

Policy and Privacy

In-Confidence

Office of the Minister of Climate Change

ENV - Cabinet Environment, Energy and Climate Committee

Consultation report back on NZ ETS regulatory changes 2022

Proposal

- 1 This paper seeks your agreement to amend regulations under the Climate Change Response Act 2002 (the Act) and your approval of issuing drafting instructions to the Parliamentary Counsel Office.

Relation to government priorities

- 2 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].
- 3 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].
- 4 The proposals in this paper relate to the Cooperation Agreement between the Labour and Green Parties. Achieving the purpose and goals of the 2019 zero carbon amendments to the Act is an agreed area of cooperation.

Executive Summary

- 5 This paper seeks policy approval for amendments to regulations under the Act and authorisation for drafting instructions to be issued.
- 6 Amendments and updates to regulations under the Act are considered every year to meet legislative requirements and to address policy issues.
- 7 Public consultation in relation to these changes took place during March and April 2022.
- 8 Early engagement with the Parliamentary Counsel Office has identified timetables against which drafting could occur.
- 9 I recommend four regulatory changes for the New Zealand Emissions Trading Scheme (NZ ETS):

- 9.1 Removing a redundant regulation allowing New Zealand Units (NZUs) to be converted to Kyoto Protocol Assigned Amount Units (AAUs) for the purpose of cancellation.
 - 9.2 Removing regulatory barriers to NZ ETS incentives for collection of synthetic greenhouse gases for export or destruction.
 - 9.3 Updating the schedule of default emissions factors for natural gas fields to maintain accuracy and minimise administrative cost to participants
 - 9.4 Updating waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection and destruction to maintain accuracy and minimise administrative cost to participants.
- 10 I anticipate bringing a Cabinet paper with the associated amendment regulations to the Cabinet Legislation Committee during August 2022.

Background

- 11 The NZ ETS is a primary tool for assisting New Zealand to meet its emission reduction targets and emission budgets.
- 12 Updates to regulations under the Act are regularly made to ensure the NZ ETS operates efficiently and remains accurate. Some regulations under the Act are required to be updated every year. Other updates occur to address policy issues as they arise.
- 13 The changes I recommend in this paper address specific technical issues.
- 14 The Ministry for the Environment (the Ministry) carried out public consultation on these proposals over March to April 2022. The proposal on updating waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection and destruction was consulted on in 2021.
- 15 Submissions clarified understanding of the issues and have assisted in the development of the recommendations in this paper.

Analysis

Recommendations

- 16 I recommend changes to the regulations or methodology in relation to the topics summarised in Table 1 below. More detail on the analysis for each proposal is provided following Table 1.

Table 1: List of recommended NZ ETS regulatory updates

| Proposed change | Regulations | Reason for change | Summary of consultation feedback |
|--|---|---|---|
| Repeal Regulation 11D to remove an accounting transaction which relates to voluntary emissions offsetting activity during the Kyoto Protocol commitment periods (2008–12 and 2013–20 inclusive). | Climate Change (Unit Register) Regulations 2008 | Regulation 11D supported claims related to pre-2021 voluntary carbon offsetting, which required offset projects to be accounted for against New Zealand's Kyoto Protocol-related targets. The Ministry has produced new guidance that makes this regulation redundant. | Feedback for this proposal was supported by submitters. |
| Change the regulations to remove the criteria for registering as a participant in relation to specific potent greenhouse gas removal activities. | Climate Change (Other Removal Activities) Regulations 2009 | Updating these regulations removes barriers to entry for this removal activity. This could increase the number of people that register to participate in the NZ ETS for storing or destroying specific potent greenhouse gases and increase the amount of gases that are exported or destroyed. | Mixed feedback from stakeholders. Two key themes emerged: there are current barriers to registering for the activity in the NZ ETS; and there is concern for the interaction between the proposed change and any future regulated product stewardship scheme for these refrigerant gases. |
| Update the default emissions factors for natural gas to reflect updated data. | Climate Change (Stationary Energy and Industrial Processes) Regulation 2009 | Maintain accuracy and minimise administrative costs to participants. | Submitters were supportive of updating the reference data to ensure accuracy. |
| Update waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection and destruction | Climate Change (Unique Emissions Factors) Regulations 2009 | Maintain accuracy and avoid administrative costs for participants. | This proposal was consulted on in 2021. Submitters were supportive of the proposal. The change is to correct an oversight, which requires renewed cabinet approval. |

