

Submission by



to the

Ministry for the Environment

on the

Improving market governance of the New Zealand Emissions Trading Scheme: Discussion document

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GENERAL COMMENTS

1. BusinessNZ Energy Council (BEC)¹ welcomes the opportunity to provide feedback on the Ministry for the Environment's ('the Ministry') consultation document *Market governance of the New Zealand Emissions Trading Scheme* (the 'document'), published on 17 November 2022.
2. New Zealand's ETS is one important tool – if not the most important tool – for reducing greenhouse gas emissions. Since 2010, great progress has been made on improving the ETS framework, with the ETS adapting every year since that time. We recognise that further developments are vital to ensuring a robust and effective tool over time. BEC acknowledges the importance of sustaining public confidence in the ETS. Good governance protects the integrity of the scheme, and its durability through time, ensuring it remains New Zealand's most important tool for reducing carbon emissions.
3. However, before any intervention is considered and implemented, the problem must be well defined. This concern was raised in BEC's [previous submission](#) on the discussion document *Designing a governance framework for the New Zealand's ETS*, published in September 2021. Although the 2022 discussion document provides greater detail, in some specific areas the problem definition remains weakly defined and the justification to intervene in some areas remains doubtful.
4. Our specific comments are structured in the order of the discussion document's topics.

Topic 1 Regulating the NZU market based on financial legislation

5. BEC supports the principles outlined in ***Option two: Financial Markets Conduct Act with suitable modifications***, to "*prohibit insider trading and market manipulation in relation to trading of NZUs*".
6. However, the inclusion in option two of an agreement in principle for "an optional centralised exchange" with the Government considering options to procure and fund an NZU exchange, is clearly a step beyond regulation to direct intervention in an already established market. BEC recognises the details about how this system could operate are vague, as the Ministry's thinking about this matter remains provisional. Nevertheless, there are currently three incumbent secondary market operators, and we are unaware of any issues that would justify government funding to set up a competing platform. The Government may also confer significant commercial benefits on the chosen exchange operator through:
 - a. technical requirements, e.g. an API link to the emissions register to automate transactions that is not open source; or
 - b. regulatory obligations, (e.g. enforcing unreasonable or mismatched licence requirements on other platform operators.
7. Rather than improving liquidity (a non-regulatory objective), such an intervention could lead to market disruption and confer market power on the chosen exchange operator.
8. Regulating the NZU market based on financial legislation, as indicated with option two, may add additional costs for participants – creating compliance burdens in the form of ongoing fees and licence requirements. Unnecessary costs created through regulations can undermine price discovery. This could lead to less liquidity, and possibly deter entry. We ask policymakers to consider this unintended consequence.
9. We also seek clarity and assurance that the proposed regulatory approach will not restrict existing contractual arrangements for NZU supply including long-term unit offtake agreements and contractual opt-in arrangements between energy suppliers and users.

¹ Background information on BusinessNZ and BEC is attached as Appendix One.

Topic 2: Regulating NZU financial advice, transactional and/or custodial services

10. BEC supports the distinction between retail and wholesale clients as set out in ***Option two: Regulating NZU financial advice, transactional and/or custodial services***, but again highlights that the justification for intervention presented is light in detail.
11. It is important that any regulations recognise the differentiating characteristics of the ETS when compared with financial markets, it being a political construct with advisory services encompassing forestry, engineering, climate change policy (domestic and international), legal and perhaps lastly, financial aspects. Before further steps to regulate are taken, it is recommended that there be a more in-depth assessment of the nature of advice required to support both a well-informed market and investment decisions relating to the decarbonisation of the economy.

Topic 3: Improved transaction reporting

12. BEC is pleased to see that the potential position and purchase limit previously proposed has been dropped. Such restrictions would have made it more difficult for firms to purchase units and hedge against the risk of potential carbon price volatility over multiple years. Moreover, since large scale participants surrender a significant quantity of units each year, a purchase limit would have made their participation unnecessarily more difficult.
13. The proposed ***Option two: Improved transaction reporting***, has some merit, however clarity is required with respect to the pricing basis and how information will be consolidated and published, e.g.
 - a. Contractual opt-in transactions are often zero rated,
 - b. Long term contracts will have differing unit prices from "spot" transfers'
 - c. The volume of these trades could lead to non-representative market prices being published.
14. Option two also includes the requirement to disclose the "*the transactor's primary reason for holding an account.*" This is supported as it may help alleviate the information-gap on the banked units held by "*individuals or organisations who have never been participants and have never received units from the crown.*" In many cases these may not be simply "speculators" as some surmise but instead entities providing market liquidity and funding mechanisms with holdings being tied to ETS participants with surrender obligations. Any disclosure mechanism should seek to establish greater understanding of the banked units on a confidential and consolidated basis. This is critical for informed unit limit recommendations and decisions from the Climate Change Commission and Government respectively.
15. We restate our prior position that ***Option three: Full transaction reporting*** should be opposed due to increased regulatory costs and the risk of loss of confidentiality of commercially sensitive material. It may also lead to a loss of trading flexibility if reporting cost requirements result in market withdrawal by some parties. ETS aggregate data only should be required. No organisational level, individual trade data or counterparty identification should be disclosed.

Topic 4: Applying the AML/CFT Act framework

16. BEC has not considered this topic in depth, however it clearly supports measures to counter money laundering and terrorism financing.
17. Once again, we recommend that any restrictions are carefully reviewed against the need to avoid impacting long established transaction mechanisms (refer paragraphs 8 and 12 above).

CONCLUDING COMMENT – TRANSITION PLANNING

18. BEC notes the absence of any timeline for the proposals. We strongly recommend that implementation (if any) must consider the need to provide adequate time for ETS participants to respond to any required changes to their current unit acquisition strategy. With a calendar year

compliance period and 31 May deadline for unit surrenders, in some cases mismatched with firm's financial years, we suggest 2 years should be the minimum implementation time notice period.

APPENDIX ONE – BACKGROUND INFORMATION ON THE BUSINESSNZ ENERGY COUNCIL

The **BusinessNZ Energy Council (BEC)** is a group of leading energy-sector business, government and research organisations taking a leading role in creating a sustainable, equitable and secure energy future.

BEC is a brand of BusinessNZ and represents the **World Energy Council** in New Zealand. Together with its members, BEC is shaping the energy agenda for New Zealand and globally.



BusinessNZ is New Zealand's largest business advocacy body, representing:

- Regional business groups: [EMA](#), [Business Central](#), [Canterbury Employers' Chamber of Commerce](#), and [Business South](#)
- [Major Companies Group](#) of New Zealand's largest businesses
- [Gold Group](#) of medium sized businesses
- [Affiliated Industries Group](#) of national industry associations
- [ExportNZ](#) representing New Zealand exporting enterprises
- [ManufacturingNZ](#) representing New Zealand manufacturing enterprises
- [Sustainable Business Council](#) of enterprises leading sustainable business practice
- [BusinessNZ Energy Council](#) of enterprises leading sustainable energy production and use
- [Buy NZ Made](#) representing producers, retailers, consumers of NZ-made goods

BusinessNZ is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy. In addition to advocacy and services for enterprise, BusinessNZ contributes to Government, tripartite working parties and international bodies including the International Labour Organisation ([ILO](#)), the International Organisation of Employers ([IOE](#)) and the Business and Industry Advisory Council ([BIAC](#)) to the Organisation for Economic Cooperation and Development ([OECD](#)).

