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ETS Consultation
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Submission on the Proposed Improvements to the New Zealand Emissions Trading Scheme

Introduction

1. This is Vector Limited's (Vector) submission on the Ministry for the Environment's (MfE) consultation document, *Improvements to the New Zealand Emissions Trading Scheme*, published in August 2018.
2. Vector generally supports MfE's proposed improvements to the New Zealand Emissions Trading Scheme (NZ ETS or the Scheme), which would help facilitate New Zealand's transition to a net zero emissions economy.
3. Sustainability is at the heart of Vector's vision of *creating a new energy future*. We support the Government's proposed introduction of a *Zero Carbon Bill*, which provides the context for the proposals in this consultation. We further support the creation of an independent Climate Change Commission that would provide advice on future emissions budgets and other key climate change issues.
4. As a leading technology solutions company, Vector is well placed to help New Zealand on its journey to a low emissions economy by introducing new technologies that drive emissions reduction and promote the use of renewable energy. We are committed to an ambitious target of achieving net zero emissions by 2030 for our own operations.
5. We set out below our responses to consultation questions that are of interest to Vector businesses and of significance to achieving our company's net zero emissions target.
6. No part of this submission is confidential. Vector's contact person for this submission is:

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Responses to selected consultation questions

Coordinating unit supply decisions

Q1: *What issues should the decision maker consider when making unit supply decisions?*

- *proper functioning of the ETS*
- *NZ's projected emission trends*
- *number of NZUs expected to be allocated*
- *emissions covered by the ETS*

- *arrangements that govern the operation of the ETS*
- *any limit on international units*
- *emissions budgets, such as those proposed in the Zero Carbon Bill*
- *recommendations from the Independent Climate Change Commission proposed in the Zero Carbon Bill*
- *agreements or arrangements regarding international emissions reductions*
- *non-ETS climate change mitigation policies*
- *modelling of New Zealand's domestic abatement potential and costs*
- *forestry reporting periods*
- *forecasts of international carbon prices*
- *inflation rates*
- *other (please explain).*

7. In Vector's view, the decision maker should consider all of the above issues when making unit supply decisions except for inflation rates. It is reasonable to assume that the general level of prices is already factored into government economic forecasts and by NZ ETS participants in their trading decisions, and is reflected in carbon price trends.
8. The decision maker can also consider other factors such as the following:
 - ongoing competitiveness of New Zealand businesses;
 - risk of carbon leakage; and
 - level of action taken by New Zealand's international trading partners and competitors.

Q2: *What, if any, restrictions should be placed on the NZ ETS decision maker when making unit supply decisions? (For example, currently one year's notice must be given for changes to unit supply volumes.)*

9. Vector believes that NZ ETS participants should be given at least a year's notice prior to the implementation of any unit supply decisions. This would provide Scheme participants greater certainty and transparency, enabling them to make more informed business decisions.
10. We suggest that any decision should be implemented at the start of a compliance year, and not changed mid-way through. We support a 'no surprises' policy to ensure disruption is minimised not only for businesses but also for consumers, and ensure a smooth transition to any new arrangements.
11. We further suggest that the announcement date of any decision be pre-determined, and form part of a published calendar of NZ ETS related decisions.

Auctioning

Q3: *Do you agree with the proposal to implement a single-round, sealed bid auction format with uniform pricing? If not, why not?*

12. Yes, Vector agrees with the proposed implementation of a single-round, sealed bid auction format with uniform pricing. We support a simple auction design, at least during the initial years of auctioning. We note that the secondary market already provides a mechanism for price discovery, to some extent.
13. We suggest that MfE or the entity conducting the auction publish clear guidance on the design, timing and content of the auction prior to auction day.
14. The details of the auction results should also be published in a timely manner.

Q4: *Do you think that auctioning frequency should be:*

- weekly (not preferred)
- monthly
- quarterly
- annually (not preferred).

15. Vector prefers that auctions be held quarterly. This will provide auction participants (including potential participants) and the market sufficient time to 'digest' the results of previous auctions, and make more informed decisions about forthcoming auctions.

Q5: *Do you agree with the proposal that all NZ ETR account holders should be able to participate at auction? If not, why not?*

16. Yes, Vector agrees that all NZ ETR account holders should be able to participate at auctions. This will promote greater market participation and liquidity, and provide greater choice to more parties on how they can best manage and reduce their emissions.
17. To maintain the integrity of the auctions, we suggest that penalties be imposed on parties defaulting on settlement.

