



Ministry for the
Environment
Manatū Mo Te Taiao

2025 Report on Reasons for Differences between Prescribed NZ ETS Limits and Price Control Settings for Units and the Climate Change Commission's Advice on these Settings

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Te Kāwanatanga o Aotearoa
New Zealand Government

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Contents

Executive summary	4
Introduction	5
Context	6
Differences in unit limits	7
Analytical judgement differences	8
Technical differences	10
Differences in price control settings	12
Key points from NZ ETS settings refresh	13

Executive summary

1. The Government's decision to extend existing auction volumes to 2030 will make 13.6 million less units available over the 2026 to 2030 settings period compared with the Commission's recommendation to increase auction volumes for 2028 to 2030.
2. The difference in approach to auction volumes stemmed from a combination of:
 - a. different analytical judgements, including how to balance the risks of oversupply and undersupply, respond to risks of achieving the third New Zealand emissions budget (EB3) and interpret market signals
 - b. technical differences, including different assumptions underpinning surplus stockpile estimates and updated data that was unavailable at the time of the Commission's advice.
3. The only difference between the Government's decision on price controls and the Commission's recommendations stems from the use of updated inflation rates.

Introduction

4. This report sets out the reasons for differences between the Climate Change Commission's (the Commission) 2025 advice on limits and price control settings for units in the New Zealand Emissions Trading Scheme (NZ ETS unit settings) and the settings that have been prescribed in the Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020¹ (the Regulations).
5. A report explaining the differences is required under section 30GC(7) of the Climate Change Response Act 2002 (the Act).
6. The information in this report about the Commission's advice has been drawn from the Commission's 2025 NZ ETS settings advice report and associated annexes, as well as further discussions held with the Commission as part of the NZ ETS settings refresh project. The refresh project was a short, targeted review of the advisory frameworks and analytical tools used to develop advice on NZ ETS settings. The objective of the refresh project was to ensure these frameworks and tools remain fit for purpose and to identify opportunities for improvement, to support market confidence.²

¹ Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020.

² Opportunities to improve New Zealand Emissions Trading Scheme Advisory Frameworks and Tools.

Context

7. Unit limits restrict the supply of emissions units into the NZ ETS through auctions. Unit limits include:
 - a. a limit on the units available by auction (auction volumes)
 - b. a limit on approved overseas units – currently zero
 - c. an overall limit on units – which consists of units available by auction and the cost containment reserve (CCR), by other means (primarily industrial allocation), and approved overseas units.
8. In practise, the effect of NZ ETS price controls settings is to set the bounds for high and low prices for units sold at auction.
9. Regulations prescribing NZ ETS unit settings need to be updated each year. This is to meet the requirement under the Act³ that, at all times, settings are in place for each of the following five calendar years.
10. The Commission provides annual advice with its recommendations on NZ ETS unit settings for the upcoming five years under section 5ZOA of the Act. The Minister of Climate Change tabled the Commission’s advice on unit settings for 2026 to 2030 on 23 April 2025.⁴

³ Climate Change Response Act 2002 No 40 (as at 01 January 2024), Public Act 30GB Regulations about limits and price control settings for units – New Zealand Legislation, section 30GB(3).

⁴ He Pou a Rangi Climate Change Commission, Advice on NZ ETS unit limits and price control settings for 2026–2030, April 2025 C.31.

Differences in unit limits

11. The Commission recommended that 30.5 million units should be available at auctions over the 2026–2030 settings period. This recommendation was based on the ‘seven steps’ methodology for determining unit settings. The methodology is a flexible organising framework for stepping through matters that must be considered under the Act and determining appropriate unit settings that accord with emissions reduction targets, given current circumstances and best assumptions for other sources of units. The Commission has consistently used the seven steps methodology for determining its recommended unit settings.
12. This year, the Government treated the outcome from the seven steps methodology as the maximum possible auction volumes that are consistent with accordance requirements. The Government then considered several options within this maximum, informed by:
 - a. analytical judgements – qualitative judgements on key points that differed from those applied by the Commission
 - b. technical differences – different assumptions for the surplus stockpile and updated data sets that directly impact on auction volumes.
13. The Government chose to extend existing auction volumes to 2030, with total auction volumes of 16.9 million units over the 2026 to 2030 settings period. The annual difference in auction volumes between the Commission’s recommendation and Government’s decision is shown in Table 1.

