE industries shift offshore to countries with weaker climate policy to reduce compliance costs. This is known as emissions leakage and could result in global emissions increasing.
- 6 The New Zealand Aluminium Smelters Limited (NZAS) receives an allocation of units annually for carrying out the EITE activity – aluminium smelting.
- 7 NZAS has unique electricity pricing arrangements and significant electricity use. There is an annual process for updating NZAS' allocative baseline² in regulations to

¹ Industrial allocation policy is legislated under the Climate Change Response Act 2002 (CCRA) and the Climate Change (Eligible Industrial Activities) Regulations 2010 (the Regulations).

² An allocative baseline is the rate at which an EITE activity receives an allocation of units. It can be expressed as NZUs per tonne of output produced. Firms carrying out an eligible activity receive a provisional allocation in advance based on forecast levels of output for the upcoming year. The allocation is corrected a year later once actual output levels are confirmed.

IN CONFIDENCE

account for this. This process has been carried out since 2010 and ensures that NZAS' annual allocation fairly reflects the emissions costs it faces.

- 8 Based on electricity data recently provided by NZAS, the proposed final allocative baseline for 2023 and the provisional allocative baselines for 2024 and 2025 is 2.042. This is a minor increase from the provisional allocative baseline for 2023.
- 9 If NZAS' 2023 provisional allocative baseline is not updated to a final allocative baseline this year, then the baseline used in NZAS' 2023 allocation correction would default to a much higher baseline of 10.1304 in Schedule 2 of the Regulations. This baseline does not factor in NZAS' current electricity contract and assumes a higher exposure to the emissions price through electricity purchases.
- 10 Updating the baseline now means that NZAS will receive an estimated provisional allocation of 586,316 units which account for on-site emissions attributed to the transformation of aluminium oxide to aluminium and other minor emissions sources. This will cost the Crown \$42.8 million at current NZU prices.
- 11 In contrast, if no updates are made to the baseline, NZAS would receive an estimated 2.9 million units. This would cost the Crown approximately \$212 million at current prices.
- 12 NZAS has been consulted on the changes to the regulations and has agreed with the calculation of the updated allocative baseline for aluminium smelting.
- 13 The amendment regulations need to be notified in the New Zealand Gazette by 2 April 2024 to allow them to come into effect following the 28-day notification period and for NZAS to meet the 30 April deadline for allocation applications.
- 14 There will be another update to NZAS' allocative baseline in 2024. This will roll together an update to account for new production, emissions and revenue data as part of the work to implement the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Act 2023, and an update to the electricity allocation factor as part of a new annual process, . The impact of these future updates is expected to be more significant than the baseline adjustment in this paper. I will seek Cabinet's approval for amendment regulations before November 2024.

Background

- 15 Several regulatory changes are required each year to keep the NZ ETS operating effectively and efficiently.
- 16 Aluminium smelting is an emissions intensive activity and aluminium is traded internationally so is an eligible EITE activity under the CCRA and the Regulations.
- 17 NZAS is entitled to receive industrial allocation of New Zealand Units (NZUs) to offset the costs of the NZ ETS.
- 18 NZAS' allocation covers the emissions costs associated with direct emissions from the transformation of aluminium oxide to aluminium, a small amount of Liquefied Petroleum Gas (LPG), and the indirect emissions cost of electricity purchases.
- 19 Section 161C(4) of the CCRA grants the Minister of Climate Change powers to adjust allocation calculations to take account of electricity-related contracts. NZAS is

currently the only recipient of industrial allocation with adjusted calculations for contracts.

