



New Zealand Institute of Forestry

Te Pūtahi Ngāherehere o Aotearoa Incorporated

**Submission to the consultation
Annual Updates to New Zealand Emissions Trading Scheme
limits and price control settings 2024**

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Introductory Comments

Thank you for the opportunity to submit on the Annual Updates to New Zealand Emissions Trading Scheme limits and price control settings 2024 consultation (the consultation).

If appropriate, the New Zealand Institute of Forestry (NZIF) wishes to be heard in support of its submission.

About the Submitter

The New Zealand Institute of Forestry (NZIF) was incorporated in 1929. It has approximately 900 members who are individual professionals in forestry. The NZIF's objects are to advance the profession of forestry in New Zealand and to be an independent advocate for forestry.

The NZIF is committed to serving the practice of forestry and the wider community through education, accountability and its code of ethics and performance standards. It fulfils a quality assurance role, setting the benchmark for professionalism and the quality of advice and practice by which members and others in the profession are measured.

NZIF members are concerned with the professional management of all forests, plantation and natural, conservation, protection and commercial. They can be found in forestry companies, consulting businesses, research institutes, educational facilities, government departments and providers of specialist services.

The members' qualifications and areas of expertise reflect the diversity of disciplines involved in managing all types of the NZ forest resource from traditional forestry degrees through science, economics, law, microbiology, hydrology, engineering, and resource management.

NZIF operates a regulated registration scheme which controls the registration and conduct of forestry professionals, whether they are consultants providing forestry advice to the public and private entities or acting in other roles.



Submission Summary

In responding to this consultation New Zealand Institute of Forestry is not responding to a significant part of the broader aspects of the consultation i.e., Unit Limit settings, Auction Price Control settings or Cost Containment Reserve Volume.

NZIF has responded to three forestry related questions but has a greater focus on how this consultation or other consultation is issued to the NZU market by Ministry for the Environment (MfE) including the material issued and follow up webinars.

Disclosure of Market Sensitive Information

The presentation of this consultation to the market at 8.30am on Wednesday 15 May 2024 when the market was already in operation as NZU prices are available from 8.00am, was a most serious failure by MfE.

It is unacceptable the MfE can not recognise the disclosure of market sensitive information must be made with more caution and certainly more care. Merely relying on the Disclaimer on the opening page at bullet three, wording starting with "*the Ministry does not accept responsibility for any action taken*" is insufficient when considering the range of participants in the broader NZ-ETS market, of which the Crown is one participant who are relying on auctions for raising necessary funding, and the price volatility potential.

Market Price Reaction

The market price reaction spoke volumes, spot prices of NZUs retraced i.e., **fell** (some may say collapsed) by 23% from a high of \$56 to \$43, not the first time officials' comments have influenced the NZU market.

It is simply unacceptable officials can impose this degree of volatility and loss of value on owners of NZUs.

Page 31 of the consultation document states

NZ ETS unit and price control settings do not directly set a price path for the NZ ETS. Price controls set the boundaries within which price discovery by the market is largely expected to occur.

Given this is MfE's expectation in considering a lower price corridor for auctions, per the consultation document, MfE are advising this is where MfE "largely expect" "price discovery" to occur i.e., market price is too high and should be lower. If this is the case, then the statement is akin to market manipulation.

No Context

The release of the consultation document was foreshadowed by an email on Tuesday 14 May 2024 after 5pm. However, the e-mail provided no detail and the e-mail of 15 May 2024

provided neither additional information nor context, meaning it was left to the market to try to decipher a nearly 40-page document when trading was able to occur i.e., the market was open.

Loss of Value

NZIF have determined a NZU **loss in value** to forestry holders, NZIF members and their clients and non NZIF members, who either own forest areas in the NZ-ETS or manage forest areas in the NZ-ETS equating **\$245,600,000**.

Poor Timing

This consultation is right in the middle of the forestry provisional emission return period 1 Jan 2024 to 30 Jun 2024 to Te Uru Rākau. When assessing the potential Auction Price Control settings from the consultation with current log prices a number of NZIF members were forced to sell into the collapsing market based on MfE consultation release.

Value Loss Determination

NZIF value loss is underpinned by the forestry removal NZU from MfEs website data available on the page *NZ ETS forecasts of emissions, removals and entitlements from the Crown's financial forecasting*.

NZIF notes the data, replicated in table following, was produced in 2023, highly likely based on registered hectares of post-1989 forest area in the NZ-ETS, and the 2024 years and beyond are forecasts.