Q6: *Do you agree that the Government should use the proceeds gained from the auctioning of NZUs for specific purposes? If so, please explain what those purposes would be.*

18. No, Vector considers it more effective for the Government's emissions reduction priorities to be funded out of the regular budget process. This would encourage businesses to focus on the most efficient and effective ways of reducing their emissions, rather than on lobbying government agencies for potentially tiny sums of money.

Price ceiling

Q7: *Do you agree with the proposal to replace the \$25 fixed priced option with a cost containment reserve price ceiling implemented through the auctioning mechanism? If not, why not?*

19. Yes, Vector agrees with the replacement of the \$25 fixed price option with a cost containment reserve price ceiling implemented through the auctioning mechanism.

Q8: *How do you think the price level and number of units in the cost containment reserve should be managed over time? (Note: specific settings will be consulted on later.) Select all that apply.*

- decision maker has discretion to determine the settings while having regard to certain factors (please explain)
- settings are determined by mandated formulae (please explain)
- other (please explain).

20. Vector believes a combination of 1) the decision maker having discretion to determine settings and 2) some settings being determined by mandated formulae to be appropriate.
21. The decision maker can have discretion in the case of unforeseen events. We suggest the development of clear guidelines around the boundaries of any discretionary mandate.
22. Some elements around pricing could be set using mandated formulae, particularly for the longer term as Scheme participants become more familiar with the auction process. A formulaic approach for some settings could be used to ensure that New Zealand carbon prices are kept in line with international prices.

Q9: *What actions should occur if the price ceiling is struck? (Select all that apply.)*

- *increase the price ceiling trigger level, if it was set on a too low or erroneous basis*
- *increase the limit on international units, if high domestic abatement costs are the cause of the excessively high prices*
- *undertake a fuller system review, if the high prices are seen as a sign of wider market dysfunction*
- *government buying international units to compensate for additional units added to the market through the price ceiling*
- *adjust the overall cap*
- *other (please explain).*

23. All of the above actions (except “other”) should be considered if the price ceiling is struck. There should be transparency around the conditions that would trigger any of the above actions to be undertaken.

Q10: *Do you agree with the proposal to review the price ceiling if another significant event occurs (such as a decision to link the NZ ETS with another carbon market)?*

24. Yes, Vector agrees that the price ceiling should be reviewed if another significant event occurs. This would avoid adverse arbitrage risks, e.g. in the case where the NZ ETS is linked with another trading scheme.
25. We suggest that the market be given adequate notice prior to the implementation of any review decision. We consider at least one compliance year’s notice to be appropriate.

Q11: *Do you agree that the \$25 FPO may not be appropriate for the short term, and may need to be adjusted before 2020? Please explain.*

26. No, it is Vector’s view that the \$25 FPO should remain in place until auctioning commences. This would provide certainty for Scheme participants, quell speculations or expectations around price levels, and maintain market stability.
27. To ensure certainty and minimise market disruption, we believe there should be no changes for the current surrender year, at the very least.

Limiting the use of international units

Q12: *Which mode of purchase for international units (direct or indirect) would be the best approach for the NZ ETS, acknowledging that there are other significant factors that will influence this decision? Please explain.*

28. Vector considers direct purchase to be a better approach for the NZ ETS once linking with other trading schemes is established. This approach would encourage greater participation in the Scheme, facilitate the discovery of international carbon prices, and enable participants to make more informed trading decisions.
29. We agree with the view that international units must meet high standards of environmental integrity. We believe there are opportunities to broaden the purpose of accessing international units to encompass social benefits. For example, the contribution of units to sustainable development, in line with the United Nations Sustainable Development Goals, can be taken into consideration.

Q13: If NZ ETS participants are able to purchase and surrender international units directly, do you think that there is justification for varying the percentage of allowable international units by participant type? If not, why not?

30. No, varying the percentage of allowable international units by participant type reduces participants' flexibility around making decisions on how they can most efficiently and effectively reduce their emissions over time, e.g. shifting to a new technology vs purchasing carbon units.
31. Some emissions intensive, trade exposed (EITE) entities do not have direct surrender obligations. It is unclear how the above restriction could be applied equitably across EITE firms.
32. Consistent with the policy intent of aligning New Zealand carbon prices with international prices, not specifying allowable international units by participant type would minimise any arbitrage opportunities.

