



11 August 2023

NZ ETS review
Ministry for the Environment
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Wellington 6143

Via email: etsconsultation@mfe.govt.nz

Tēnā koutou

A functional Emissions Trading Scheme with the right incentives

Powerco welcomes this opportunity to provide feedback on the proposed changes to the New Zealand Emissions Trading Scheme (*ETS*) and the “permanent forest category” (together, *ETS review proposals*). The ETS review proposals and the Biodiversity Credit Scheme (*BCS*) are linked, and Powerco will separately engage on the BCS.

Powerco is one of Aotearoa’s largest gas and electricity distributors, supplying around 344,000 (electricity) and 113,000 (gas) urban and rural homes and businesses in the North Island. These energy networks provide essential services and will be core to Aotearoa New Zealand achieving a net-zero economy in 2050. Information about our network is provided in Attachment 1. Powerco is committed to reducing our own greenhouse gas emissions, we have measured and reported on our emissions by way of a Greenhouse Gas Emissions inventory since FY 2019/2020. In addition to internal measures to reduce our greenhouse gas emissions; we are currently considering how those efforts could be supported in future, by offsetting via the voluntary carbon market.

Powerco is a participant in the ETS in relation to our operation of electrical switchgear containing sulphur hexafluoride. We therefore have interests in both the ETS compliance and voluntary market in this ETS review.

Summary of Submission

Powerco broadly supports the objectives behind the ETS review and BCS, namely to:

- Strengthen incentives for gross emissions reductions and domestic climate action.
- Incentivise appropriate afforestation, including the amount of exotic forest planting incentivised.
- Develop better protection of New Zealand’s biodiversity.

Powerco's key submissions are as follows:

- a) Powerco supports a **functional ETS and stable market through policy certainty**. A steady and predictable New Zealand Unit (NZU) price is a critical signal to support businesses to make the necessary investments in decarbonisation and electrification to meet our 2050 target. Reforms to the ETS should seek to avoid policy uncertainty, market instability and price volatility.
- b) While driving gross emissions reductions is critical, penalising early movers on climate action through retrospective changes that undermine forestry investments will not provide the policy confidence needed to support either gross emissions reductions or net emissions reductions through indigenous and where appropriate, exotic forestry. Powerco therefore supports policy reform that includes the **recognition and grandfathering of existing investments** and forestry registrations.
- c) The voluntary offset market is at a critical stage in New Zealand. Development of a **formal framework for voluntary participation** in credible emissions reductions would support wider domestic decarbonisation and avoid New Zealand businesses being forced to invest in offshore decarbonisation and emissions removal projects.
- d) A **biodiversity credit market is appropriate** and necessary. Powerco supports the development of the market as a priority in the next Government term. This market could serve dual purposes – supporting voluntary action and also supporting resource consent applicants to substantiate “net gain” outcomes associated with development under the Resource Management Act 1991 (*RMA*) and its successor legislation.

Powerco feedback on ETS review proposals

A functional ETS and stable market

Recent policy uncertainty caused by changes to ETS policy settings, including the ETS Review and changes in approaches to NZU pricing and supply, has caused market and NZU price volatility. This policy and pricing uncertainty creates disincentives to both investment in gross and net emissions reductions. Decarbonisation projects are capital intensive and require predictability in pricing to support business cases. Without a consistent and predictable price signal, emitters are unlikely to make decarbonisation investments of the scale necessary to achieve the Climate Change Response Act's 2050 targets.

Before progressing any material ETS policy reform, it is necessary to consider how that reform will impact the ETS, NZU pricing and our ability to achieve the 2050 targets. Market participants – both mandatory and voluntary – urgently need certainty on the future structure of the ETS to keep national and entity-level emissions reduction targets within reach.

