



Cabinet Environment, Energy and Climate Committee

Minute of Decision

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New Zealand Emissions Trading Scheme: Tranche Two: A Phase-Down of Industrial Allocation

Portfolio **Climate Change**

On 2 May 2019, the Cabinet Environment, Energy and Climate Committee:

- 1 **noted** that the New Zealand Emissions Trading Scheme (NZ ETS) is the government's key tool to assist New Zealand to meet its climate change targets, and that:
 - 1.1 the government is reforming the NZ ETS to ensure it can support the transition to a low-emissions and climate resilient New Zealand;
 - 1.2 this requires amendments to the Climate Change Response Act 2002 (CCRA);
- 2 **noted** that these amendments are being developed in tranches;
 - 2.1 in December 2018 Cabinet agreed to tranche one of amendments to the CCRA and drafting has commenced [CAB-18-MIN-0606.01];
 - 2.2 tranche two comprises of a series of papers with discrete proposals which will be considered by Cabinet over March to May 2019;
 - 2.3 tranche one and two will result in a single bill amending the CCRA to be introduced to the House in mid-2019, and to enter into force in 2020;
- 3 **noted** that the tranche two paper, attached under ENV-19-SUB-0017, focuses on phasing down industrial allocation in the NZ ETS;
- 4 **noted** that the proposals in the paper under ENV-19-SUB-0017, relate only to industrial allocation and have no implications for any future decisions on agriculture or for any allocations or other support for agricultural participants;
- 5 **noted** that decisions requested in the paper under ENV-19-SUB-0017, are for drafting purposes only and will be agreed subject to a subsequent Cabinet decision after Budget 2019 is delivered;
- 6 **noted** that the purpose of industrial allocation in the NZ ETS is to mitigate the risk of emissions leakage;

- 7 **noted** that while emissions leakage continues to be a risk for some eligible persons carrying out EITE activities, individual improvements in emissions-intensity and competing jurisdictions increasingly pricing their own emissions justify some adjustments to levels of industrial allocation;
- 8 **noted** that current levels of industrial allocation will take an increasing proportion of future emission budgets within the context of meeting the Climate Change Bill (CCB) and Paris Agreement emissions reduction targets;
- 9 **agreed in principle**, for the purpose of issuing drafting instructions, to phase down industrial allocation with the first reduction applying to the calendar 2021 emissions reporting year;
- 10 **agreed in principle**, for the purpose of issuing drafting instructions, to establish minimum phase-down rates that will be set in legislation and specified as a minimum annual reduction applied to the level of assistance for all eligible activities of 0.01 for each of the years 2021 to 2030, 0.02 for each of the years 2031 to 2040 and 0.03 for each of the years 2041 to 2050;
- 11 **noted** that an annual reduction of 0.01 means that the Level of Allocation, as defined in the CCRA, will be reduced from 0.9 to 0.89 in 2021, 0.88 in 2022 and so forth for highly emission-intensive activities, and from 0.6 to 0.59 in 2021, 0.58 in 2022 and so forth for moderately emission-intensive activities;
- 12 **agreed in principle**, for the purpose of issuing drafting instructions, that the responsible Minister may make regulations to reduce the minimum phase-down rate for the period 2031 to 2040, and for the period 2041 to 2050, if the Commission recommends such a reduction based on an assessment that there is an ongoing and substantial risk of emission leakage;
- 13 **agreed in principle**, for the purpose of issuing drafting instructions, that the Commission may not recommend, and the Minister may not make regulations for, a minimum phase-down rate less than 0.01 for each of the years 2031 to 2040 or a minimum phase-down rate less than 0.02 for each of the years 2041 to 2050;
- 14 **agreed in principle**, for the purpose of issuing drafting instructions, that there will be a decision-making process that will allow the government to set activity-specific phase-downs of any one or more eligible activities in regulations in advance for the 2026–30 emissions budget period and for each subsequent five-year budget period established under the CCB;
- 15 **agreed in principle**, for the purpose of issuing drafting instructions, that regulations will set mandatory phase-downs for the relevant budget period, and indicate intended phase-down rates for the following budget period;
- 16 **agreed in principle**, for the purpose of issuing drafting instructions, that the collective effect of the minimum phase-down rate and all of the regulations phasing down individual activities for a given budget period must generally not be inconsistent with New Zealand’s meeting the emissions budget for that period;
- 17 **agreed in principle**, for the purpose of issuing drafting instructions, that when making decisions on an activity-specific phase-down of allocation the Minister for Climate Change must have regard to:
- 17.1 New Zealand’s targets and indicative future emission budgets as set under the CCB and New Zealand’s Nationally Determined Contributions under the Paris Agreement;

