

CARBON MARKET BUSINESS BRIEF

NEW ZEALAND

NZ ETS AT A GLANCE

Years in operation	Began in 2008. Annual compliance periods, with units due to be surrendered by 31 May of the subsequent year.
Overall cap & trajectory	<p>As of September 2021, the overall limit in the NZ ETS was 193.8 million units over 2021-2026, of which 106.4 million was for auctioning and 41.5 million for the cost containment reserve (calculated using AR4 GWPs). The balance represents anticipated industrial free allocation (45.9 million units), which is not bound by the overall limit. The longer-term trajectory will be shaped by economy-wide budgets for domestic net emissions.</p> <p>Emissions budgets for 2022-35 will be announced by the government in May 2022. In October 2021, the government announced in-principle emissions budgets of 292 million tCO₂e over 2022-25, 307 MtCO₂e over 2026-30, and 242 MtCO₂e over 2031-35 (calculated using AR5 GWPs). By law, the government can adjust previously announced NZ ETS unit settings when new emissions budgets are announced.</p>
Target(s)	<p>Revised NDC target for a net 50% reduction compared with 2005 gross emissions by 2030.</p> <p>The country has legislated for a 2050 target of at least a 24-47% cut in biogenic methane below 2017 levels (including a 10% cut by 2030) and net-zero emissions of other GHGs.</p>
Emissions Reduced to date	Pre-pandemic, the NZ ETS was projected to reduce net 2020 emissions by 2.9 MtCO ₂ e (annually).
Sectors covered	<ul style="list-style-type: none"> • Forestry (mandatory for deforestation of pre-1990 forest land; voluntary for post-1989 afforestation) • Liquid fossil fuels • Stationary energy • Industrial processes • Waste • Agriculture (reporting only) <p>Under legislation passed in June 2020, agriculture will face an emission price no later than 2025, and a voluntary permanent forestry activity for post-1989 forests will be introduced in 2023.</p>
GHGs covered	CO ₂ , methane, HFCs, N ₂ O, PFCs and SF ₆
# of covered entities	As of June 2021, there were 200 mandatory participants, plus 77 agricultural processor entities with reporting obligations only and 2198 voluntary participants (of which 2169 conduct post-1989 forestry).

Allocation method	<p>Output-based free allocation to emissions-intensive, trade-exposed (EITE) industry. Historically, one-off free allocations to fishing quota owners and pre-1990 forest owners. Post-1989 forest owners (or lease/rights holders) can opt to earn units for net removals.</p> <p>Quarterly auctions were introduced in 2021, hosted by NZX and EEX. A total of 19.3 million NZUs are being auctioned in 2022 (excluding reserve units).</p>
Trading rules	Unlimited banking and no borrowing
Use of offsets and linking	At present, no overseas units are eligible and any future use of approved overseas units by participants will be bound by the overall limit. The NZ ETS is not linked to systems in other jurisdictions. Two domestic unit mechanisms (Permanent Forest Sink Initiative and Negotiated Greenhouse Agreements) will end before 2024.
Other features	<p>Reforms adopted in 2020 established a cost containment reserve (CCR) and an auction reserve price (ARP). The CCR will release a fixed volume of NZUs into auctions if the unit price reaches a trigger price, set at NZ\$70/t in 2022 and rising 12% annually (including inflation). The ARP for 2022 is NZ\$30/t and rises 7% annually (including inflation).</p> <p>In March 2021, the government introduced a Confidential Reserve Price to operate in addition to the ARP. This is set by the Minister based on prevailing prices in the secondary market. Price control settings may be revised after new emissions budgets are announced in May 2022.</p> <p>In the energy sector, surrender obligations generally apply upstream at the point of fuel production or import, but large fuel users can opt in to surrender obligations with a carve-out of the upstream obligation.</p>
Penalties for non-compliance	Three times the market price plus the surrender requirement for failing to submit allowances on time. Adjusted penalties will apply for other types of infringements.
Use of revenues	In 2021, the government announced that from 2022, ETS auction revenue will be directed to a Climate Emergency Response Fund to support emissions reductions initiatives under the government's Emissions Reduction Plan.

MAJOR DEVELOPMENTS

At the end of May 2021, the independent Climate Change Commission presented the government with its final recommendations for New Zealand's first three emissions budgets (out to 2035) and specific guidance for its Emissions Reduction Plan covering 2022-25. The Commission recommended that for meeting emissions budgets, offshore mitigation should only be used in exceptional circumstances. This does not preclude the use of offshore mitigation to help bridge the gap between emissions budgets and New Zealand's 2030 NDC. The Commission recommended aligning NZ ETS unit supply and price control settings with emissions budgets, strengthening the market governance regime, reviewing the phase-out of industrial free allocation, clarifying the treatment of voluntary mitigation, and managing the amount of exotic forest planting driven by the NZ ETS to strengthen incentives for gross emissions reductions.

From July to September 2021, the government consulted on improvements to industrial free allocation and market governance. In October and November 2021, the government consulted on its first Emissions Reduction Plan, which was informed by the Commission's recommendations. The final plan will be announced in May 2022.

Also informed by the Commission's advice, the government in October 2021 increased its emissions reduction target under the Paris Agreement to a 50% cut in net GHG emissions by 2030, compared with 2005 gross emissions. The forthcoming Emissions Reduction Plan will set out how this target will be met across all sectors.