- 20 NZAS has a special process for allocation because of its significant electricity use and because of the nature of its electricity supply contract with Meridian. Other EITE firms buy electricity at or near spot prices and receive NZUs to cover costs passed through for electricity generation emissions at a standard rate. NZAS receives a lower, and variable, amount of NZUs because its exposure to spot market electricity costs is limited and changes annually.
- 21 Previous analysis of its current electricity contract with Meridian has shown that NZAS faces no NZ ETS cost component through the price it pays for electricity under this contract. This has resulted in NZAS' allocative baseline being reflective of predominately process emissions with some emissions costs from liquid fossil fuel and gas usage.
- 22 Allocations to NZAS are based on three variables: the production of aluminium, the emissions intensity (the allocative baseline), and the assistance rate applicable to highly emissions intensive industries. The respective assistance rate is 0.86 for 2024 and is being phased down by 1 percentage point per year this decade.
- 23 NZAS' allocative baselines for the previous and current years are adjusted every year according to how much electricity NZAS consumed in the previous year under its contracts and from the spot market. A provisional allocative baseline is also created for the next year to assist NZAS and the Government with forecasting. This annual operational and technical update protects the Crown from over-allocating or under-allocating NZUs to NZAS.

Analysis

NZAS allocative baseline update

- 24 Cabinet has previously authorised the Minister of Climate Change to adjust NZAS' allocative baseline to reflect the NZ ETS costs from electricity consumption without referring to Cabinet, except where financial or policy implications are significant enough to warrant Cabinet consideration [ENV-18-MIN-0051 and CAB-18-MIN-0628].
- 25 I used this delegation to approve drafting instructions for the amendment regulations, which are detailed in the following table.³ Once regulations are drafted, Cabinet approval is required to submit the regulations to the Executive Council.

Year	Current Allocative Baselines (NZUs/tonne of product)	Proposed Allocative Baselines (NZUs/tonne of product)
2023	2.034 (provisional)	2.042 (final)
2024	2.034 (provisional)	2.042 (provisional)
2025	Not set	2.042 (provisional)

- 26 Updates to the final and provisional baselines are based on electricity consumption data provided by NZAS.

³ Updates are proposed for years 2023-2025 only. Prior years are provided to illustrate the change in allocative baseline resulting from decisions in relation to NZAS' main electricity contract.

- 27 The final 2023 allocative baseline is higher than was set provisionally because NZAS purchased marginally more electricity from the spot market than in 2022⁴.
- 28 Updates to the provisional baselines for 2024 and 2025 are based on NZAS' 2023 consumption data which they noted as a reasonable forecast of their electricity purchases.

Amendments avoid under- or over-allocation of emission units to NZAS

- 29 If NZAS' 2023 provisional allocative baseline is not updated to a final allocative baseline this year, then the baseline used in NZAS' 2023 allocation correction would default to a much higher baseline of 10.1304 in Schedule 2 of the Climate Change (Eligible Industrial Activities) Regulations 2010. This baseline does not factor in NZAS' electricity contract and assumes a higher exposure to the emissions price through electricity purchases.
- 30 Updating the allocative baselines now means that NZAS will receive an estimated provisional allocation of 586,316 units which account for on-site emissions attributed to the transformation of aluminium oxide to aluminium and other minor emissions sources. This will cost the Crown \$41 million at an NZU price of \$70. In contrast, if no updates are made to the baseline, NZAS would receive an estimated 2.9 million units, costing the Crown approximately \$203 million.
- 31 My recommended updates to the allocative baselines for aluminium smelting are based on evidence of the emissions costs faced by NZAS under their existing contract. They are consistent with the purpose of industrial allocation policy and the statutory objectives of the NZ ETS. The application of existing methodologies and processes provides for market confidence in decision making on the NZ ETS.

Legal advice (legally privileged)

- 32 9(2)(h)
- 

Additional matters that will affect future updates to NZAS' allocative baselines

Implementation of the industrial allocation amendment act

- 33 Work on implementing the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Act 2023 is currently underway. As part of this process, new data on direct and indirect emissions per tonnes of aluminium produced has been sourced from NZAS. This may result in further changes to NZAS' allocative baseline in 2024. These changes will impact NZAS' final allocation for 2024 and provisional allocation for 2025 onwards. Cabinet decisions on changes to the baseline will be sought later this year.