Removing the regulation allowing conversion of NZUs to Kyoto Protocol era emission units for cancellation

- 17 Regulation 11D of the Climate Change (Unit Register Regulations) 2008 permits holders of NZUs to convert these to AAUs for cancellation. The purpose of the regulation was to support claims related to pre-2021 voluntary carbon offsetting, which required offset projects to be accounted for against New Zealand's Kyoto Protocol-related targets.
- 18 The Ministry publishes guidance on offsetting activities in the voluntary carbon market. Previous guidance recommended cancelling AAUs as a means of accounting for voluntary offsets against New Zealand's international targets under the Kyoto Protocol. Regulation 11D of the Unit Register Regulations requires the Registrar to give effect to this cancellation process.

- 19 The Ministry has since published interim guidance that no longer recommends the use of conversion of NZUs to AAUs for carbon offsetting [ENV-22-MIN-0005 refers]. The cancellation process under regulation 11D is now redundant. How the voluntary carbon market will operate in the Paris Agreement era is still developing, and the Ministry will update guidance in line with international best practice as needed.
- 20 Submissions which addressed this proposal were supportive. There was broad recognition that removing redundant regulation is sensible.
- 21 I propose regulation 11D of the Unit Register Regulations be repealed for reasons of redundancy. Repealing 11D will ensure regulations are in line with the Ministry's guidance and current practice in the voluntary carbon market. Stakeholders are expecting this change.

Remove eligibility criteria to register as an NZ ETS Participant for exporting or destroying refrigerant greenhouse gases

- 22 NZ ETS participants can receive NZUs for exporting or destroying hydrofluorocarbons (HFCs) or perfluorocarbons (PFCs). To be eligible to receive NZUs, one of two criteria under the Climate Change (Other Removal Activities) Regulations 2009 must be met:
- 22.1 A person must be a manager of a Product Stewardship (PS) scheme accredited under the Waste Minimisation Act 2008; or
- 22.2 The HFCs or PFCs which are exported or destroyed must have been imported into New Zealand on or after 1 January 2013.
- 23 I recommend removing these two eligibility criteria for HFCs and PFCs. These criteria could be acting as a barrier to increasing the collection of potent greenhouse gases for export or destruction and potential investment in recycling and destruction facilities in New Zealand.
- 24 Given the increase in emission unit prices and the value of these gases, there is greater public interest in this removal activity.
- 25 The regulation restricting the import dates of HFCs and PFCs as a removal activity eligible for NZUs was introduced to prevent an arbitrage opportunity. It prevented a person from importing and stockpiling synthetic greenhouse gases prior to 2013, then receiving emission NZUs for exporting those gases after 1 January 2013. The Ministry assesses this arbitrage opportunity no longer exists.
- 26 There are significant differences in stakeholder opinions about the proposal. Feedback in favour of the proposed change came from industry stakeholders that see the current settings as a barrier to innovation in this area.
- 27 Submissions suggested that if the criteria were removed from regulations there would be an increase in collecting refrigerants for destruction or export, and therefore a decrease in reported emissions in New Zealand.

