



Cabinet

Minute of Decision

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Review of the New Zealand Emissions Trading Scheme

Portfolio Climate Change

On 27 September 2022, following reference from the Cabinet Economic Development Committee, Cabinet:

Background

- 1 **noted** that in *Ināia tonu nei: a low emissions future for Aotearoa*, the Climate Change Commission (the Commission) recommended that the government amend the New Zealand Emissions Trading Scheme (NZ ETS) to strengthen incentives for gross emissions reductions and to manage the amount of exotic forest planting the scheme drives, in line with its advice on the emission reductions and removals needed to meet emissions budgets (recommendations 11.1 and 25.2a);
- 2 **noted** that in December 2021, Cabinet agreed to prioritise gross emissions reductions in the emissions reduction plan (ERP), alongside maintaining support for net emissions reductions, in line with the Commission's analysis and advice on emissions budgets [CAB-21-MIN-0547.02];
- 3 **noted** that in May 2022, as part of the ERP, Cabinet agreed in principle to the recommendations of the Commission to amend the NZ ETS to strengthen the incentives for gross emissions reductions and to manage the amount of exotic forests driven by the scheme, subject to the outcomes of a targeted review of the NZ ETS [CAB-22-MIN-0152];

Purpose of the review of the NZ ETS

- 4 **agreed** that the first phase of the review will consider what balance of gross and net emissions reductions should be incentivised through the NZ ETS, and will develop recommendations on a preferred balance of both gross emissions reductions and emissions removals required to meet the emissions budgets;
- 5 **agreed** that the second phase of the review will include proposals to amend the NZ ETS to drive gross and net emissions reductions in line with the government's preferred balance;
- 6 **agreed** that the other matters in-scope of the review, described in paragraphs 8.1 and 8.2 below, will be considered alongside the balance of emissions reductions incentivised by the NZ ETS in the first phase of the review;

Scope of the review

- 7 **agreed** the review of the NZ ETS should consider the following questions:
- 7.1 what balance of gross and net emissions reductions is expected to be driven by the current design and settings of the NZ ETS, and what are the economic, environmental, and distributional impacts of this balance;
 - 7.2 what balance of gross and net emissions reductions should the NZ ETS incentivise in the future;
 - 7.3 how could the NZ ETS be amended to support the government's preferred balance of gross and net emissions reductions;
 - 7.4 how would the balance of emissions reductions incentivised by the NZ ETS change over time;
 - 7.5 what are the potential impacts, trade-offs, and risks to society and the economy of the options for shifting the balance of gross and net emissions reductions;
 - 7.6 what are the options to amend the design and settings of the NZ ETS and strengthen incentives for gross emissions reductions;
 - 7.7 what levels of net emissions reductions should be from exotic forests and indigenous forests, and how to improve NZ ETS incentives for indigenous afforestation;
 - 7.8 what role does the NZ ETS currently play in meeting New Zealand's nationally determined contribution, and what role should it play in the future;
- 8 **agreed** that the following issues are also in-scope of the review:
- 8.1 how to include additional sources of emissions removals in the NZ ETS;
 - 8.2 the extent to which the design of the NZ ETS should support emissions reductions or a range of co-benefits;
- 9 **agreed** that the review will use the following high-level objectives for the NZ ETS to assess the outcomes of the review:
- 9.1 predictable – the NZ ETS plays a clear and central role in New Zealand's climate change response;
 - 9.2 stable – the NZ ETS price signal is stable and reflects the marginal costs of gross emissions reductions;
 - 9.3 effective – the NZ ETS drives a balance of gross and net emissions reductions in line with the Commission's demonstration pathway to meet the 2050 target, while supporting an equitable transition to a low-emissions economy;

Process for the review and next steps

- 10 **agreed** that the review be carried out by an inter-agency team of officials, beginning in September 2022 and concluding in June 2023;
- 11 **agreed** to the Governance Terms of Reference for the review, attached to the paper under CAB-22-SUB-0412, which have been endorsed by the Interdepartmental Executive Board;

- 12 **agreed** to a report back to Cabinet in December 2022, providing recommendations on a preferred balance of gross and net emissions reductions to be incentivised through the NZ ETS to contribute to New Zealand's domestic emissions budgets and nationally determined contributions;
- 13 **agreed** to a report back to Cabinet in the first quarter of 2023 seeking agreement to:
- 13.1 a package of proposals to amend the NZ ETS to drive gross and net emissions reductions in line with Cabinet's preferred balance;
- 13.2 publicly consult on this package in the second quarter of 2023;
- 14 **invited** the Minister of Climate Change, the Minister of Energy and Resources, the Minister for the Environment, and the Minister of Forestry to jointly report back in accordance with paragraphs 12 and 13 above, and to be responsible for the communications for the review;
- 15 **noted** that the Minister of Climate Change proposes to publicly consult on Cabinet's preferred proposals to prioritise gross emissions reductions in the NZ ETS in the second quarter of 2023, with a view to making final policy decisions by the end of the second quarter;
- 16 **noted** that Cabinet's preferred policy proposals can be progressed through changes to the Climate Change Response Act 2002 following the 2023 General Election;
- 17 **noted** that the proposed timeframes are ambitious but achievable, as the Commission has provided a strong foundation for officials to assess the balance of gross and net emissions reductions in the NZ ETS;
- 18 **noted** that this timing aligns with the Commission's recommendations to have developed and implemented proposals to strengthen the NZ ETS incentive for gross emissions reductions and manage the amount of exotic forest planting driven by the scheme by 31 December 2024;
- 19 **noted** that the review will be carried out in parallel with other climate work programmes, including changes to the permanent post-1989 forestry category, and that alignment between the work programmes is necessary;
- 20 **noted** that it will be critical to engage with Iwi/Māori throughout the review process, and that officials are exploring options to facilitate this and are developing an engagement plan;
- 21 **noted** that the Minister of Climate Change has consulted the Minister of Energy and Resources and the Minister of Forestry on the proposed scope of the review, as directed by Cabinet;
- 22 **agreed** to publicly announce the scope, process, and timing for the review following Cabinet's decisions on these matters.

Rachel Hayward
Acting Secretary of the Cabinet