⁴ The provisional baseline is based on confirmed electricity usage from the previous calendar year.

A new process for annual updates to the electricity allocation factor

- 34 The Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Act 2023 established a new annual process for updating the electricity allocation factor (EAF). The EAF is used to estimate the indirect emission costs associated with purchasing electricity from the spot market. The first update to the EAF will be carried out later in 2024 and will have an impact on NZAS' final allocative baseline for 2024 and provisional allocative baseline for 2025 as it purchases a small amount of electricity outside of its contract with Meridian..

A renegotiated electricity supply contract

- 35 The electricity supply contract between NZAS and Meridian Energy Limited is being renegotiated. The indirect emissions costs faced by NZAS under any new contract will be studied by my officials once the contract is finalised. I will then seek Cabinet approval to reflect any new emission costs in NZAS's allocations from 2025.

Timing and 28-Day rule

- 36 It is intended that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 come into force 28 days after the date of their notification in the New Zealand Gazette. The amendment regulations need to be in force to allow sufficient time for NZAS to meet the 30 April 2024 deadline for allocation applications.
- 37 Consideration of this paper at the 21 March LEG Committee meeting means that no waiver from the 28-day rule is required.

Cost-of-living Implications

- 38 No cost-of-living implications have been identified as a result of these amendments.

Financial Implications

- 39 This update has resulted in an increase to NZAS' allocative baseline. However, due to production figures lower than what was forecast for 2023⁵, the update will result in NZAS owing the Crown an estimated 1,217 New Zealand Units (approximately \$85,000 at a price of \$70 per NZU).
- 40 Further to this, updating the allocative baselines now prevents the allocative baseline for aluminium smelting reverting to the default baseline of 10.1304 prescribed in Schedule 2 of the regulations. This avoids a significant over-allocation of NZUs to NZAS at an additional cost to the Crown of approximately \$164.5 million at an NZU price of \$70.

Compliance

- 41 The regulations comply with each of the following:
- 41.1 the principles of the Treaty of Waitangi;
 - 41.2 the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 or the Human Rights Act 1993;

⁵ NZAS' unaudited final production of 333,870t of aluminium

- 41.3 the principles and guidelines set out in the Privacy Act 2020;
 - 41.4 relevant international standards and obligations;
 - 41.5 the Legislation Guidelines (2021 edition), which are maintained by the Legislation Design and Advisory Committee.
- 42 The Minister of Climate Change may recommend the making of regulations under s 161A(1)(c) of the Climate Change Response Act 2002 to prescribe allocative baselines. In accordance with s 161C(4) of the Act, the Minister may adjust a specified emissions figure (and consequently, their allocative baseline) after taking into account certain electricity-related contracts. No specific statutory prerequisite exists for the making of regulations under s 161A(1)(c). However, s 3(2) of the Act requires persons exercising a power or discretion under the Act to do so in a manner that is consistent with the purpose of the Act. This requirement has been met.

Regulations Review Committee

- 43 No grounds have been identified for the Regulations Review Committee to draw the disallowable instrument or regulations to the attention of the House of Representatives as a Standing Order requirement.

Certification by Parliamentary Counsel

- 44 The draft regulations were certified by the Parliamentary Counsel Office (PCO) as being in order for submission to Cabinet.

Legislative Implications

- 45 Regulatory amendments to the Climate Change (Eligible Industrial Activities) Regulations 2010 will be required to implement the proposed changes.

Impact Analysis

Regulatory Impact Statement

- 46 Cabinet has previously agreed that no Regulatory Impact Analysis will be required to accompany the annual legislative proposals containing updates to NZAS' baselines in the amended regulations [CAB Min (12) 43/6 refers]. A Regulatory Impact Analysis completed in June 2010⁶ informed the decision to annually update NZAS' allocative baselines.