Driving gross emissions reductions whilst not penalising early movers on climate action

Powerco urges the Government to take into account two principles for any ETS reform option:

- Creating a clear signal on future policy direction to reintroduce stability to the market and certainty for all market participants as soon as possible. This will unblock not only NZU trading, which is currently dampened due to market uncertainty, but will also give investors the confidence to progress decarbonisation projects, many of which are also currently on hold given the uncertainty regarding investing in those initiatives vs carbon removals.
- Any changes to the ETS, particularly those that might impact the value of forestry units, should only apply prospectively, not retrospectively. Retrospective application of any changes would not only undermine existing property rights in those units (and forestry holdings more generally) but would also effectively penalise early movers in the voluntary market who have sought to invest in carbon removals as a mechanism to enhance climate action.

Permanent forest category redesign – the role of native forestry in the ETS and beyond

The ETS review proposals note that the current settings incentivise removals from faster-growing exotic forest. The Government has expressed general support for increasing indigenous afforestation levels and has introduced a parallel consultation on the “permanent forest category” (the *PFC*) introduced to the ETS from 1 January 2023 to support this.

Powerco supports the move to incentivise native afforestation and recognises the significant benefits and co-benefits of native forests, including protecting and restoring New Zealand’s rapidly deteriorating biodiversity, providing freshwater and land stability improvements and involving communities more actively in carbon farming (through the promotion of indigenous silviculture and nurseries).

Powerco also recognises the range of interests that currently exist in exotic pine plantation forestry, which have been built up in reliance on current market settings. To enable the transition to a greater proportion of indigenous forest over time without the market shock of a sudden change, Powerco supports transition forest concepts and carbon accounting that specifically supports and enables that transition without penalising existing investment.

Transition forests would enable Powerco and other voluntary market participants who have invested or are considering investing in forestry removals to meet emissions reduction targets while supporting the move from exotic to indigenous plantation.

Over time, as forests transition to a greater proportion of permanent indigenous forestry, Powerco supports investigation of how the benefits of those forests beyond carbon mitigation might be used to

incentivise restoration and enhancement of New Zealand's natural environment. We see a direct link to the proposed BCS, and the offset regime under the new Natural and Built Environment Act.

Formalising a role for the voluntary offset market

The voluntary carbon market is at a critical point of potential expansion in New Zealand. 2023 marks the first year that many of New Zealand's largest companies and financial institutions will commence mandatory climate-related disclosures. As organisations develop, set and report on emissions reductions targets, many will be considering the use of voluntary market offsets to provide a climate positive response for those emissions that cannot be reduced.

According to the Voluntary Carbon Markets Initiative (VCMI), a non-profit initiative launched at COP 26 in 2021:¹

Voluntary carbon markets have the potential to help fill gaps in financing for climate mitigation, enhance corporate efforts to transition to Net Zero and support the achievement of countries' Nationally Determined Contributions and sustainable development objectives. They can also support and accelerate the introduction of robust, well-designed climate policies.

A range of non-state actors are taking action through voluntary carbon markets in New Zealand and internationally.² International initiatives, including the Taskforce on Scaling Voluntary Carbon Markets and VCMI, have released reports on methods of scaling these markets globally and ensuring that voluntary offsetting claims have integrity.

The ability for the voluntary carbon market to 'fill the gaps' in New Zealand's climate mitigation is currently limited. Many New Zealand companies would like to acquire voluntary market offsets from credible New Zealand-based emission reduction or removal projects. Domestic projects are likely to have a range of other environmental, social and stakeholder engagement benefits for the communities in which New Zealand businesses operate. However, at present, outside of the ETS there are relatively few options to source New Zealand-generated and credible gross or net emissions reduction projects. Given the potential double-counting credibility issue associated with utilising NZUs without commensurate Nationally Determined Contributions adjustments, many New Zealand corporates are forced to look overseas.

Powerco therefore supports consideration of how the ETS could provide a clear, readily available and credible source of domestically generated, robust voluntary market offsets. Powerco stresses that development of a functional voluntary market should not be pursued to the detriment of the ETS

¹ Voluntary Carbon Markets Initiative, *Claims Code of Practice: Building integrity in voluntary carbon markets* (June 2023), at 5 (available [here](#)).

