

# Impact Summary: NZ ETS Improvements - Receiving emission units where there are overdue obligations

## Section 1: General information

### Purpose

The Ministry for the Environment is solely responsible for the analysis and advice set out in this Regulatory Impact Statement. This analysis and advice has been produced for the purpose of informing final decisions to proceed with a policy change to be taken by Cabinet.

### Key Limitations or Constraints on Analysis

There are no limitations or constraints on the analysis in this summary.

### Responsible Manager (signature and date):



Matthew Cowie

Manager – Climate Change Policy

Climate Change Directorate

Ministry for the Environment

Date:

22/11/18

*A Quality Assurance Panel with representatives from the Ministry for the Environment and the Treasury Regulatory Quality Team has reviewed the Regulatory Impact Assessment (RIA) "Impact Summary: NZ ETS Improvements - Receiving emission units where there are overdue obligations" produced by the Ministry for the Environment and dated November 2018. The panel considers that it meets the Quality Assurance criteria.*

*More detail on the assessment of this and the other RIAs can be found at: [link to be added].*

## Section 2: Problem definition and objectives

### 2.1 What is the policy problem or opportunity?

Pursuant to the Climate Change Response Act 2002, some participants in the New Zealand Emissions Trading Scheme (NZ ETS) are eligible to receive New Zealand units (NZUs) from the Crown.<sup>1</sup>

Under current law, eligible participants would be entitled to receive their allocation of NZUs even if they have an overdue obligation to surrender NZUs from a previous reporting period.

The Climate Change Response Act 2002 does not contain a mechanism to allow the enforcing agency to effectively 'net-off' the surrender obligation by requiring the allocation to be deducted by the amount of the overdue obligation.

The Government seeks to improve the integrity and administrative efficiency of the NZ ETS by increasing compliance with NZ ETS obligations. It considers that the ability to net-off the debt against the allocation will assist it to realise these objectives.

### 2.2 Who is affected and how?

Persons affected by this issue are:

- The NZ ETS regulators, who incur administrative costs from pursuing overdue obligations while also transferring NZUs to the same accounts.
- Participants who are required to surrender NZUs and are also eligible to receive NZUs under an allocation plan. Surrender obligations are usually met in a timely manner. However, there are some instances where an obligation becomes considerably overdue.

### 2.3 Are there any constraints on the scope for decision making?

There are no constraints on the scope for decision making, or interdependencies or connections, other than that resolution could require amendment to primary legislation.

A similar proposal to 'net-off' forestry emissions returns is contained in forestry proposals to improve the ETS. These proposals do not overlap but seek to solve similar issues across sectors.

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<sup>1</sup> Some recipients of units are not also participants, and do not have an obligation to submit emissions returns or surrender units. This proposal does not impact on these recipients. For example, participants which own or have a registered right or leasehold of post-1989 forest-land or are a party to a Crown conservation contract (Part 1 of Schedule 4 of the CCRA) or who export goods containing synthetic greenhouse gases (subpart 3 of part 2 of Schedule 4 of the CCRA) may be carrying out 'removal activities' and be eligible for an industrial allocation of NZUs.

## Section 3: Options identification

### 3.1 What options have been considered?

Two options, both of which would resolve the policy problem, have been considered and consulted on:

Option 1: When an entitlement to NZUs is approved by the Environmental Protection Authority (EPA), immediately before transferring the NZUs to the holding account, any amount of NZUs which are overdue pursuant to an NZU surrender obligation owed by the same participant may be deducted from the full allocation amount. Any remaining balance would then be transferred to the participant, ensuring the participant still benefits from the value of the full allocation amount.

This amendment would increase the likelihood of the EPA recovering NZUs which are owed and overdue, and NZU surrender obligations being met in general, and is fair to those who comply with their obligations. As all NZUs represent one tonne of carbon dioxide equivalent, they are considered fungible, and there are no issues of the Crown receiving a unit of a higher or lower value.

There would be no impact on the quality of emissions returns or data from this option, as it involves transfers of units between accounts after applications and returns are submitted.

