



# Approval to lodge 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited' Cabinet paper

Date Submitted:	30 November 2021	Tracking #: BRF-824	
Security Level	Policy and Privacy In-Confidence	MfE Priority:	Not Urgent

	<b>Action sought:</b>	<b>Response by:</b>
Hon James SHAW, Minister of Climate Change	<ol style="list-style-type: none"> <li><b>Approve</b> lodgement of Cabinet paper</li> <li><b>Note</b> updated Cabinet paper as Appendix 1</li> <li><b>Note</b> Talking points attached as Appendix 2.</li> </ol>	2 December 2021

Actions for Minister's Office Staff	<b>Return</b> the signed report to MfE.
Number of appendices and attachments # 2	<p>Appendix 1: Cabinet paper 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited'</p> <p>Appendix 2: Talking points to 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited'</p>

## Key contacts

Position	Name	Cell phone	1st contact
Principal Author	Jill Fernandes		
Responsible Manager	James Coombes	s 9(2)(a)	✓
Director	Lisa Daniell		

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# Approval to lodge 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited' Cabinet paper

## Key Messages

1. This briefing seeks approval to lodge the '*Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited*' Cabinet paper for the Cabinet Environment, Energy and Climate Committee meeting on 9 December 2021.
2. Feedback was received from the Prime Minister's Office to reframe the paper in plain English and set out the process that led to requiring this Cabinet decision.
3. Feedback received from Ministerial consultation has been addressed in the paper. A clean version and track changes version is provided in Appendix 1.
4. Talking points are provided in Appendix 2 - *Talking points to 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited'*.
5. A decision on the electricity allocation factor (EAF) for the New Zealand Aluminium Smelter (NZAS) needs to be made at the Cabinet Environment, Energy and Climate Committee on 9 December 2021 so that NZAS's allocative baseline can be set in regulations. This would allow NZAS to apply for its final allocation within the statutory deadline of 30 April 2022.

## Recommendations

We recommend that you:


- a. **Note** the Cabinet paper '*Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited*' attached as Appendix 1 is amended based on feedback received from ministerial consultation.
- b. **Agree** to lodge the '*Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited*' Cabinet paper on 2 December 2021 for your Cabinet Environment, Energy and Climate Committee meeting on 9 December 2021.

Yes/No

- c. **Note** talking points attached as Appendix 2: *Talking points to 'Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited'*.
- d. **Agree** that this briefing and appendices will be released proactively on the Ministry for the Environment's website once the final policy decisions have been made and communicated to the New Zealand Aluminium Smelter Limited.

Yes/No

## Signature

Lisa Daniell Director - Climate Mitigation	s 9(2)(a) 
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Hon James SHAW, Minister of Climate Change	
[Date field]	

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## **Appendix 1: Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited**

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## Appendix 2: Talking points to ‘Setting an electricity allocation factor for the New Zealand Aluminium Smelters Limited’

### Purpose

1. This Cabinet paper seeks approval to set an electricity allocation factor (EAF) for the New Zealand Aluminium Smelters Limited (NZAS) for its emission unit allocation under the New Zealand Emissions Trading Scheme (NZ ETS).
2. The NZ ETS imposes costs on NZAS for its emissions from aluminium smelting and electricity. The estimated impact of the NZ ETS on electricity prices is described as the EAF.
3. NZAS receives an allocation to offset its NZ ETS costs under the industrial allocation policy. In 2020, NZAS was allocated 1.5 million units (NZUs) valued at \$97.5 million (\$65.00 per NZU as at 30 November 2021). The EAF value impacts only the electricity component of NZAS’s allocation.

### NZAS renegotiated its electricity contract and so the EAF needs to be updated

4. In January 2021, NZAS and Meridian agreed to a new electricity price and term for the main electricity contract.
5. In comparison to the previous 2015 contract, the renegotiated main contract is much shorter, significantly cheaper and the price is fixed for the duration of the contract.
6. Therefore, the EAF underlying the calculation for NZAS’s allocation needs to be updated so that it reflects the emissions costs from the renegotiated contract.

### Setting a new EAF for NZAS

7. Two EAF options were considered that reflect the NZ ETS costs incurred by NZAS for electricity use under the main contract. A modelled value – 0.0 tCO<sub>2</sub>-e/MWh and the status quo – 0.206 tCO<sub>2</sub>-e/MWh.
8. The modelled EAF value is the recommended option. The model is based on the impacts to the electricity market and on Meridian’s overall profitability if NZAS had closed in August 2021. The modelling demonstrated that emissions pricing had no impact on the price of the main contract.
9. Retaining the status quo option, would likely overcompensate NZAS for its NZ ETS costs and create unfair fiscal penalties for taxpayers.
10. I recommend setting NZAS’s EAF for the main contract at zero. This means there are no emissions costs passed on to NZAS under this contract. This will result in a reduction of approximately \$60 million in Crown expenditure.

11. If the preferred EAF option is approved, the next step will be amending Climate Change (Eligible Industrial Activities) Regulations 2010 in March 2022 so that NZAS's allocation for 2021 is accurate and reflects the new EAF.

#### **NZAS Consultation**

12. NZAS was consulted on the options and prefers the status quo (EAF - 0.206 tCO<sub>2</sub>-e/MWh) mainly because it is consistent with past approaches.
13. In my view, accuracy of the EAF is more important than consistency. s 9(2)(f)(iv)

[REDACTED]

#### **Risks and mitigation**

14. This decision is of high sensitivity to NZAS as it affects a large part of its annual allocation of units. To manage the relationship risk, I will inform NZAS's CEO following the Cabinet decision.
15. A policy decision must be made now so that amendment regulations can be drafted and published by the end of April 2022. There is a risk that NZAS will not be able to apply for its allocation if this decision is not made by 9 December 2021.

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