Table 1: Differences in unit limits between the Commission’s 2025 advice and those prescribed in regulations

Million units	2026	2027	2028	2029	2030
Prescribed New Zealand Units (NZUs) available by auction (base auction volumes)	5.2 <i>CCC – 5.2</i>	4.3 <i>CCC – 4.3</i>	3.3 <i>CCC – 7.0</i>	2.4 <i>CCC – 7.0</i>	1.7 <i>CCC – 7.0</i>
Total cost containment reserve volumes	6.5 <i>CCC – 6.5</i>	5.9 <i>CCC – 5.9</i>	5.3 <i>CCC – 5.3</i>	4.7 <i>CCC – 4.7</i>	3.9 <i>CCC – 3.9</i>
Total NZUs available by auction	11.7 <i>CCC – 11.7</i>	10.2 <i>CCC – 10.2</i>	8.6 <i>CCC – 12.3</i>	7.1 <i>CCC – 11.7</i>	5.6 <i>CCC – 10.9</i>
Industrial allocation (not subject to NZ ETS settings decision)*	4.6 <i>CCC – 5.7</i>	4.4 <i>CCC – 5.7</i>	4.1 <i>CCC – 4.6</i>	4.0 <i>CCC – 4.5</i>	4.0 <i>CCC – 4.0</i>
Approved overseas units	0 <i>CCC – 0</i>	0 <i>CCC – 0</i>	0 <i>CCC – 0</i>	0 <i>CCC – 0</i>	0 <i>CCC – 0</i>
Overall limit on units	16.3** <i>CCC – 17.4</i>	14.6** <i>CCC – 15.9</i>	12.7 <i>CCC – 16.9</i>	11.1 <i>CCC – 16.2</i>	9.6 <i>CCC – 14.9</i>

* Note the Commission did not update industrial allocation figures for 2026 and 2027, instead incorporating the impacts of updated forecasts into the discrepancy adjustment. This means the total difference here between the Commission and the Government’s industrial allocation volumes is greater than the explanation below (paras 34–36)

** Note the government chose to update the overall limits for 2026 and 2027 to align with our best estimate of industrial allocation volumes.

14. This year's approach reflects a departure from how the Government has made NZ ETS settings decisions in previous years, which have been based strictly on the application of the 'seven steps' methodology. This report explains the rationale for the Government's decision.

Analytical judgement differences

15. There were four major areas where the Government made different analytical judgements compared with the Commission.

The balance of risks between oversupply and undersupply of unit volume under the emissions cap, and how best to manage those

16. When determining unit limits, there is both a risk of oversupply and undersupply of units into the market. Oversupply of units could affect the ability for New Zealand to meet its emissions reduction targets. Undersupply risks the proper functioning of the market, potentially leading to excessive price volatility, which could unnecessarily impact businesses and consumers and damage the ability of the NZ ETS to efficiently reduce emissions in line with our emissions reduction targets.
17. The Commission is concerned about oversupply, but also about the damage that undersupplying the market could cause, for example through excessive price volatility. Its preferred approach to balance these risks this year was by providing for auction volume up to the emissions cap over years 2028 to 2030, with a robust auction reserve price⁵ preventing units from entering the market if they are not needed.
18. To further mitigate the risk of oversupply, the Commission took a new approach to phasing the increased auction volumes. It recommended distributing auction volumes evenly across 2028 to 2030. This would mean relatively lower auction volumes in 2028 and higher auction volumes in 2029 and 2030, compared with the default approach (declining in line with the NZ ETS cap). This would preserve more volume in later years that could be more easily changed in future.
19. The Government's decision took a more cautious approach to the risk of oversupply for achieving emissions reduction targets – especially the challenging EB3. Given the significant uncertainty associated with estimating the surplus, it is possible that the surplus could be larger or smaller than estimated. Because of the one-sided nature of auctioning as a lever (once units have been auctioned, the Government cannot easily remove them from the market), this year, the Government had a higher tolerance for the risk of undersupply than it did for oversupply. Additionally, the Government considered the risks of under-supply to be low in the short term, given its view that signs suggest the market is currently well-supplied (explained further below).
20. The Government did not follow the Commission's proposed approach to phasing auction volumes and chose instead to continue the longstanding approach of distributing auction volumes in line with the NZ ETS cap. Changing the approach to distributing auction volumes was not necessary because the Government's lower unit settings meant further mitigation of the risk of oversupply was unnecessary.

⁵ Rising to \$87 by 2030.

Additional emphasis on supporting achievement of the third emissions budget

21. EB3 is expected to be particularly challenging, and there is currently a gap between projected emissions and the EB3 target. The Commission highlighted that aligning the unit limits with the 2026 to 2030 emissions projections in the Government's second emissions reduction plan is still in accordance with the third emissions budget, since the deeper reductions are not required until after the period of the Commission's advice. The Commission noted that future advice that does cover part of the third emissions budget period (2031 to 2035) can align with an adjusted pathway that accounts for the additional reductions needed.
22. The Government's decision to extend status quo volumes is intended to better support meeting the EB3 target by reducing the existing gap between projected emissions and EB3 sooner. Keeping unit settings tighter now increases the chance that the surplus stockpile is eliminated before EB3 begins and will mean the NZ ETS will be more effective at reducing net emissions during the EB3 period.