Climate Implications of Policy Assessment

- 47 The Climate Implications of Policy Assessment (CIPA) team at the Ministry has been consulted. They confirmed the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

Population Implications

- 48 The proposed amendments have no population implications.

⁶ As published on the Treasury's website: [New Zealand Emissions Trading Scheme: Industrial Allocation - 29 June 2010 - Regulatory Impact Statement - Ministry for the Environment \(treasury.govt.nz\)](#)

Human Rights

- 49 There are no inconsistencies between the proposed amendments with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Use of external Resources

- 50 No external resources were engaged in the preparation of the policy advice in this paper.

Consultation

- 51 There are no statutory consultation requirements for these regulations in the CCRA. In line with Cabinet Manual requirements, NZAS was consulted about, and agreed with, the calculation of the baselines in the proposed amendment regulations.
- 52 The Treasury, Ministry for Primary Industries, and Ministry of Business, Innovation and Employment were consulted on this paper. The Department of Prime Minister and Cabinet and the Environmental Protection Authority were informed. Where specific comments were provided, they are reflected in this paper.

Communications

- 53 NZAS and the Environmental Protection Authority will be notified when the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 are notified in the New Zealand Gazette. No other parties are affected.

Publicity

- 54 The amended regulations will be notified in the New Zealand Gazette and published on the NZ Legislation website following Cabinet approval.

Proactive Release

- 55 I propose to proactively release this paper on the Ministry for the Environment's website in full, subject to redactions equivalent to those under the Official Information Act 1982, once amendment regulations are published.

Recommendations

I recommend that the Cabinet Legislation Committee:

- 1 **Note** that Cabinet has previously authorised the Minister of Climate Change to make adjustments to the allocation level for New Zealand Aluminium Smelter Limited (NZAS) to reflect the New Zealand Emissions Trading Scheme (NZ ETS) costs to NZAS from electricity consumption without referring to Cabinet, except where the financial or policy implications are significant enough to warrant Cabinet consideration [ENV-18-MIN-0051 and CAB-18-MIN-0628]
- 2 **Note** that I have determined recommended adjustments to the allocation level for NZAS, based on evidence of emission cost pass through, consistent with the purpose of industrial allocation policy and the statutory objectives of the NZ ETS.
- 3 **Note** that NZAS has been consulted on the proposed adjustment to its allocation level and agrees with the adjustment.

IN CONFIDENCE

- 4 **Note** that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 will give effect to the decisions referred to in recommendation 2 above.
- 5 **Note** that these amendments need to come into effect before the 30 April 2024 so that NZAS can apply for its NZ ETS allocation under the industrial allocation provisions of the Climate Change Response Act 2002 by this deadline
- 6 **Authorise** the submission to the Executive Council of the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024
- 7 **Note** that it is intended that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2024 come into force 28 days after the date of their notification in the New Zealand Gazette.

Authorised for lodgement

Hon Simon Watts

Minister of Climate Change

Appendices

Appendix 1: Emissions Trading Scheme Climate Change (Eligible Industrial Activities) Amendment Regulations 2023



Briefing: Approval to issue drafting instructions for the annual update to the allocative baseline for NZAS

Date submitted: 15 February

Tracking number: BRF-4093

Security level: Policy and Privacy [In-Confidence]

MfE priority: Urgent

Actions sought from Ministers		
Name and position	Action sought	Response by
To Hon Simon WATTS Minister of Climate Change	<p>Agree to issue drafting instructions to the Parliamentary Counsel Office to update the New Zealand Aluminium Smelter's allocative baseline.</p> <p>Provide feedback on draft Cabinet paper.</p> <p>Agree to shorten Ministerial consultation to 5 working days.</p>	19 February
CC Hon Nicola WILLIS Associate Minister of Climate Change	N/A	N/A

Actions for Minister's office staff
Return the signed briefing to the Ministry for the Environment (ministerials@mfe.govt.nz).

