Vector Limited
101 Carlton Gore Road
PO Box 99882, Newmarket
Auckland 1149, New Zealand
www.vector.co.nz
Corporate Telephone
+64-9-978 7788
Corporate Facsimile
+64-9-978 7799

10 September 2012

Finance and Expenditure Select Committee
Parliament Buildings
WELLINGTON 6011

Submission on the Climate Change Response Amendment Bill

Introduction

1. Vector Limited ("Vector") welcomes the opportunity to make this submission on the Climate Change Response (Emissions Trading and Other Matters) Amendment Bill ("the Bill"), introduced to Parliament on 20 August 2012.

2. No part of this submission is confidential and Vector is happy for it to be made publicly available.

3. Vector's contact person for this submission is:

   Luz Rose
   Senior Regulatory Analyst
   04 803 9051
   Luz.Rose@vector.co.nz

Promoting efficient markets

4. As a matter of principle, Vector supports the efficient operation of markets in the energy sector, including the New Zealand Emissions Trading Scheme ("ETS").[1] Efficient markets enable participants to find the least-cost opportunities for the abatement of greenhouse gas emissions, and importantly, provide the right incentives for investment.[2] This is consistent with the Government's objectives set out in the Bill, in particular, to "ensure that the ETS more effectively supports the Government's economic growth priorities" and "improve the operation and administration of the ETS".

[1] http://www.vector.co.nz/sites/vector.co.nz/files/Vector%20Submission%20ETS%20Amendments.pdf, paragraph 3
[2] Ibid.

5. This submission focuses on the following proposed measures in the Bill that would have an impact on market efficiency and are relevant to Vector's businesses:

   a. sulphur hexafluoride ("SF_6") emissions obligations;

   b. crude oil and other liquid hydrocarbons; and

   c. regulation-making powers in relation to auctions.

SF_6 emissions obligations

6. Vector **strongly supports** the Bill's proposal to "move the ETS obligations relating to sulphur hexafluoride from importers and manufacturers to users" (Explanatory note, page 2) by amending Schedule 3, Part 4, Subpart 2 of the Climate Change Response Act 2002 ("the Act").

7. Placing emissions obligations on users rather than importers of SF_6 (based on 100% of volume imported) promotes efficiency by more accurately reflecting the cost of emissions as the SF_6 is emitted over time (actual emissions).

8. Vector notes that SF_6 is not intentionally vented or consumed by the switchgear that contains it on Vector's networks.[3] There is some leakage during the lifetime of a switch but this is a minute amount - in Vector's case, only 0.1% to 0.4% of total volume each year.[4] When the switch is at the end of its operational life, the remaining SF_6 is recovered prior to equipment disposal.[5] In this sense, electricity lines companies should be seen as 'stewards' rather than 'consumers' of SF_6.[6]

9. Imposing obligations at the point of importation disproportionately inflates the cost of SF_6 emissions. Charges based on 100% rather than the minute amounts emitted over time would be a gross overpayment. Over-signalling the cost of SF_6 emissions would have an adverse impact on firms that own electricity switches.[7] This does not contribute to the Government's economic growth objectives that the Bill seeks to progress.

10. Importantly, paying emissions charges up front does not provide incentives for users to reduce emissions.[8]

---

[3] http://www.vector.co.nz/sites/vector.co.nz/files/4%20%2020110406Vector%20Submission-ETSIssuesStatement.pdf, paragraph 20
[4] Ibid.
[5] Ibid.
[6] http://www.vector.co.nz/sites/vector.co.nz/files/Vector%20Submission%20ETS%20Amendments.pdf, paragraph 23
[7] http://www.vector.co.nz/sites/vector.co.nz/files/4%20%2020110406Vector%20Submission-ETSIssuesStatement.pdf, paragraph 20
[8] Ibid., paragraph 21

11. Underlying Vector's use of SF_6 is a very simple objective: Vector wishes to have the lowest level of emissions possible. This is driven by the following considerations:[9]

    a. Safety of Vector's equipment. Switchgear can become unsafe if SF_6 pressure drops, so Vector has systems in place to monitor SF_6 pressure and takes action to recharge it to keep the equipment safe.

    b. Cost. SF_6 is expensive and is therefore a resource not to be wasted.

    c. SF_6 has a high global warming potential and it is better for the environment for any kind of emissions to be eliminated, if not kept to an absolute minimum.