- 28 There was concern regarding the intentions of refrigerant exporters. Some submitters proposed that exporters should only be eligible to earn NZUs if they had evidence of destruction. This would prevent any possibility of dumping or increasing the emissions of another country.
- 29 Participants registering for the activity would have to submit documentation to the Environmental Protection Agency (EPA) to collect NZUs. Participants would also need to apply for export permits from the EPA and be subject to the Ozone Layer Protection Act and Regulations 1996. The EPA also monitors compliance of participants in the NZ ETS.
- 30 I do not agree that restriction should be imposed. There is potential for the exported refrigerants to be recycled offshore, reducing the global need for new refrigerants, and providing an economic opportunity that may increase the collection of refrigerants here. Such a restriction would also have unintended consequences given some businesses are international refrigerant exporters.
- 31 Stakeholders opposing the proposal were concerned about impacts of removing the requirement for an accredited project stewardship manager to undertake the activity. The Waste Minimisation Act 2008 [ENV-20-MIN-0024 refers] requires HFCs and PFCs to be managed over their lifecycle by a regulated PS scheme.
- 32 The Government's emissions reduction plan (ERP) also includes reference to a proposed regulated PS scheme for HFCs and PFCs. There is concern that removing the current eligibility criteria could undermine the implementation of a regulated scheme.
- 33 The Refrigerant Recovery Trust (the Trust) presently manages a voluntary stewardship scheme and is opposed to the removal of the eligibility criteria. They, and some other related parties, propose that a future regulated scheme should be funded by NZUs generated from export or destruction of SGGs. The Trust argues that the proposal undermines its ability to do this in the future, and it would need to rely on an industry levy instead.
- 34 Monopolising the economic benefits of the activity in the way proposed by the Trust is inappropriate. It is not conclusive there would be increased collection of gases compared to the recommended regulation change.
- 35 No other proposed regulated PS seeks to control such an economic resource this way, as they are all funded through a levy on manufacture or import. There may be some economies of scale advantages through monopolising, but these could also be realised through commercial agreements outside the NZ ETS and PS regulations.
- 36 The NZ ETS regulation change can co-exist with a refrigerant PS scheme. It simply increases the number of persons collecting end of life refrigerants and who will also have participation and reporting requirements under PS regulations.

- 37 I recommend updating the Climate Change (Other Removal Activities) Regulations 2009 to remove these eligibility criteria. These criteria are acting as barriers to increasing the collection of potent greenhouse gases for export or destruction.

Update the schedule of default emissions factors for natural gas fields

- 38 Emissions factors are an important part of the NZ ETS and are used by participants to calculate emissions and removals from their activities. The default emissions factors (DEFs) for mining or purchasing natural gas are published in a schedule to the Climate Change (Stationary Energy and Industrial Processes) Regulations 2009 for each gas field.
- 39 Feedback was in support of updating natural gas DEFs to improve their accuracy for emissions returns. Some submitters provided additional comment related to fugitive emissions from natural gas, which were out of scope for this proposed regulatory change.
- 40 I propose to update the schedule of gas fields and their emissions factors. Natural gas emissions factors need to be regularly updated and added to regulations so emissions calculations for NZ ETS obligations are accurate.

Updating waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection and destruction

- 41 Participants in the NZ ETS calculate their emissions based on emissions factors prescribed in regulations. The Climate Change (Unique Emissions Factors) Regulations 2009 (UEF Regulations) provide the ability to apply for the use of unique emissions factors that vary from the DEF for the activity.
- 42 The Ministry consulted on and updated the emissions factor for waste going to landfill in 2021 to reflect changes in waste composition. However, updated waste composition data were not incorporated into the UEF regulations, where they are used in the calculation of UEFs for waste disposal.
- 43 This omission affects landfill participants wishing to apply for UEFs used to calculate 2022 emissions reported in emissions returns due to be submitted in 2023.
- 44 I propose to update Schedule 3 of the Climate Change (Unique Emissions Factors) Regulations 2009 to correct this omission to ensure participants can apply for accurate UEFs and provide accurate emissions returns for 2022 calendar year activity.

The role of the NZ ETS, the emissions reduction plan and other NZ ETS policy areas

- 45 New Zealand's first ERP was released on 16 May 2022. The plan sets out coherent measures that are complementary and reinforcing to describe how we are going to meet emissions budgets and progress towards our 2050 target. Emissions pricing through the NZ ETS is a key part of the policy package.

