LAWYERS FOR
CLIMATE ACTION NZ INC.

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6 April 2023

Committee Secretariat
Environment Committee
Parliament Buildings
Wellington

by email: en@parliament.govt.nz

SUBMISSIONS ON THE CLIMATE CHANGE RESPONSE (LATE PAYMENT PENALTIES AND INDUSTRIAL ALLOCATION) AMENDMENT BILL

Introduction

1 Lawyers for Climate Change Action Inc (**LCANZI**) is a non-profit group of over 500 lawyers. We advocate for legislation and policies to ensure Aotearoa New Zealand meets or exceeds its commitments under the Paris Agreement and achieves net zero carbon emissions as soon as possible and no later than 2050. More information about us can be found on our website: https://www.lawyersforclimateaction.nz/.

2 LCANZI welcomes the opportunity to make submissions on the Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Bill (**Bill**).

3 The Bill amends various provisions in the Climate Change Response Act 2022 (Act) relating to the Emissions Trading Scheme (ETS). This submission focusses on the proposal to link the free allocation qualification thresholds to the carbon price.

Submission

4 The purpose of the ETS is to cap net emissions in covered sectors of the economy in accordance with the emissions budgets, our NDC and the 2050 target.

5 The free allocation scheme was intended to create an exception for firms in emissions-intensive and trade-exposed industries to avoid being displaced by offshore producers who are subject to weaker emissions pricing.

6 The Act currently contains thresholds to determine whether an activity is moderately or highly emissions-intensive (and thus eligible for industrial allocation). Eligible businesses with moderate emissions receive 60 per cent of carbon costs at no charge, and high emitters are intended to receive 90 per cent.

7 The Bill would amend the qualification threshold for both moderately and highly emissions-intensive activities to link those to the price of carbon. The higher the price of carbon, the more businesses will be eligible in each category.

8 The following table shows the impact of the change on eligibility with an indicative carbon price of $75/unit:

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Committee members: Bronwyn Carruthers KC (President) /
James Every-Palmer KC (Treasurer) / Sophie Meares (Secretary) /
Michael Sharp / Lloyd Kavanagh / Zoe Brentnall / Cassandra Kenworthy /
Jennifer Campion / Frankie McKeefry / Grant Hewison /

Qualification threshold	Current settings	Proposed settings	Carbon price = $75 per unit
Moderate	800 whole tonnes per $1 million of specified revenue.[1]	800 × (25 ÷ *n*) tonnes per $1 million in revenue, where *n* is the price of carbon.[2]	267 tonnes per $1 million in revenue
Heavy	Equal to or greater than 1,600 whole tonnes per $1 million of specified revenue.[3]	1,600 x (25 ÷ n) tonnes per $1 million in revenue, where *n* is the price of carbon.[4]	534 tonnes per $1 million in revenue

9 As can be seen, the threshold would be radically reduced at the $75/unit price level and would fall further still assuming carbon prices rise in the future.

10 LCANZI opposes this proposal for the following reasons:

(a) The ETS should create incentives to reduce carbon intensity. In contrast, linking thresholds to the carbon price means that more and more activities would qualify for free allocation over time as the carbon price increases. This creates perverse incentives for businesses to wait for eligibility rather than make low-emissions investments.[5] Furthermore, businesses close to the boundary between the two categories will be rewarded from becoming more carbon intensive and migrating from "moderate" to "heavy" as they will receive a greater free allocation.

(b) The free allocation system was intended to be transitional, however this proposal would, fourteen years later, effectively expand eligibility. This would be counterproductive to the overarching purpose of the ETS. The increasing price of carbon ought to be incentivising increased efforts to reduce emissions, not qualifying more companies to receive subsidies.

(c) The General Policy Statement of the Bill suggests that the rationale for the proposal to adjust the qualification thresholds is 'the increased costs to an emitting business, and, therefore, the risk of emissions leakage'. However, our view is that the risk of leakage is overstated and there is a lack of positive evidence of potential and/or actual leakage in New Zealand. Studies have concluded that there is no evidence to date of significant carbon leakage.[6]

(d) The current free allocation is not "free" to the New Zealand taxpayer. At 6 million units per annum and an NZU price of $75, that is approximately $500

[1] Section 161C(a), Climate Change Response Act 2022.
[2] Clause15 of the Bill.
[3] Section 161(b), Climate Change Response Act 2022.
[4] Clause 15 of the Bill.
[5] Dr Hood, *Submission to the Environment Select Committee: Climate Change Response (Late Payment Penalties and Industrial Allocation) Amendment Bill* dated 2 April 2023.
[6] Benjamin Rontard and Catherine Leining, *Future Options for Industrial Free Allocation in the NZ ETS*, Motu Working Paper 21-13, September 2021, page 5.

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million of potential NZU auction revenue forgone each year. It seems very questionable that the current allocation is the best use of that money, let alone pursuing policies which will increase it. The position is even worse after 2037 when auctioning is projected by the Commission to cease. From that date the opportunity cost associated from the free allocation will become a cash cost as the Government will be forced to purchase forestry or overseas units to give them for free to greenhouse gas emitting industries.

(e) The proposed change to the free allocation qualification thresholds is a significant policy issue, not a minor technical change. LCANZI is concerned that this proposal was not consulted on and submits that it should be removed from the Bill, which was supposed to address minor technical issues. We are not aware of any analysis as to the number of businesses which will be affected, or the projected free allocation amounts.

Signed on behalf of Lawyers for Climate Action NZ Inc. by James Every-Palmer KC, Jeremy Bell-Connell and Jeremiah McLanahan