The conclusions to be drawn from recent New Zealand Unit prices⁶ about the size of the surplus and outlook for supply and demand over the next 5 years

23. The Commission considered that there are several factors that contributed to the New Zealand Unit (NZU) spot price sitting below the auction reserve price, including wider regulatory uncertainty about the NZ ETS and climate policy overall, participants' limited market foresight, and the inefficiency of the NZ ETS market. While the price and availability of units in the secondary market indicated that there is sufficient unit supply in the short term, the Commission did not consider this provided evidence in itself for increasing the surplus estimate or concluding that status quo settings would provide sufficient units in line with targets from 2028 onwards.
24. The Government considered that recent NZU prices and partial clearance of auctions in 2024 support the view that the surplus may be larger than the Commission's central estimate, and that sufficient units in line with targets are likely to be available in the market over the next five years, even with tighter unit settings than those recommended by the Commission.

The approach to regulatory predictability and market stability

25. Both the Commission and the Government agree that regulatory predictability and stability in the market are best supported by prioritising consistency of methodological approach and process, where changes are well-signalled and understood, and settings implement the emissions cap. While it was not the determinative factor, this year Government also noted feedback from public consultation that maintaining status quo settings would support overall market stability and took that into account in its 2025 settings decisions. The Government considered that improved market stability from

⁶ This refers to both the secondary market spot price as well as recent auctions not clearing, which reflect that spot prices are below the auction reserve price.

extending status quo auction volumes justified the reduction in regulatory predictability that comes with a departure from the strict application of the seven steps methodology.

Technical differences

26. In addition, there were several analytical updates or changes made by the Ministry for the Environment (MfE) in their final analysis and estimates for the surplus stockpile and industrial allocation volumes. These were factored into the Government's decision to extend status quo volumes.
27. A key change in the surplus estimate methodology this year has been the introduction of the concept of 'holding' volumes. These refer to units that are being held to cover emissions that have already occurred but haven't yet been surrendered to fulfil the current compliance cycle. Holding volumes are subtracted from the total stockpile to calculate the estimated surplus stockpile. Both the Commission and the Government made this methodological change (as recommended by an expert report commissioned by the Ministry for the Environment) but took a different approach with regards to how this change impacts hedging volumes (units held in anticipation of future emissions).

Updated surplus stockpile assumption – level of hedging volume

28. The separation out of the holding volume raised questions about whether any overlap or double counting exists between the hedging assumption used in previous decisions and the new holding volume category. If an overlap exists, it would result in higher estimates of the surplus stockpile because fewer units are being subtracted from the overall stockpile of units. This directly impacts auction volumes, with a reduction in auction volumes corresponding to the difference in surplus stockpile estimates.
29. The Commission's advice treated holding volumes and hedging volumes as additional to each other. Specifically, the Commission did not adjust the hedging coverage assumption used in previous decisions, which may account for coverage now considered to be holding volumes. The Commission highlighted in its advice that this was an area of uncertainty and suggested the Government test its assumptions during feedback.⁷
30. The evidence we have been able to gather indicates that at least some emitters do not hold distinct (or additional) holding and hedging volumes. Instead, many emitters use units held for upcoming compliance to hedge price (if they hedge at all).
31. However, it has been challenging to quantify this overlap. The NZU holders survey, submissions on the NZ ETS Settings discussion document and desktop research based on firms' financial reports have provided limited insight on the specific level of overlap.
32. In absence of robust quantitative evidence, the Government chose to take a conservative estimate (ie, assuming a greater overlap), as underestimating the overlap risks underestimating the size of the surplus stockpile. This could mean the surplus stockpile is not fully drawn down as intended, increasing the challenge in achieving New Zealand's emissions reduction targets.

⁷ He Pou a Rangi | Climate Change Commission. NZ ETS unit limits and price control settings for 2026–2030. p43

33. Given the holding volume estimate is based on emissions that have actually occurred, it is more appropriate to retain this estimate based on the best available data. Therefore, the adjustment should be applied to the hedging volume estimate via changes to the future hedging assumptions. This increased the Government's surplus central estimate by 5.4 million units compared with the Commission's estimate.⁸ It also increased the upper range of the surplus estimate by 10.0 million units compared to the Commission. This accounts for almost a third of the difference between the Commission's recommend auction volumes and the Government's agreed auction volumes.

