



Cabinet

Minute of Decision

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New Zealand Emissions Trading Scheme: Non-Legislative Tools for Market Governance Framework

Portfolio **Climate Change**

On 29 August 2022, following reference from the Cabinet Economic Development Committee, Cabinet:

Background

- 1 **noted** that the New Zealand Emissions Trading Scheme (NZ ETS) market is subject to a patchwork of regulation that leaves gaps, and that there is no single regulator responsible for market oversight;
- 2 **noted** that the NZ ETS market risks were identified in 2014, and that work on the NZ ETS market governance project has been ongoing since 2015;
- 3 **noted** the 2015 review of the NZ ETS found that market governance of the NZ ETS could be improved and was not fit for purpose;
- 4 **noted** that the Minister of Climate Change's view is that eight years is sufficient time for consideration and that decisions are now urgent;
- 5 **noted** that the identified market risks in the NZ ETS market require regulation;
- 6 **noted** that officials will undertake further work to consider regulatory options to address the identified market risks;
- 7 **noted** that on 10 December 2018, Cabinet agreed in principle, subject to final decisions on the broader, coherent market governance framework, to:
 - 7.1 prohibit insider trading and market manipulation in the NZ ETS market;
 - 7.2 as much as is practical and appropriate:
 - 7.2.1 to approach insider trading and market manipulation in the same manner as they are treated in the Financial Markets Conduct Act 2013 (FMCA);
 - 7.2.2 to have penalties and offences for insider trading and market manipulation in the NZ ETS mirror the equivalent relevant penalties and offences in the FMCA;


[CAB-18-MIN-0606.01]

- 8 **noted** that officials consulted on market risks, options, and market governance scenarios in 2018 and 2021;
- 9 **noted** that progressing amendments to the NZ ETS market governance framework is a priority area for the government;

Progressing non-legislative tools to improve market efficiency and operations of the NZ ETS

- 10 **agreed in principle**, subject to paragraphs 12 and 13 below, to address governance of trading risks with an optional centralised exchange;
- 11 **agreed in principle**, subject to paragraphs 12 and 13 below, that the optional centralised exchange be designed to preserve the option of treating New Zealand Units (NZUs) as a financial product;
- 12 **directed** the Ministry for the Environment (MfE), in consultation with the Ministry of Business, Innovation and Employment (MBIE) and the Ministry for Primary Industries (MPI), to undertake further analysis on an optional centralised exchange to address governance of trading risks to better understand:
- 12.1 the technical requirements of the optional centralised exchange and the legislative changes required;
 - 12.2 how future decisions on potential legislative tools to support a comprehensive package for market governance of the NZ ETS, including those on whether or not NZUs should be treated as a financial product, might have implications on how this optional centralised exchange is designed, implemented and operated;
 - 12.3 the level of funding required, and to whom, in order to give effect to the preferred approach to design, implementation and operation as identified through the work described above;
- 13 **noted** that the Minister of Climate Change intends to return to Cabinet in November 2022 with:
- 13.1 the technical requirements of the optional centralised exchange;
 - 13.2 how future decisions on potential legislative tools might have implications on this optional centralised exchange;
 - 13.3 the level of funding required;
- 14 **noted** that the Minister of Climate Change also intends to return to Cabinet in early 2023 to seek agreement for any supporting legislative amendments identified as being required for the optional centralised exchange, alongside consideration of a comprehensive market governance package for the NZ ETS;
- 15 **noted** that a Request for Information or tender process will help inform the technical requirements and/or legislative changes required;

16 s 9(2)(f)(iv)



17 s 9(2)(f)(iv)

Progressing legislative amendments to regulate market risks in the NZ ETS

- 18 **noted** that the proposal to treat NZUs as financial products has not been tested with the marketplace;
- 19 **directed** MfE, in consultation with Treasury, MBIE and MPI, to prepare a discussion document for targeted engagement by end of September 2022, for Cabinet's consideration in November 2022;
- 20 **noted** that the consultation package should:
- 20.1 seek feedback on:
 - 20.1.1 treating NZUs as a financial product;
 - 20.1.2 treating financial advice relating to NZUs as a financial advice service;
 - 20.1.3 treating market risks in the NZ ETS as financial risks;
 - 20.1.4 including the NZ ETS market under existing financial frameworks legislation;
 - 20.1.5 appointing the Financial Markets Authority to oversee and regulate the NZ ETS market;
 - 20.2 seek to better understand the impacts and prioritisation of the seven identified market risks for stakeholders;
 - 20.3 seek feedback from stakeholders on the financial and administrative impacts of leveraging the FMCA and applying the following policy tools to the NZ ETS market:
 - 20.3.1 introducing a Code of Conduct, licensing and registration framework using a similar approach as the FMCA to regulate the provision of financial advice relating to NZUs;
 - 20.3.2 applying the licensed market framework using a similar approach as the FMCA to regulate market operators;
 - 20.3.3 prohibiting insider trading and market manipulation using a similar approach as the FMCA;
 - 20.3.4 any other FMCA provisions that may be relevant to addressing the seven market governance risks;
 - 20.4 seek feedback on the impact on stakeholders of leveraging the existing Anti-Money Laundering and Counter-financing of Terrorism Act 2009 in the NZ ETS market;
 - 20.5 seek feedback on the impact on stakeholders of increased disclosure obligations under an improved transaction reporting framework to include transaction price and value reporting via the New Zealand Emissions Trading Register;
 - 20.6 seek feedback on the scope and overlap between the proposal to treat financial advice relating to NZUs as financial advice, and forestry adviser services under the Forests Act 1949, and the appropriate legislative approach;