Appendices and attachments
1. Draft Cabinet paper: Climate Change (Eligible Industrial Activities) Amendment Regulations 2024

Key contacts at Ministry for the Environment			
Position	Name	Cell phone	First contact
Principal Author	Elliot Dunn		
Responsible Manager	Kate Whitwell	0221375939	✓
General Manager (Acting)	Susan Baas		

Minister's comments

Approval to issue drafting instructions for the annual update to the allocative baseline for NZAS

Key messages

1. This paper seeks your approval to instruct the Parliamentary Counsel Office (PCO) to draft amendment regulations for the Climate Change (Eligible Industrial Activities) Regulations 2010 to update the allocative baseline for New Zealand Aluminium Smelters Ltd (NZAS). Officials are also seeking your feedback on the draft Cabinet paper seeking Cabinet agreement to these amendment regulations.
2. To ensure that the amendment regulations are published in time for NZAS to apply for its allocation by 30 April, we seek your approval for a shortened Ministerial consultation timeframe of 5 working days for the Cabinet paper. If a full 10 days' Ministerial consultation is required, officials recommend that the Cabinet paper request a waiver of the 28-day rule for regulations to come into effect.
3. This is a routine, annual process. Aluminium smelting has a special allocation process because of the electricity pricing arrangements NZAS has with Meridian. Each year a notice is issued to NZAS seeking electricity consumption data which is used to calculate an updated allocative baseline. This annual update ensures emissions costs are accurately reflected in the allocation it receives.
4. Based on the data recently provided by NZAS, the proposed final allocative baseline for 2023 and provisional allocative baselines for 2024 and 2025 is 2.042. This is a minor increase from the provisional allocative baseline for 2023.
5. Based on confirmed 2023 production data and the updated baseline, the change results in NZAS needing to pay back approximately 1217 emission units (NZUs) to the Crown of the 594,000 NZU provisional allocation it received last year.

Recommendations

We recommend that you:

- a. **Note** that the amendments proposed in the draft Cabinet paper finalise the 2023 allocative baseline, update the 2024 provisional allocative baseline, and create a 2025 provisional allocative baseline.
- b. **Agree** to instruct Parliamentary Counsel Office to draft amendments to the Climate Change (Eligible Industrial Activities) Regulations 2010 to prescribe the final allocative baseline for 2023 as 2.042 and the provisional allocative baselines for 2024 and 2025 as 2.042 for aluminium smelting by NZAS.

Yes | No

- c. **Provide** feedback on the draft Cabinet paper seeking authorisation from Cabinet to amend the Climate Change (Eligible Industrial Activities) Regulations 2010.
- d. **Note** that amendments to the regulations must be finalised and published in the New Zealand Gazette in time for NZAS to apply for its allocation on 30 April.
- e. **Agree to:**
- a. **Either** shorten Ministerial consultation to 5 working days to accommodate this timeline.

Yes | No

- b. **Or** request from Cabinet a waiver of the 28-day rule.

Yes | No

Signatures

Susan Baas
 General Manager – Markets (Acting)
Climate Change Mitigation and Resource Efficiency
13 February



Hon Simon WATTS
Minister of Climate Change

Date

Approval to issue drafting instructions for the annual update to the allocative baseline for NZAS

Purpose

1. This paper seeks your approval to issue drafting instructions to PCO to draft amendments to the Climate Change (Eligible Industrial Activities) Regulations 2010 to update the aluminium smelting allocative baseline that applies to NZAS.
2. Officials are also seeking your feedback on the draft Cabinet paper to approve those amendment regulations (Appendix). Your agreement is also sought to a shortened Ministerial consultation period of 5 working days.

