

ETS Reforms - Pricing considerations

The recent passing of the Climate Change Response (Emissions Trading Reform) Amendment Act makes a number of reforms to the ETS which are aimed at ensuring it is a more effective tool to help meet NZ's emission reduction targets.

Key changes include the introduction of a cap on emissions under the ETS, new price controls measures, and the establishment of auctions for NZ units, all of which will impact pricing and are intended to incentivise participants to reduce their emissions.

Participants in the ETS have previously been able to purchase an unlimited number of NZ units from the Government at a fixed price of \$25 per unit. But from 2021, instead of being able to buy an unlimited number of units at a fixed price, participants will need to purchase units through auctions that only have a limited number of units available for purchase. The limited number of units available for purchase will be determined by the emissions cap and other supply factors.

Emissions cap

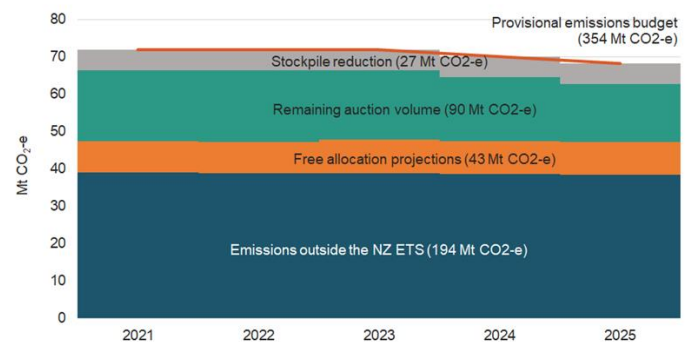
The emissions cap will be determined based on the national emissions budget. From there, a series of steps are taken to determine the number of units that are available to be auctioned.

1. Emissions from outside of the scheme are removed from the NZ ETS cap (e.g. agricultural emissions).
2. Any required technical or forestry related adjustments are made.
3. Free allocation units are removed.

4. An agreed volume of units is removed to drive stockpile reduction.
5. A limit is set on international units.
6. The remaining volume is available to be purchased at auctions.

Based on the Government's provisional emissions budget for 2021 – 2025 of 354 Mt CO₂-e, the total number of units available to be auctioned over this five year period is 90 million.

The below graph from the Ministry for the Environment shows the breakdown of the Government's provisional emissions budget for 2021 – 2025. The provisional emissions budget will be finalised in 2021 following advice from the Climate Change Commission.



Source: Ministry for the Environment

Auctions

Auctions will become the key tool for managing the supply of units into the ETS, and the new price control measures will apply to auctions to prevent unacceptably high or low auction prices. Auctioning will be held quarterly and is intended to start in 2021.

Auction schedules will be published every September for the upcoming year, and overall supply volumes are

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subject to adjustment on a rolling basis. Annual volumes will be split evenly across all four auctions, and if units remain unsold at the end of an auction they will roll-over to the next auction if it is in the same calendar year.

The current auction schedule for 2021 is:

Date	Volume available
17 March 2021	4.75m units
23 June 2021	4.75m units
1 September 2021	4.75m units
1 December 2021	4.75m units
Total for 2021	19m units

Fixed price increase

As auctions are not intended to commence until 2021, the arrangement where units can currently be purchased from the Government at a fixed price will continue. However, the fixed price has been increased from \$25 per unit to \$35 per unit (effective 22 June 2020), which sends a signal to participants about the expected direction of emission prices under the auction process.

The continued availability of units at the fixed price of \$35 depends on when auctioning starts.

- If the first auction occurs at any stage **during 2021**, then the \$35 fixed price will be available to cover emissions that occur within the 2020 calendar year. Participants could access the \$35 fixed price until the end of the 31 May 2021 surrender deadline.
- If the first auction occurs at any stage **during 2022**, then the \$35 fixed price will be available to cover emissions that occur within both the 2020 and 2021 calendar years. Participants could access the \$35 fixed price until the end of the 31 May 2022 surrender

deadline.

- If the first auction occurs **later than 2022**, then the same approach applies – participants can access the \$35 fixed price for emissions within the previous calendar year until the 31 May surrender deadline in the next calendar year.

While the current intention is for auctions to commence in 2021, the above shows that there is scope for this to be delayed and for the fixed price arrangement to continue beyond this year

Price controls for auctions

The price controls for auctions are:

- a "cost containment reserve" (**CCR**), which acts a price ceiling that releases a specified number of additional units to the market to help meet the demand that is driving the price of units higher (and is intended to slow/reduce the price rise); and
- a minimum price that units can be sold for at auction.

The trigger price for the CCR and minimum prices for the 2021 to 2025 period are:

	2021	2022	2023	2024	2025
CCR trigger price	\$50.00	\$51.00	\$52.02	\$53.06	\$54.12
Minimum price	\$20.00	\$20.40	\$20.81	\$21.22	\$21.65

The annual increase represents a 2% increase in line with forecast inflation.

The volume of the CCR will be made up of:

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- units that have been withheld from auctioning to help reduce the current stockpile of units already in the ETS, and which are included within the ETS cap;
- units that amount to 5% of the total volume of the units in the ETS, but which are above the ETS cap (and therefore have to be 'backed' by an equivalent tonne of removals or reductions procured by the Government to ensure integrity).

The volume of the cost containment reserve for the 2021 to 2025 will be:

	2021	2022	2023	2024	2025	Total
Stockpile reduction volume	5.4m units	5.4m units	5.4m units	5.4m units	5.4m units	27m units
5% of total units	1.6m units	1.6m units	1.6m units	1.6m units	1.5m units	8m units
Total volume of cost containment reserve	7.0m units	7.0m units	7.0m units	7.0m units	7.0m units	35m units

Want to know more?

If you would like further information or have any queries or concerns, please contact Anderson Lloyd's specialist [Renewable Energy and Carbon Trading Team](#).