Further changes to the NZ ETS are under consideration in 2022. For example:

- Revised forestry regulations are anticipated in 2022 to support legislated changes taking effect from 2023. From March to April 2022, the government consulted on proposals to limit exotic planting under the new permanent post-1989 forestry activity being implemented from 2023, adjust averaging accounting for remote and marginal post-1989 forests, and improve incentives for indigenous afforestation.
- The Minister of Climate Change and Minister of Agriculture must report back to Cabinet by the end of 2022 on a pricing system for farm-level emissions as an alternative to the NZ ETS. He Waka Eke Noa, the Primary Sector Climate Change Partnership, consulted on design proposals from February to March 2022 and will submit its recommendations to the government in May 2022. The Climate Change Commission will submit advice to the government by May 2022 on potential assistance to the agriculture sector under an alternative pricing system, and by June 2022 on the sector’s progress with preparing for emissions pricing relative to its legislated commitments.
- When regulations for the 2027 extension to NZ ETS unit supply and price management settings are announced in 2022, the government has the option to revise previously announced settings for 2023-2026. The Climate Change Commission is tasked with advising the government on those settings before decisions are made.

MARKET COMMENTARY

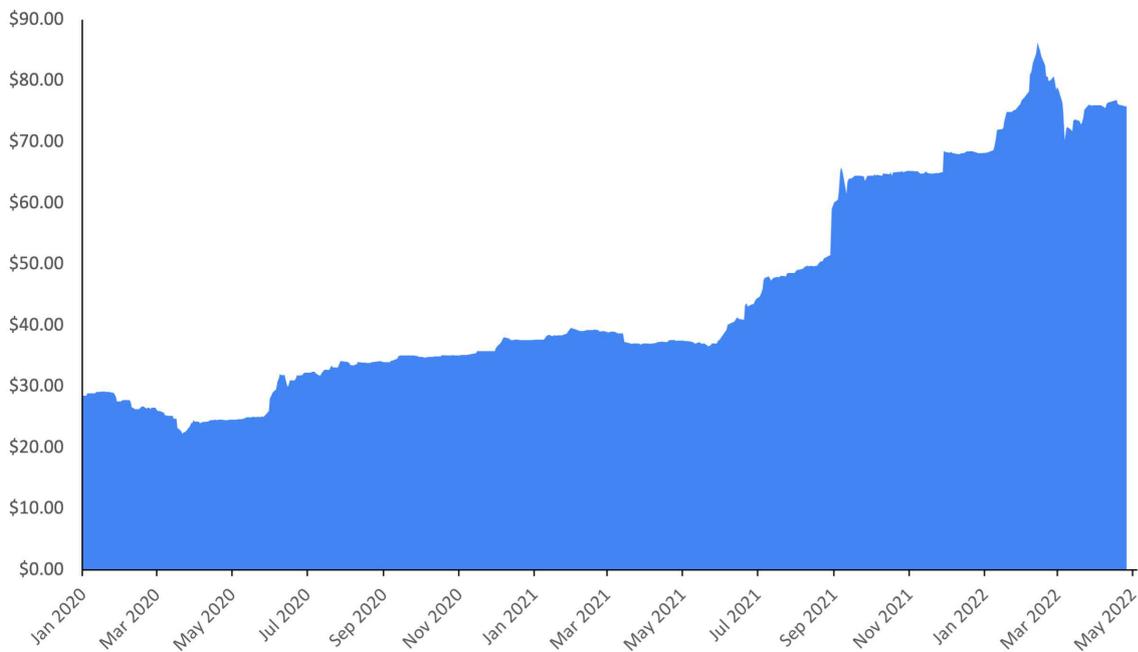


FIGURE 1
Spot NZU prices
Source: Jarden

Like many other emissions trading systems, the NZ ETS traded up to record highs in 2021, and continued in the first four months of 2022. Spot NZUs peaked just above NZ\$85 in early 2022 and had settled into the NZ\$70-75 range throughout April – up 200% since April 2020, and more than double the NZ\$35 level of April 2021.

One of the main drivers has been the removal of the so-called fixed price option for compliance from the 2021 calendar year. Previously, emitters could either purchase and surrender NZUs or pay a fixed price per tonne of emissions (set at NZ\$35 for the 2020 compliance year). Its removal coincided with the first year that the NZ ETS also featured a cap on emissions, and the appearance of new players in the market.

Settlement prices at the quarterly auctions over the past year have reflected the ascent of NZU prices, with the most recent auction in March 2022 clearing at NZ\$70. All 4.8 million NZUs on offer were sold, as well as 5.7 million of the 7 million units in the cost containment reserve.

USEFUL LINKS

[New Zealand Emissions Trading Register](#)

[New Zealand Climate Change Commission](#)

[Climate Change Response Act 2002](#)

[Climate Change Response \(Emissions Trading Reform\) Amendment Bill](#)

[NZ ETS Auctions](#)

REFERENCES

[New Zealand Emissions Trading Scheme](#) – Ministry for the Environment

[Overview of the New Zealand Emissions Trading Scheme Reforms](#) – Ministry for the Environment

[Climate Change \(Auctions, Limits, and Price Controls for Units\) Regulations 2020](#)

[Guide to the New Zealand Emissions Trading Scheme – March 2022 update](#) – Motu Economic and Public Policy Research

[Ināia tonu nei: a low emissions future for Aotearoa](#) – Climate Change Commission

[Press release: Budget 2022 to boost health and climate action](#) – 15 December 2021

REFERENCES

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