NZ ETS forecasts of emissions, removals and entitlements from the Crown's financial forecasting – all figures millions

Calendar year	2023	2024	2025	2026	2027	2028
ETS cap (net emissions)	29.2	27.9	25.8	23.2	20.9	18.1
Auction volume	15	14.1	12.6	10.7	9.1	6.9
Forecast industrial allocation	6.3	6.2	6.2	6.1	6	6
Forestry removals	12.8	12.7	13.6	14.9	16.3	17.8
Other removals	2.3	2.4	2.4	2.4	2.4	2.4
Forecast NZU removals, industrial allocation, and auction volumes	36.4	35.4	34.7	34.1	33.8	33.1

Source <https://www.epa.govt.nz/industry-areas/emissions-trading-scheme/market-information/privately-held-units/>

MPI advise on their website, under the heading **Emissions Trading Scheme for Forestry as at 31 December 2022**, 539,888 hectares of post-1989 forest area was registered as at 31 December 2022. The date is significant as 31 December 2022 was the close of the third

Mandatory Emissions Reporting Period (MERP3) and provides the most accurate post-1989 forest area available.

Based on 2023 data from MfE and 2022 data from MPI it is fair to assume the Forestry removal NZUs of 12.8 million is derived from the 539,888 hectares of registered post-1989 forest land on 31 December 2022 with NZU delivery in the following calendar year 2023.

NZIF acknowledge not all the 12.8 million 2023 NZUs may be held by forestry based NZIF members, or non NZIF members, at consultation release date and a number of those NZUs are held for surrender under stock change accounting for example.

NZIF also acknowledge the MfE data is for the single 2023 emissions return year entitlement and we know forestry participants are long term participants / holders of NZUs over multiple years.

Based on this information we draw our conclusion as follows

1. MPI data – 539,888 hectares of post-1989 forest in the NZ-ETS
2. Most businesses in New Zealand maintain a 31 March balance date
3. Closing market price on last March business day 29 March 2023 being \$58.35¹
4. Forestry based NZIF Members and non-members NZUs holdings being 25% (conservatively) of the 2023 year number of 12.8 million and
5. The same forestry based NZIF members and non-members NZUs holdings cross multiple years i.e., the five year period of MERP3
6. A loss of value could be determined as \$245,600,000.00²

Price Control Corridor

The consultation document's focus, for the NZU market of which NZIF members are a significant participant in and supplier of NZUs, is on page 27 **Price Control trigger prices (auction price corridor) options** and provides the headline and very strong market signal on page 27 as

Option 2: Lower price corridor trigger prices

Given the time available to assess all the information in this nearly 40-page document when the market is trading NZIF implores MfE to answers the question: *What consideration did you give to how the NZU market prices would react?*

¹ Source Bloomberg and Commtrade

² \$58.35 minus \$43 multiply 12.8 million multiply 5 years (MERP3) multiply 25%

If the answer is simply “we did not” or “we are not concerned with this aspect” then MfE have failed to, at the very least, respect its own stakeholders which is bordering on negligent.

MfE Test

Table 1: Option Assessment Criteria (the MfE test) on page 12 of the consultation document is explained as the criteria used to assess options, reiterated in the consultation document on page 28 Table 11 Option comparison for trigger prices.

Notwithstanding an error in Table 11 on release date, this table being a crucial element of the MfE test which had to be corrected later, the overall MfE test result is Option two – Lower price control settings is on balance worse than the status quo.

This raises the obvious question – why include this as an option when it is worse than the status quo?

Additionally, MfE have stated in Table 1 on page 12 of the consultation document more weighting is applied to the “Likelihood of incentivising (net) emission reductions”

Table 11 under Likelihood of incentivising (net) emission reductions is a negative and as more weighting is applied to this category it is difficult to understand why MfE presents this as a viable Option 2 without a counterfactual such as Option three i.e., **Raise price control settings** as a balancer to this table.

This area of the document, which is the crucial element when trying to understand how MfE reached its conclusions, should not be this difficult for market participants to decipher and furthers the NZIF position releasing this material in the trading day demonstrates, at best, a lack of understanding within MfE of the impact of this consultation document.

MfE Webinar

MfE webinar Wednesday 29 May 2024 **NZ ETS Unit Settings and Annual Regulatory Updates 2024** from 14 minutes 35 seconds onward an MfE official advises price controls must be considered in relation to the 2050 target but states price control setting do not determine market prices and prices are determined by buyers and sellers of units. Further the official advises in relation to the auction floor and the CCR “but note this does not mean we could not change on, like the floor, or just the ceiling”

Such statements are not consistent with the consultation document as there is no obvious area of the consultation document which considers a higher price corridor and it is very hard to argue MfE are realistically “interested in feedback” on a higher price corridor when the Auction floor is at \$64 and the market is trading at \$56 at the time of release.



