

Policy and Privacy

In-Confidence

Office of the Minister of Climate Change

LEG - Cabinet Legislation Committee

## Climate Change (Eligible Industrial Activities) Amendment Regulations 2023

### Proposal

- 1 I propose the Cabinet Legislation Committee (LEG) authorise submission of the attached Climate Change (Eligible Industrial Activities) Amendment Regulations 2023 to the Executive Council.
- 2 The amendment regulations prescribe the New Zealand Aluminium Smelters Limited (NZAS) final allocative baseline<sup>1</sup> for 2022 and provisional allocative baselines for 2023 and 2024 under the New Zealand Emissions Trading Scheme (NZ ETS).

### Relation to Government Priorities

- 3 The Government declared a climate change emergency on 2 December 2020. The Cabinet Business Committee (CBC) agreed that climate change “demands a sufficiently ambitious, urgent, and coordinated response across government to meet the scale and complexity of the challenge” [CBC-20-MIN-0097 refers].
- 4 Enabling a just transition to a low-emissions, climate resilient future is also a government priority. This was emphasised by the CBC when they noted the intention to “put the climate at the centre of government decision-making” and agreed that “climate change requires decisive action by all levels of government, the private sector, and communities” [CBC-20-MIN-0097 refers].

### Executive Summary

- 5 Several regulatory changes are required each year to keep the NZ ETS operating efficiently. Smelting aluminium is an eligible industrial activity under the Climate Change Response Act 2002 (CCRA) and the Climate Change (Eligible Industrial Activities) Regulations 2010 (the Regulations) because it is an emissions intensive activity and there is international trade. NZAS is

<sup>1</sup> An allocative baseline specifies how many emission units an eligible activity receives per unit of output. The baseline for NZAS is expressed in New Zealand Units (NZU) per tonne of aluminium produced. Eligible firms receive a provisional allocation based on forecast levels of output. The allocation is finalised once actual output levels are known.

eligible to receive an allocation of emission units to assist it offset the costs of the emissions trading scheme.

- 6 Aluminium smelting has an annual update process for allocation regulations because of NZAS' electricity pricing arrangements and significant electricity use (approximately 12-13 per cent of New Zealand's electricity demand). This process ensures the annual allocation fairly reflects emissions costs under current policy.
- 7 The proposed changes to the Regulations result in a minor change from previous rates of allocation.
- 8 The amendment regulations need to be published in the New Zealand Gazette by 31 March 2023 to allow sufficient time for NZAS to meet the 30 April 2023 deadline for allocation applications.

### Background

- 9 Several regulatory changes are required each year to keep the NZ ETS operating effectively and efficiently. Aluminium smelting is an emissions intensive activity and has international trade so is an eligible industrial activity under the CCRA and the Regulations.
- 10 NZAS is entitled to receive industrial allocation of New Zealand Units (NZUs) to offset the costs the NZ ETS.
- 11 NZAS' allocation covers the emissions costs from direct emissions from onsite production, indirect emissions cost of electricity purchased on the wholesale market and the indirect emissions cost of electricity purchased through electricity supply agreements.
- 12 Section 161C(4) of the CCRA grants the Minister of Climate Change powers to adjust allocation calculations to take account of electricity-related contracts. NZAS is the only recipient of industrial allocation with adjusted calculations for new contracts.
- 13 NZAS has a special process for allocation because of its significant electricity use (approximately 12-13 per cent of New Zealand's electricity demand) and because of the nature of its electricity supply contracts. Other firms buy electricity at or near spot prices and they receive NZUs to cover electricity generation emissions at a standard rate. NZAS receives a lower, and variable, amount because its exposure to the spot market electricity cost is limited.
- 14 Allocations to NZAS are based on three variables, namely, the production of aluminium, the emissions intensity (the allocative baseline), and the assistance rate. The assistance rate is currently being phased down by 1% per year.
- 15 NZAS' allocative baselines for the previous and current years are adjusted every year according to how much electricity NZAS consumed in the previous year under its contracts and from the spot market.



- 16 A provisional allocative baseline is also created for the next year to assist NZAS and the Government with forecasting. This annual operational and technical update protects the Crown from over-allocating or under-allocating NZUs to NZAS.

**Analysis**

- 17 Cabinet has previously authorised the Minister of Climate Change to adjust NZAS’ allocative baseline to reflect the NZ ETS costs from electricity consumption without referring to Cabinet, except where financial or policy implications are significant enough to warrant Cabinet consideration [ENV-18-MIN-0051 and CAB-18-MIN-0628].
- 18 I used this delegation to approve drafting instructions for the amendment regulations, which are detailed in the following table. <sup>2</sup>

Year	Current Allocative Baselines (before change)	Proposed Allocative Baselines (with updates)
2019	5.366 (final)	5.366 (final, unchanged)
2020	5.194 (final)	5.194 (final, unchanged)
2021	2.120 (final)	2.120 (final, unchanged)
2022	2.005 (provisional)	2.048 (final)
2023	2.005 (provisional)	2.034 (provisional)
2024	Not set	2.034 (provisional)

- 19 The 2022 final allocative baseline is slightly higher than was set provisionally as the provisional baseline was based on no spot-market purchases of electricity.
- 20 Analysis of NZAS’s revised main electricity contract showed there is no NZ ETS cost component contained in the price it pays for its electricity purchased through this contract. Cabinet decided in 2021 to reflect this in the calculation of its baselines. The significant drop between 2020 and 2021 baselines shows the impact of this change.
- 21 The provisional allocative baselines for 2023 and 2024 are based on NZAS’ electricity consumption forecast for 2023 as provided by them.