20.7 seek feedback on alternative market governance proposals to achieve the same outcomes of mitigating the seven risks;

21 **noted** that the Minister of Climate Change intends to return to Cabinet in November 2022 to seek agreement to commence the targeted engagement with stakeholders;

22 **noted** that subject to the outcomes of this targeted engagement and further analysis, the Minister of Climate Change intends to introduce any comprehensive market governance package this parliamentary term;

23 **noted** that MfE will provide a regulatory impact analysis when seeking policy decisions;

Funding implications

24 s 9(2)(b)
(ii)

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25 s 9(2)(f)(iv)

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26 s 9(2)(f)(iv)

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27 s 9(2)(f)(iv)

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28 s 9(2)(f)(iv)

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29 s 9(2)(f)(iv)

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30 s 9(2)(f)(iv)

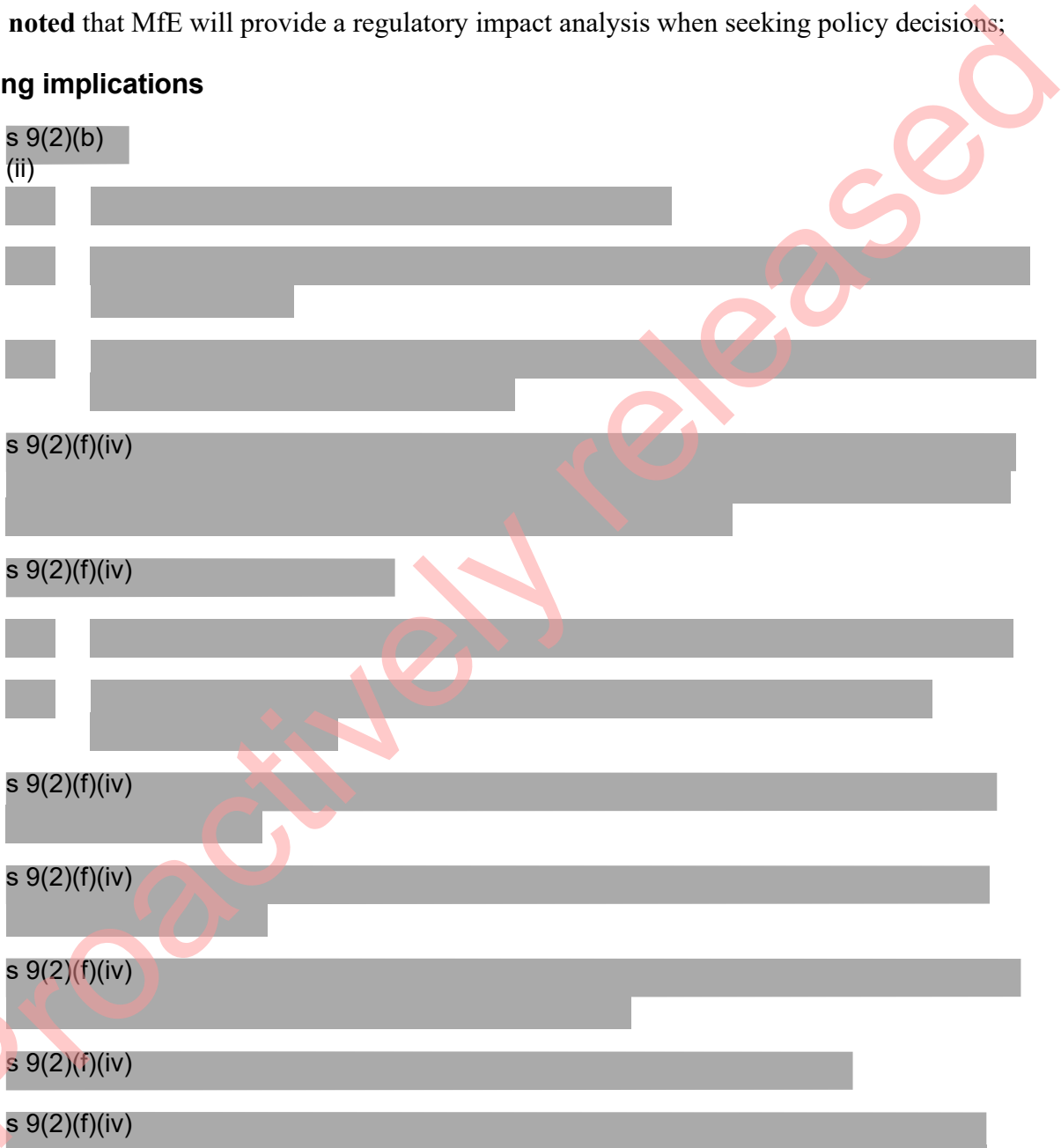
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31 s 9(2)(f)(iv)

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32 s 9(2)(f)(iv)

[Redacted text block]



Legislative implications

- 33 **noted** that any proposals for legislative amendments will likely require a Climate Change Response Amendment Bill;
- 34 **noted** that an appropriate place for the Amendment Bill will be sought on the 2023 Legislation Programme.

Rachel Hayward
Acting Secretary of the Cabinet

Proactively released