Submission

Specific questions from consultation document

8. We are interested in your views on the Commission's interpretation of increased transfers of pre-1990 units. Do you think the sale of pre-1990 units have increased? If so, what factors are influencing this?

Pre-1990 forest allocation units held long term³

New data about the transfer of pre-1990 allocation units out of their original recipients' accounts indicates that they are being sold at a faster rate than previously projected, allowing them to be used by participants for additional emissions. To account for this, we have updated our estimate of the volume of pre-1990 units that are likely to become available for sale and reduced our estimate of units held long-term from 14 to 7 million.

NZIF members and non members are/have been the long term holders of pre-1990 NZUs since applications for these NZUs closed in November 2011. Issuance was made under Forestry Allocation Plans in two tranches, first on or before 31 Dec 2012 and the second in 2013. The rationale for issuance was a partial compensation for land loss value.

Pre-1990 NZUs have always been available for transfer out of their original recipients accounts and therefore able to be used by participants for additional emissions, using the Climate Commission lens.

NZIF considers it is highly likely holders of pre-1990 NZUs will have reduced holdings given market conditions prior to now. NZIF notes, original recipients of pre-1990 NZUs have the ability to reinstate their account with NZUs (not necessarily pre-1990 NZUs) on the same basis as the original pre-1990 NZUs and NZIF would expect the Climate Commission has accounted for this potential in their modelling.

9. What is your preferred option for the price control corridor? Is there any other option that you think we should consider? What factors should inform the price these are set?

NZIF view is simply any discussion on price corridor should not be about preferred options until the more fundamental issue is addressed, which is how information in relation to price corridors is expressed to a market place which is actively trading NZUs.

A more considered presentation of information, as NZIF recommends, should not then immediately lead on to a discussion regarding whether a NZU is a financial product or not, it

³ Page 47 He Pou a Rangi Climate Change Commission: Advice on NZ ETS unit limits and price control settings for 2025-2029



is simply officials are speaking to the market, what officials say matters and how they say it has an influencing effect on NZU prices in the market.

Specifically in relation to lowering the auction floor, which NZIF does not favour, this action alone (or even the discussion of the action) is likely to lead to lower prices in short term as point one.

Point two is in formally changing the price control corridor whereby either the floor or the CCR is changed is a significant signal from the government and such decisions require far more consideration than is suggested in this consultation document.

NZIF view is the effect of lower the price floor may mean more units will be sold at auction, assuming the market does not trade through the new lower floor, because the signal alone is a strong signal of lower ambition overall. Assume auctions are partially or fully successful then the Climate Commission will likely model more excess units building up and the downstream effect of all these matters will depress investment in more forests and low carbon transition likely leading to higher emissions which the government will have to face i.e., a larger financial impost at some point

10. Do you consider a price corridor (ie, an auction floor price and a CCR), to be important? Why or why not?

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A more considered presentation of information, as NZIF recommends, should not then immediately lead on to a discussion regarding whether a NZU is a financial product or not, it is simply officials are speaking to the market, what officials say matters and how they say it has an influencing effect on NZU prices in the market.

Specifically in relation to lowering the auction floor, which NZIF does not favour, this action alone (or even the discussion of the action) is likely to lead to lower prices in short term as point one.

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Recommendation

1. MfE immediately move to review guidelines in place for its officials to consider the potential market impacts before making public comments about the ETS, assuming there are such guidelines.
2. MfE engage market specialist(s). Market specialists who are not involved in the ETS market but have significant financial market experience are resident in New Zealand and NZIF urges MfE to engage such specialists.
3. MfE ensure any future communications from governmental bodies do not inadvertently destabilise the NZU market is essential for maintaining the integrity and functionality of the ETS, especially during critical periods when government auctions are essential for raising necessary funding.

The implications of these statements are far-reaching. The lack of MfE communication considerations has directly contributed to the recent market turmoil.

Not only has confidence in the ETS been eroded, but there is also an increased likelihood of failed government auctions.



General Comments

NZIF would like to thank you for the opportunity to submit on this consultation. We would welcome any opportunity to provide further clarification in relation to the points we have made in the body of this submission.

If you have any queries, please contact the undersigned.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'J Treadwell', written in a cursive style.

James Treadwell (Fellow and RMNZIF)
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