- 17.2 The risk of emission leakage on an activity-specific basis, including:
- 17.2.1 emission pricing and other policies in competing jurisdictions, their cost, any assistance such as allocation, and its phase-out;
 - 17.2.2 the markets for international trade in the specified products produced by eligible industrial activities;
 - 17.2.3 any ability of industrial allocation recipients in New Zealand to pass on increased costs to customers;
- 17.3 any risk that the value of the industrial allocation for an eligible activity exceeds the cost of meeting NZ ETS obligations affecting the activity;
- 17.4 other sources of supply into the NZ ETS, including offshore emission reductions obtained by the government or available to NZ ETS participants;
- 17.5 the availability of low-emission technologies related to each activity;
- 17.6 New Zealand's relevant international obligations;
- 17.7 the proper functioning of the NZ ETS;
- 17.8 the cost to the taxpayer of providing allocation;
- 17.9 recommendations of the Climate Change Commission;
- 17.10 any other matters the Minister for Climate Change considers relevant;
- 18 **agreed in principle**, for the purpose of issuing drafting instructions, that before regulations setting an activity-specific phase-down are made, the Climate Change Commission (the Commission) must prepare advice on the phase-down and provide the responsible Minister with a report detailing its recommendations for the regulations;
- 19 **noted** that ongoing operational costs for the Commission will be managed as part of its overall work programme;
- 20 **agreed in principle**, for the purpose of issuing drafting instructions, that if final decisions depart from the Commission's recommendations, the responsible Minister must provide a report giving reasons for any decisions that differ from the CCC's advice, present the report to Parliament, and make it publicly available;
- 21 **noted** that regulations will need to be in effect before 1 January 2026 and before the start of each subsequent budget period to have effect throughout that period;
- 22 **agreed in principle**, for the purpose of issuing drafting instructions, that the Minister must be satisfied that consultation with affected parties has occurred before making regulations, including publication of a draft proposal and a period of at least 20 working days for submissions;
- 23 **noted** that this means that the Minister will need to consult with affected parties on any proposal that has not already been included in consultation carried out by the Commission;

- 24 **agreed in principle**, for the purpose of issuing drafting instructions, that if a budget is revised or if, in exceptional circumstances, the matters that the Minister considered in making it require reconsideration, a regulation setting activity-specific phase-downs for a particular budget period may be amended during the budget period, if recommended by the Commission;
- 25 **noted** that the Minister for Energy and Resources' work programme on process heat is looking at a range of measures to encourage uptake of best available low emissions technology in the industrial sector, including EITE firms;
- 26 **authorised** the Minister for Climate Change to further clarify policy decisions relating to the amendments proposed in the paper under ENV-19-SUB-0017, in a way not inconsistent with Cabinet's decisions;
- 27 **invited** the Minister for Climate Change to issue drafting instructions to the Parliamentary Counsel Office based on the decisions presented in the paper under ENV-19-SUB-0017;
- 28 **agreed** the Minister for Climate Change, in consultation with the Minister of Finance, the Minister of Energy and Resources and the Minister for Economic Development, can make in-principle policy decisions, for the purpose of issuing drafting instructions, to allow the bringing forward of free allocation to incentivise technological change to low carbon alternatives for emissions-intensive trade-exposed industries, other than agriculture;
- 29 **agreed** that no announcements will be made about industrial allocation until the in-principle policy decisions have been approved by Cabinet.

Vivien Meek
Committee Secretary

Present:

Rt Hon Winston Peters
Hon Kelvin Davis
Hon Dr Megan Woods
Hon David Parker (Chair)
Hon Stuart Nash
Hon James Shaw
Hon Eugenie Sage

Officials present from:

Office of the Prime Minister
Officials Committee for ENV

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Minister for Climate Change