- 46 Policy decisions relating to the proposals in this document did not impact the development of the ERP. Other areas of policy work related to the NZ ETS such as forestry and market governance remain out of scope and will not be affected by the proposals outlined in this paper.

Legislative Implications

- 47 Regulatory amendments will be required to implement the proposals. The following regulations will need to be amended:

47.1 Climate Change (Unit Register) Regulations 2008

47.2 Climate Change (Other Removal Activities) Regulations 2009

47.3 Climate Change (Stationary Energy and Industrial Processes) Regulations 2009

47.4 Climate Change (Unique Emissions Factors) Regulations 2009

Financial Implications

- 48 There are financial implications associated with the Climate Change (Other Removal Activities) Regulations 2009 proposal. The fiscal impacts of any increase in removals reported into the NZ ETS and the associated allocation of NZUs to participants are expected to be low. Increased removal activity will fall within existing appropriations and are minor compared to other NZ ETS entitlements.
- 49 The Trust is currently the only eligible person who can receive NZUs for the export of pre-2013 imported SGG in bulk. It received 36,372 NZUs for 2020 removals (valued at \$2.8m NZD based on NZU prices of \$75.00).¹
- 50 The Trust will likely perform the bulk of removal activities in the near future due to having established physical assets and relationships (informal or commercial) with service agents.
- 51 There is a low probability of the amount of removals doubling or exceeding level maintained under current appropriations. As this change was not signalled in advance to the industry (beyond the consultation period), people are unlikely to have stockpiled gas to take advantage of it. We note that some of the removals that would be reported by newly eligible participants may have otherwise been reported by the current participant.

¹ Normalised amount per NZU. Actual price applied to NZUs at the time of emission return submission not accounted for.

Te Tiriti o Waitangi Implications

- 52 Māori have a significant interest in climate change action and the NZ ETS, particularly in the forestry sector. There are no direct Te Tiriti o Waitangi implications from the proposals in this paper.
- 53 I am satisfied under section 3A of the Act, that iwi and Māori interested in NZ ETS regulations have had the opportunity to provide feedback on the changes.

Impact Analysis

Regulatory Impact Statement

- 54 The Ministry's Regulatory Impact Analysis Panel has reviewed the Impact Statement: Updating the Climate Change (Other Removal Activities) Regulations 2009. The panel considers that it meets the quality assessment criteria necessary for Ministers to make informed decisions on the proposals in this paper.

Climate Implications of Policy Assessment

- 55 The Ministry has been consulted and confirm that the CIPA requirements do not apply to these changes as the threshold for significance is not met.

Population Implications

- 56 There are no immediate gender or disability implications from the recommendations in this paper.

Human Rights

- 57 The recommendations in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Consultation

- 58 The Ministry published a discussion document for public consultation on three of the proposed changes to regulations on 17 March through to 28 April 2022. The fourth proposal on updating waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection and destruction was consulted on in 2021.
- 59 Twenty-nine submissions were received for the 2022 consultation. Submitters ranged from individuals through to large companies and non-governmental organisations. There were 32 submissions in 2021.
- 60 The Treasury, Ministry of Foreign Affairs and Trade, Ministry for Primary Industries, Ministry for Business, Innovation and Employment, Environmental Protection Authority, the New Zealand Customs Service, and the Ministry of Transport were consulted on this paper. The Department of Prime Minister and

Cabinet, and Te Puni Kōkiri were informed. Where feedback has been received, it has been considered and incorporated as appropriate.

Communications

- 61 Announcements about the NZ ETS need to be managed carefully to avoid any inconsistencies and market risks, including sudden NZU price changes in the NZ ETS secondary market. Information should not be disseminated in a way that advantages some market participants over others and compromises NZ ETS investments.
- 62 No communications material is required for the proposals in this paper. Officials will continue to engage with the Trust on the interactions of the NZ ETS with the PS scheme.