² McKinsey estimated that demand for carbon credits internationally doubled between 2017 and 2020 in the aftermath of the Paris Agreement being signed, and that demand could reach up to 1.5 to 2.0 gigatons of carbon dioxide (GtCO₂) by 2030 and up to 7 to 13 GtCO₂ by 2050 (McKinsey & Company, *A blueprint for scaling voluntary carbon markets to meet the climate challenge* (January 2021), available [here](#)).

compliance market – it will be important that predictable price signals and liquidity is present in the ETS markets. However, given the scale of the ETS review the Government is embarking on, Powerco supports consideration of the domestic voluntary market as part of this policy package in reductions and removals.

The development of a government-led framework for voluntary market actions can build on the current guidelines around the voluntary market³ and draw on international developments and literature (most notably, the VCMI in late June 2023 released the *Claims Code of Practice: Building integrity in voluntary carbon markets*. This, together with the final report of the Taskforce on Scaling Voluntary Carbon Markets,⁴ provide guidance on integrity of claims, market infrastructure, governance and implementation that the New Zealand Government could look to in formalising our own framework).

Powerco understands the complexities that may be associated with development of a voluntary carbon market in New Zealand, including reconciling voluntary market activity with the national greenhouse gas inventory (via corresponding adjustments). However, the current lack of clarity on the appropriate operation of the voluntary market threatens the integrity of units traded and claims made by entities. We ask the Government to prioritise the development of a more formal voluntary carbon market framework.

Indigenous forestry, biodiversity credits/offsets and effects management policy collaboration

As a lifeline utility, Powerco provides a service that at times creates unavoidable effects on the environment, which are (where necessary) mitigated, offset or compensated for under the RMA. Reliance on such mitigation, and in particular offsetting and compensation, is likely to increase as a result of the recently released National Policy Statement on Indigenous Biodiversity and the increased recognition of the 'effects management hierarchy' in planning documents.

Powerco is interested to see how the BCS could support greater investment in biodiversity improvements through the role of biodiversity credits or offsets, and their potential role in environmental effects offsetting and compensation. A BCS could play a key role in both enabling biodiversity compensation through the effects management hierarchy and in further incentivising native afforestation outside the drivers within the ETS.

Any future BCS should be developed in close connection with ETS reform so that decisions regarding incentivisation of native afforestation and the BCS work together to encourage greater pace and scale of conversion from exotic to native forestry over time.

³ MfE "Interim guidance for voluntary climate change mitigation" (2022) and MfE, "Guidance for voluntary carbon offsetting – updated and extended until 31 December 2021" (2019).

⁴ January 2021, available [here](#).

Conclusion

Powerco supports the objectives of these reforms, namely, to further protect our environment in emissions reduction, improved land use and protection of biodiversity.

Powerco's submission seeks to ensure any reforms provide certainty needed in the ETS price signal, do not undermining existing emissions investments, and encourage entry into the voluntary carbon market, for the benefit of Aotearoa New Zealand's environment and economy.

Should officials require any additional information regarding Powerco or the changes sought above, please do not hesitate to contact us via Adam Du Fall, Ph +64 6 7596268 or email: planning@powerco.co.nz

Ngā mihi,



Adam Du Fall
Head of Environment
POWERCO

Powerco has read and acknowledges the Privacy Statement outlined in the Consultation Document dated June 2023.

Attachment One – Further information about Powerco

Powerco is New Zealand’s largest electricity distribution network and largest gas distribution network in terms of network length. Our network spreads across the upper and lower central North Island servicing 344,000 (electricity) and 113,000 (gas) homes, businesses and industries. This represents 16% of the electricity connections and 46% of gas connections in New Zealand. Our electricity distribution network measures over 28,000 km in length and our gas network 6,100 km.