12. There is therefore a strong alignment between Vector's objectives and the Government's economic growth and emissions reduction objectives, as reflected in the Bill. Sending the right price signals and avoiding perverse incentives by imposing charges based on actual emissions by SF_6 users support these objectives.

13. Vector looks forward to providing feedback on the regulations that would give effect to the Bill's proposal on SF_6 emissions obligations. It anticipates options that would not be too onerous for large users of this gas, particularly during the first few years of mandatory SF_6 emissions reporting. This would be consistent with the Bill's aims of making the ETS more business-friendly while demonstrating New Zealand's commitment of doing its fair share in climate change mitigation.[10]

Crude oil and other liquid hydrocarbons

14. Under Schedule 3, Part 2 (Liquid Fossil Fuels), the Bill proposes a new Subpart 2 which will add own-use of crude oil and other liquid hydrocarbons to the list of activities facing emissions obligations from 1 January 2014.

15. While this new subpart appears to be intended for oil and gas exploration/production mining activities, the drafting creates a clear risk of overlap with "refining petroleum" and "combusting used oil" or "waste oil" under Schedule 3, Part 3.

16. The drafting also creates the risk of double counting. The point of obligation for natural gas is upstream, i.e. the miner, however, some of the natural gas will be

[9] http://www.vector.co.nz/sites/vector.co.nz/files/4%20%2020110406Vector%20Submission-ETSIssuesStatement.pdf, paragraphs 16-18
[10] http://www.beehive.govt.nz/release/ets-amendment-bill-passes-first-reading

used by downstream users in liquid form, e.g. LPG and condensate. The amendment as drafted would place a second point of obligation on these downstream users of LPG and condensate for which a unit surrender obligation already lies with the miner.

17. Vector **recommends** that the Bill add a "for the avoidance of doubt" provision, clarifying that emissions obligations under the new Subpart 2 are distinct from, or in addition to, existing obligations under Schedule 3, and that they are directly related to mining activity(ies). This would ensure the double counting of emissions is avoided.

Regulation-making powers in relation to auctions

18. Vector considers the auction of NZUs to be consistent with the operation of efficient markets, provided the auction design promotes greater price transparency and provides clear signals as to parties' willingness to pay for the units. Auctions are a low-cost mechanism of allocating resources and inject liquidity into the market.

19. Vector, however, is concerned with the proposed expansion of the responsible Minister's ("the Minister") powers to sell New Zealand units by auction under section 30G(1)(p). Vector reiterates that it does not support any discretionary power to effect significant changes to the ETS,[11] particularly when those changes are not required to be subject to meaningful stakeholder consultation.

20. The exercise of discretionary power is inconsistent with good regulatory practice and with the Government's Statement of Regulation, which states that the Government will "[r]esist the temptation or pressure to take a regulatory decision until [it] has considered the evidence, advice and consultation feedback…"[12] The Statement of Regulation further requires that "a particularly strong case [be] made for any regulatory proposals that are likely to impose additional costs on business during the current economic recession".[13] Vector **recommends** that an additional provision be inserted requiring the Minister to conduct stakeholder consultation on the design of auctions before making regulatory recommendations.

21. Vector considers the one year notice period required before the Minister can make recommendations to amend auction regulations under section 30G(3D) to be too short and potentially destabilising. Vector **recommends** that a longer and more stable period for the application of auction regulations be adopted to provide certainty for market participants. Vector does not object to providing built-in

[11] http://www.vector.co.nz/sites/vector.co.nz/files/Vector%20Submission%20ETS%20Amendments.pdf, paragraph 17
[12] http://www.treasury.govt.nz/economy/regulation/statement/govt-stmt-reg.pdf, page 2
[13] Ibid.

flexibility for the auction regulations to be amended in the interim should there be a need to do so. Consistent with good regulatory practice, any proposed amendments should be subject to stakeholder consultation.

22. On a related matter, Vector is concerned that the retention of the Minister's power to make recommendations for regulations prescribing the transfer of units (section 30G(1)(b)), the holding, surrender, conversion and cancellation of units (section 30G(1)(c)), and the carry-over of units (section 30G(1)(d)) could discourage or impede the access of international units at short notice. In the interest of greater market efficiency and liquidity, Vector **recommends** that this power be moderated through the removal of section 30H(5) which overrides the procedure for appropriate consultation.

Yours sincerely

Bruce Girdwood
Manager Regulatory Affairs