Adjusting surplus estimates based on 2024 net surrenders information

34. Data on 2024 surrender compliance volumes published by the Environmental Protection Authority after the Commission provided its advice has allowed the Ministry for the Environment to refine the estimate of holding volumes. These figures indicate net surrenders of 34.0 million for the period 1 July 2024 to 30 June 2025, 0.2 million units lower than provisional estimates of the holding volume. This increases the surplus estimate by 0.2 million units compared with the Commission's estimate, with a corresponding reduction in auction volumes.

Updating industrial allocation forecasts for recent data and to align with 2025 projections

35. Industrial allocation forecasts have been updated to incorporate 2024 actual allocations, which were released after the Commission provided its advice. Aggregate industrial allocation was very close to the level forecast by the Commission but with some differences at the sectoral level.
36. In addition, future output adjustment assumptions have been updated to align information available as of mid-July 2025. The most material change is bringing forward the assumption of when Methanex will close by one year to the end of 2027 and assuming lower production levels prior to reflect ongoing winter closures to release gas for electricity generation. This is the same set of assumptions used in the 2025 projections.⁹
37. Together, these changes result in industrial allocation forecasts 2.1 million units lower than the Commission forecast for the 2026 to 2030 settings period. This could allow a corresponding increase in auction volumes.

⁸ Additional details on the methodology for estimating the overlap between hedging and holding volumes can be found in pages 15–16 of [Regulatory Impact Statement – 2025 update to New Zealand Emissions Trading Scheme limits and price control settings for units](#).

⁹ [Updated emissions projections to 2050 released | Ministry for the Environment](#).

Differences in price control settings

38. Both the Commission and the Government adjusted the last three years of price controls to account for inflation. Price control settings prescribed in regulations use the most recent inflation rates from Budget Economic and Fiscal Update 2025.¹⁰ The Commission had used earlier forecasts of inflation rates,¹¹ but recommended Government should use the latest inflation rates. As with last year, price control settings were also rounded to the nearest whole number.
39. This means the prescribed price control settings for some years vary by \$1–2 from those in the Commission’s 2025 advice (highlighted in table 2). However, they are the same as the Commission’s in inflation-adjusted terms.

Table 2: Differences in price control settings between the Commission’s 2025 advice and those prescribed in regulations

		2026 (no difference)	2027 (no difference)	2028	2029	2030
Cost containment reserve trigger price	Tier 1	\$203	\$213	\$224	\$236	\$248
		CCC \$203	CCC \$213	CCC \$223	CCC \$235	CCC \$246
	Tier 2	\$254	\$267	\$280	\$295	\$309
		CCC \$254	CCC \$267	CCC \$279	CCC \$293	CCC \$308
Auction reserve price		\$71	\$75	\$78	\$82	\$87
		CCC \$71	CCC \$75	CCC \$78	CCC \$82	CCC \$86

40. There were no differences between the Commission’s recommended cost containment reserve volumes and those agreed by the Government.

¹⁰ Budget Economic and Fiscal Update 2025 | The Treasury New Zealand.

¹¹ Half Year Economic and Fiscal Update 2024 | The Treasury New Zealand.

Key points from NZ ETS settings refresh

41. Following public consultation on NZ ETS settings this year, MfE and the Commission jointly undertook a short, targeted review of the advisory frameworks and analytical tools used to develop advice on NZ ETS settings.
42. The objective was to ensure these tools and frameworks remain fit for purpose and identify opportunities for improvement, noting that NZ ETS auctions were established five years ago, so it is timely to undertake a review. This process also enabled us to better understand the differences in our advice this year. We concluded that the overall advisory and analytical frameworks for NZ ETS settings remain suitable. Differences in conclusions can arise from the uncertainties inherent in the NZ ETS settings process, and can offer valuable insights, provided they are transparent and well understood.
43. The project identified several opportunities for improvement, for both the Commission and MfE.
 - a. **Enhancing communication of key judgements and assumptions** – highlighting the decision-space for decision-makers – enabling decision-makers to understand that alternative options can still meet statutory requirements.
 - b. **Improving clarity in how market conditions have been considered and address potential sources of confusion** – explicitly explaining how factors like non-clearing auctions inform advice, and proactively clarifying recommendations which may differ markedly from stakeholder expectations, where possible.
 - c. **Managing surplus uncertainty and addressing risk** – both organisations can explore ways to illustrate the implications of the surplus uncertainty, for example by showing what a different estimate of the surplus might mean for auction settings.
 - d. **Continually improving analytical tools and approaches** – exploring alternative models and approaches to support richer insights, including through ongoing collaboration.
44. Together, this is expected to support improved confidence and better-informed decision making for the NZ ETS settings process in future years. Differences in analysis should be easier to identify.