**Timing and 28-Day Rule**

- 22 It is intended that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2023 come into force 28 days after the date of their notification in the New Zealand Gazette. The amendment regulations need to be in force to

<sup>2</sup> Updates are proposed for years 2022-2024 only. Prior years are provided to illustrate the change in allocative baseline resulting from decisions in relation to NZAS’ main electricity contract.

allow sufficient time for NZAS to meet the 30 April 2023 deadline for allocation applications.

- 23 Consideration of this paper at the 17 March LEG Committee meeting means that no waiver from the 28-day rule is required.

#### **Regulations Review Committee**

- 24 I do not consider that there are grounds for the Regulations Review Committee to draw the regulations in this paper to the attention of the House under Standing Order 319.

#### **Certification by Parliamentary Counsel**

- 25 These regulations have been certified by the Parliamentary Counsel Office as being in order for submission to Cabinet and are attached at Appendix 1.

#### **Financial Implications**

- 26 The changes proposed in this paper will have only a negligible impact on the Crown's operating balance. Based on NZAS' unaudited production figures for 2022, this update will result in NZAS receiving around 14,000 additional New Zealand Units than if the allocative baseline was not updated to reflect actual electricity use. This is covered by the appropriation for industrial allocation.

#### **Legislative Implications**

- 27 Regulatory amendments to the Climate Change (Eligible Industrial Activities) Regulations 2010 will be required to implement the proposed changes.

#### **Impact Analysis**

##### *Regulatory Impact Statement*

- 28 Cabinet has previously agreed that no Regulatory Impact Analysis will be required to accompany the annual legislative proposals containing updates to NZAS' baselines in the amended regulations [CAB Min (12) 43/6 refers]. A Regulatory Impact Analysis completed in June 2010<sup>3</sup> informed the decision to annually update NZAS' allocative baselines.

##### *Climate Implications of Policy Assessment*

- 29 The Climate Implications of Policy Assessment (CIPA) team at the Ministry has been consulted. They confirmed the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

#### **Population Implications**

- 30 The proposed amendments have no population implications.

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<sup>3</sup> As published on the Treasury's website: [New Zealand Emissions Trading Scheme: Industrial Allocation - 29 June 2010 - Regulatory Impact Statement - Ministry for the Environment \(treasury.govt.nz\)](#)



## Human Rights

- 31 There are no inconsistencies between the proposed amendments with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

## Consultation

- 32 There are no statutory consultation requirements for these regulations in the CCRA. In line with Cabinet Manual requirements, NZAS was consulted about, and agreed with, the calculation of the baselines in the proposed amendment regulations.
- 33 The Treasury, Ministry for Primary Industries, and the Ministry of Business, Innovation and Employment were consulted on this paper. The Department of Prime Minister and Cabinet and the Environmental Protection Authority have been informed. Where specific comments were provided, they are reflected in this paper.
- 34 NZAS and the Environmental Protection Authority will be notified when the Climate Change (Eligible Industrial Activities) Amendment Regulations 2023 are published. No other parties are affected.

## Proactive Release

- 35 I propose to proactively release this paper on the Ministry for the Environment's website in full, subject to redactions equivalent to those under the Official Information Act 1982, once amendment regulations are published.

## Recommendations

The Minister of Climate Change recommends that the Committee:

- 1 **Note** that Cabinet has previously authorised the Minister of Climate Change to make adjustments to the allocation level for the New Zealand Aluminium Smelter Limited (NZAS) to reflect the New Zealand Emissions Trading Scheme (NZ ETS) costs to NZAS from electricity consumption without referring to Cabinet, except where the financial or policy implications are significant enough to warrant Cabinet consideration [ENV-18-MIN-0051 and CAB-18-MIN-0628]
- 2 **Note** that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2023 will give effect to the decisions referred to in recommendation 1 above
- 3 **Note** that these amendments need to come into effect before the 30 April 2023 so that NZAS can apply for its NZ ETS allocation under the industrial allocation provisions of the Climate Change Response Act 2002 by this deadline
- 4 **Authorise** the submission to the Executive Council of the Climate Change (Eligible Industrial Activities) Amendment Regulations 2023

- 5 **Note** that it is intended that the Climate Change (Eligible Industrial Activities) Amendment Regulations 2023 come into force 28 days after the date of their notification in the New Zealand Gazette.

Authorised for lodgement

Hon James Shaw

Minister of Climate Change

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Appendix 1: Emissions Trading Scheme Climate Change (Eligible Industrial Activities) Amendment Regulations 2023

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