Market governance

Q18: For each of the seven areas that we have identified as being sources of potential risk, what is your assessment of the level of risk that they create, both now and in the future? Please provide examples or evidence if possible.

- inadequate, false or misleading advice
- a lack of transparency, monitoring and oversight for trades
- risks of manipulation of the NZU price
- insider trading
- money laundering risks
- credit and counterparty risks
- potential conflicts of interest
- other (please explain).

33. Vector believes all of the above (except "other") pose both current and future risks for the NZ ETS. We generally agree with the consultation document's analysis why these actions or areas could put the integrity of the Scheme at risk.

Market information

Q19: Do you think that there would be benefits from publishing individual emissions data reported by NZ ETS participants? (Please explain.)

34. Yes, Vector would welcome greater transparency around emissions data, subject to commercial sensitivity considerations and the appropriate privacy and security settings.

Q20: Do you think cases of non-compliance should be published? (Please explain.)

35. Yes, but only non-compliance that results in criminal prosecution should be published.
36. In addition, the Environmental Protection Authority (EPA) could publish non-attributable case studies of non-compliance to increase participants' awareness of the Scheme's requirements and penalties for non-compliance.

Q21: How would publishing these types of information affect you?

37. Vector already discloses information required by New Zealand regulators in relation to its greenhouse gas emissions under the *Climate Change Response Act 2002*.

38. We believe that greater transparency enables parties to make more informed decisions relating to the NZ ETS, and on how they can best improve resilience for their businesses and communities. It provides a 'level playing field' for all parties, encouraging greater access to, and participation in, the NZ ETS.

Compliance and penalties

Q22: Do you agree with the proposal to introduce strict liability infringement offences for low-level non-compliance? If not, why not?

39. Yes, consistent with the principles of proportionality and effectiveness, Vector considers the introduction of strict liability infringement offences to be more appropriate than the use of criminal offences for low-level compliance.

Q23: What are your views on the levels of the proposed fines?

40. In Vector's view, the levels of fines and detection system should be considered together.

Q24: Has the excess emissions penalty for failing to surrender or repay units by the due date caused issues for you? If so, please explain.

41. No, excess emissions penalty for failing to surrender or repay units by the due date has not been an issue for Vector.

Q25: Should the excess emissions penalty for failing to surrender or repay units by the due date be changed? If so, please explain.

42. No, Vector believes the existing arrangements work.
43. We consider the \$30 penalty to be sufficient to deter non-surrender of units, at least at this stage.

Q26: What option do you see as most appropriate for the excess emissions penalty?

- set the penalty at a fixed dollar value and remove the ability to reduce the penalty
- use a proportional approach where the penalty is a percentage of the outstanding surrender obligation
- other (please explain).

44. Vector considers a proportional approach to be appropriate for the excess emissions penalty.

Technical and operational improvements

Q31: Do you agree with the proposal that the Government should be able to amend UEFs from previous years? If not, why not?

45. Yes, the Government should be able to amend Unique Emissions Factors (UEFs) from previous years but within a limited period and with no penalties (or subject to a threshold), unless deliberate acts of deceit have occurred.
46. Vector understands that the setting of UEFs is verified by an EPA recognised verifier. An 'unlimited' retrospective approach would appear to be draconian in this circumstance.

Q34: Do you agree with the proposal that the deadline for surrenders and repayments is 60 working days from the date a notice is sent? If not, why not?

47. Yes, Vector agrees with the proposed deadline for surrenders and repayments of 60 working days from the date a notice is sent.

Q36: Do you agree with the proposal that account operators continue to operate NZ ETS accounts until a succession plan is in place. If not, why not?

48. Yes, Vector agrees that account operators should be able to continue to operate NZ ETS accounts until a succession plan is in place.

Q37: Do you agree with the proposal that units should vest in the Crown if the account operator chooses to close the account? If not, why not?

49. Yes, Vector agrees that units should vest in the Crown if the account operator chooses to close the account.

Concluding comment

50. We are happy to discuss with MfE officials any aspects of this submission, and share insights from our initiatives that contribute to achieving a net zero emissions future.

Yours sincerely
For and on behalf of Vector Limited



Richard Sharp
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