Proactive Release

- 63 I propose to proactively release this paper on the Ministry's website, subject to redactions as appropriate under the Official Information Act 1982.

Recommendations

The Minister of Climate Change recommends that the Committee:

- 1 **note** that in March and April 2022 the Ministry for the Environment (the Ministry) undertook public consultation on the following proposed updates to the New Zealand Emissions Trading Scheme (NZ ETS):
 - 1.1 Removing a redundant regulation allowing New Zealand Units (NZU) to be converted to Kyoto Protocol Assigned Amount Units which are then cancelled
 - 1.2 Removing regulatory barriers to NZ ETS incentives for collection of synthetic greenhouse gases for export or destruction
 - 1.3 Updating the schedule of default emissions factors for natural gas fields to maintain accuracy and minimise administrative cost to participants.
- 2 **note** that in 2021 the Ministry undertook public consultation on the following proposed update to the NZ ETS which is proposed as a part of the 2022 updates:
 - 2.1 Updating waste composition data used in calculating waste emissions. Due to an oversight, the corresponding update to unique emissions factors for waste disposal did not occur.

Removing the regulation allowing cancelling of Kyoto Protocol era emission units

- 3 **note** that regulation 11D of the Climate Change (Unit Register) Regulations 2008 is now redundant.

- 4 **note** there was broad support among consultation respondents for repealing this regulation.
- 5 **agree** to repeal Regulation 11D in Climate Change (Unit Register) Regulations 2008.

Removing regulatory barriers to encourage greater collection of synthetic greenhouse gases for export or destruction

- 6 **note** the criteria in the Climate Change (Other Removal Activities) Regulations 2009 allow persons exporting or destroying hydrofluorocarbons (HFCs) or perfluorocarbons (PFCs) and who meet eligibility criteria to register as an NZ ETS participant and receive NZUs for this activity.
- 7 **note** removing this barrier would allow innovation and investment into recycling and destruction facilities to occur and would result emission reductions in New Zealand.
- 8 **note** divergence in stakeholder opinions on this proposed change.
- 9 **agree** to remove eligibility criteria from Regulation 22 of the Climate Change (Other Removal Activities) Regulations 2009.

Updating the schedule of default emissions factors for natural gas fields

- 10 **note** that emissions factors for natural gas fields need to be updated to align with the most recent natural gas composition data.
- 11 **agree** that Schedule 2 Table 10 of the Climate Change (Stationary Energy and Industrial Processes) Regulations 2009 be updated with emissions factors and classes based on 2021 calendar year data.

Updating waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection

- 12 **note** there was an omission in the implementation of regulations consulted on in 2021.
- 13 **agree** to correct this omission by updating waste composition data in schedule 3 of the Climate Change (Unique Emissions Factor) Regulations 2009 to the values consulted on in 2021.

Drafting instructions

- 14 **authorise** the Minister of Climate Change to further clarify and develop policy matters relating to the amendments recommended above, in a way consistent with Cabinet's decisions.
- 15 **invite** the Minister of Climate Change to issue drafting instructions to Parliamentary Counsel Office to promulgate amendment regulations by 26 September 2022 for the decisions in this paper:

- 15.1 removing a redundant regulation allowing NZUs to be exchanged for Kyoto Protocol Assigned Amount Units which are then cancelled.
- 15.2 removing regulatory barriers to encourage greater collection of synthetic greenhouse gases for export or destruction.
- 15.3 *updating the default emissions factors for waste and* natural gas fields to maintain accuracy and minimise administrative cost to participants.
- 15.4 *updating* waste composition data used in calculating unique emissions factors for waste disposal in relation to landfill gas collection to maintain accuracy and minimise administrative cost to participants.

Authorised for lodgement

Hon James Shaw

Minister of Climate Change

**Appendix 1: Regulatory impact assessment - Updating the Climate Change
(Other Removal Activities) Regulations 2009**

Proactively released