Option 2: For either the EPA or a participant to net-off emissions returns once received or when submitting. This would significantly complicate reporting and emissions data. For example, assume an NZ ETS participant with an overdue surrender obligation of 1500 NZUs (representing 1500 tonnes of carbon dioxide equivalent emissions for a year) and an entitlement to 2000 NZUs for a year. Emissions and reporting data would only reveal the net entitlement of 500 NZUs.

Additionally, if the obligation for netting off rested with the participant, the penalty provisions will need further refinement to account for netting off miscalculations.

### 3.2 Which of these options is the proposed approach?

Option 1 is the proposed approach. Option 1 has a lower administrative cost and is less complex. Existing systems could be updated to automate much of this process, reducing the potential for human error leading to mistakes which may incur a penalty.

Automating the process is more likely to result in outstanding surrender obligations being met as the units are automatically transferred.

## Section 4: Impact Analysis (Proposed approach)

### 4.1 Summary table of costs and benefits

<b>Affected parties</b> <i>NZ ETS participants, the regulator, and the Crown</i>	<b>Comment:</b> nature of cost or benefit (eg ongoing, one-off), evidence and assumption (eg compliance rates), risks	<b>Impact</b> <i>\$m present value, for monetised impacts; high, medium or low for non-monetised impacts</i>
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#### Additional costs of proposed approach, compared to taking no action

Regulated parties	<p>Some initial and immediate costs if overdue surrender obligations need resolving, limited to those that are both eligible to receive NZUs and also have outstanding surrender obligations. Such costs will not be re-incurred once all current overdue obligations within scope are repaid.</p> <p>A participant affected by this change may have less flexibility in the way that they meet their surrender obligation. However, the proposal only applies to outstanding surrender obligations, not all surrender obligations, which the participant has the opportunity to meet in a timely manner.</p> <p>Outstanding surrender obligations would still be subject to the compliance and penalties regime in the ETS.</p>	Low
Regulators	There would be an initial implementation cost to upgrade the system to automate transfer of the appropriate number of NZUs to the Crown account.	Very low
Wider government		Nil
Other parties		Nil
<b>Total Monetised Cost</b>		Low
<b>Non-monetised costs</b>		Nil

#### Expected benefits of proposed approach, compared to taking no action

Regulated parties	<p>Potential for reduced compliance costs, as overdue obligation issues are resolved more easily where the participant is entitled to be allocated with NZUs. This may reduce the participant's interactions with the penalty regime to the extent underlying surrender obligations are met by allocations.</p>	Low
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Regulators	Administrative savings from reduced compliance work and recovery of NZUs it is owed.	Low
Wider government	NZ ETS compliance will improve as a result of being able to access NZUs it is owed as a surrender obligation more quickly and easily and this will in turn improve the integrity of the scheme. This amendment will mitigate the risks to the Crown associated with unmet surrender obligations, including the ability to meet domestic and international climate change targets.	Medium
Other parties		Nil
<b>Total Monetised Benefit</b>		Low
<b>Non-monetised benefits</b>		<i>Medium</i>

#### **4.2 What other impacts is this approach likely to have?**

There will be no other impacts.

## **Section 5: Stakeholder views**

#### **5.1 What do stakeholders think about the problem and the proposed solution?**

Consultation was held on this proposal within a package of planned NZ ETS improvements over July – August 2018.

All submissions on this issue supported the proposed approach, being option 1. There were no submissions opposing the proposal, or supporting the alternative option.

## **Section 6: Implementation and operation**

#### **6.1 How will the new arrangements be given effect?**

This proposal is one of several operational changes that will be carried through to the proposed Climate Change Response Amendment Bill in 2019, and come into effect from 1 January 2020.

## **Section 7: Monitoring, evaluation and review**

#### **7.1 How will the impact of the new arrangements be monitored?**

The scheme regulator will continue to monitor the emissions reporting and unit allocations of participants once the new arrangements are implemented.

#### **7.2 When and how will the new arrangements be reviewed?**

No review of the arrangements is planned.