Background

3. NZAS is a mandatory participant in the NZ ETS for the activity of aluminium smelting and is required to surrender NZUs to the Crown each year for its process emissions. It also faces a small amount of indirect emissions costs from liquified petroleum gas (LPG) and electricity purchases from the spot market.
4. NZAS receives industrial allocation to cover a portion of these emissions costs as it is emissions intensive and trade exposed. NZAS has a special allocation process because of its significant electricity use and because of the electricity pricing arrangements it has with Meridian that limits its exposure to an emissions price.
5. Electricity purchased through its main contract with Meridian does not contain an emissions price, whereas electricity purchased from the spot market contains emission costs passed through from generators, currently estimated and expressed as 0.537 t CO₂-e/MWh.
6. NZAS' allocative baselines for the previous and current years are adjusted annually according to how much electricity NZAS consumed via its main contract and the spot market in the previous calendar year.
7. Cabinet has previously authorised the Minister of Climate Change to adjust NZAS' baselines to reflect its electricity purchases [ENV-18-MIN-0051 and CAB-18-MIN-0628 refers]. Amendment regulations still require Cabinet approval.

Analysis and advice

NZAS allocative baseline update

8. The proposed 2023 baseline amendment is based on actual 2023 electricity consumption data provided by NZAS (table below). The provisional baseline for

2024 and 2025 are set using the same 2023 data. This is usual practice until actual data is available in future years.

Year	Current Allocative Baselines (before change)	Proposed Allocative Baselines (with updates)
2023	2.034 (provisional)	2.042 (final)
2024	2.034 (provisional)	2.042 (provisional)
2025	Not set	2.042 (provisional)

9. The final 2023 allocative baseline is higher than was set provisionally because NZAS purchased marginally more electricity from the spot market than in 2022.
10. The impact of confirmed 2023 production data, and the amended allocative baseline will result in NZAS paying back approximately 1217 NZUs of the 594,000 it received last year for its 2023 provisional allocation. The EPA will deduct this amount from the 2024 provisional allocation NZAS will receive using the proposed 2024 provisional baseline.
11. NZAS' baselines will likely be updated again later this year due to the implementation of the industrial allocation reforms. Renegotiation of NZAS' main electricity contract may also have implications for its future allocation. We will discuss these with you when they arise.

Other considerations

Consultation and engagement

12. NZAS was informed of the proposed baselines and agreed with the calculations. Officials will contact NZAS to advise them of the expected publication date of the amended regulations once agreed to by Cabinet.
13. The draft Cabinet paper is currently out for agency consultation. We will communicate any feedback from this when we provide you a draft for Ministerial consultation.

Risks and mitigations

Timing

14. Your decision on issuing drafting instructions is needed now so that amendment regulations are published in time for NZAS to apply for its allocation by 30 April.
15. Due to the constrained timeline, officials are seeking your approval of a shortened Ministerial consultation period of 5 working days. If a full 10 days' Ministerial consultation is required, officials recommend that the Cabinet paper request a waiver of the 28-day rule for regulations to come into effect.

Legal issues

S9(2)(h)



Financial implications

18. A reduction of 1217 NZUs (~\$85k at a \$70 carbon price), is considered minor in contrast to the almost 600k NZUs NZAS receives annually (~\$42 mill). No changes are required to the appropriation for industrial allocation.

Next steps

19. Subject to your agreement, PCO will draft amendment regulations.
20. Pending your feedback, we will provide you with a final draft Cabinet paper on 29 February and seek approval to commence Ministerial consultation.

Timeline of key dates

Task	Date
Instruct the PCO to draft regulations	20 February
Circulate draft LEG paper for Ministerial consultation (5 working days)	5 March
Lodge LEG paper	14 March
LEG considers regulations	21 March
Cabinet and Executive Council	25 March
Notification of amendment regulations in the NZ Gazette	Week of 25 March
NZAS applies to EPA for its allocation of NZUs using new allocative baselines	By 30 April 2024

Appendices

Appendix: Draft Cabinet paper: Climate Change (Eligible Industrial Activities)
Amendment Regulations 2024