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Ministry for the Environment

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DairyNZ Submission on the Review of the New Zealand Emissions Trading Scheme

Introduction

1. DairyNZ submits on the Ministry for the Environment's review of the New Zealand Emissions Trading Scheme (ETS).
2. DairyNZ is the industry-good organisation representing all 11,000 of New Zealand's dairy farmers. We seek to progress a positive future for New Zealand dairy farming through enhanced sustainability, profitability, and competitiveness. The dairy sector employs 55,000 people and generates \$25.7bn in export earnings: 1 in 4 of every export dollar New Zealand earns.
3. DairyNZ is committed to dairy farming playing its part in transitioning to a low emissions economy alongside the rest of New Zealand. We have active programmes to support farmers as they transition to lower greenhouse gas emissions and build their resilience to a changing climate.
4. The rationale for the review of the ETS appears to be that New Zealand will over rely on forestry removals, with a correspondingly insufficient reduction in its gross emissions.
5. Agricultural biological greenhouse gas emissions are not a part of the ETS, but the ETS does capture farmers' energy and transport greenhouse gas emissions and costs. The Government is yet to announce details of an alternative pricing scheme for biological methane and nitrous oxide. The default legislative 'backstop' currently sees these emissions priced within the ETS at a processor level from 2025.
6. This submission provides DairyNZ's perspective on the necessity and operation of the ETS and how agricultural greenhouse gas emissions should be treated.
7. We believe that the ETS Review is premature without further consideration and modelling of New Zealand's long-term pathway to net zero and its implications. It is also difficult at this stage, and without further quantitative information, to recommend a preferred policy option.

It's important to have a stable and durable Emissions Trading Scheme

8. The Climate Change Response Act has had six major amendments since the ETS was included in the Act in 2008. The review's new focus on gross emissions reductions, positing changing property rights and re-valuing forestry removals has seen uncertainty grow and confidence fall. Recently, the NZETS secondary NZU market price has bounced around depending on Government announcements and



speculation – contrary to what is expected of a stable, durable, long-term, and singularly focussed mechanism.

9. New Zealand's ETS is a useful and necessary tool that helps New Zealand make choices to reduce greenhouse gases. For the ETS to work well, it needs to be effective, and other rules should work together with it to help it do its job.
10. Having a stable and durable ETS mechanism provides the following benefits to ETS market participants:
 - **Predictable Costs:** A stable ETS provides participants with predictability in terms of the cost of emitting carbon. When the rules remain consistent, businesses can better estimate their future emissions-related expenses, facilitating financial planning and supporting investment in emissions reductions.
 - **Long-Term Planning:** Companies often require significant lead time to implement emission reduction strategies. A stable ETS enables participants to develop and execute long-term plans to gradually reduce emissions, avoiding rushed and costly adjustments due to sudden changes in regulations.
 - **Efficient Resource Allocation:** With a stable scheme, participants can allocate resources more efficiently towards emission reduction technologies and strategies. They can confidently invest in projects that will yield long-term benefits without the fear of regulatory upheaval.
 - **Technology Innovation:** Stable policies encourage research and development of innovative emission reduction technologies. When participants know the regulatory landscape won't shift abruptly, they are more likely to invest in and adopt cutting-edge solutions.
 - **Stakeholder Confidence:** A durable scheme signals a commitment to emission reduction goals, instilling confidence in stakeholders, including investors, customers, and the general public. This can contribute to a positive reputation and improved relationships.
 - **Economic Stability:** A consistent ETS helps stabilize the market for emissions allowances, preventing sudden fluctuations in prices that can affect participants' budgets and strategies.
11. The ETS creates a market for emissions allowances, allowing the forces of supply and demand to determine the price of emissions. This encourages cost-effective emission reductions as participants strive to reduce emissions at the lowest possible cost.
12. The ETS can and should send an appropriate long-term signal to participants. While we note that a volatile price can have moderate impacts for petrol or electricity prices, the same cannot be said for land managers. In that instance, any volatility can have damaging effects, and some cases may prove irreversible e.g., wholesale conversion of farmland to forestry.

Set the direction first, understand the implications and then discuss ETS reform options.

13. New Zealand's approach to transitioning towards low emissions should begin by establishing a clear strategic path. Additionally, it is critical to have consistent support from political parties across the spectrum, to create a durable and stable framework for the transition.
14. If the Government agrees with the Climate Change Commission that the focus should now be on gross greenhouse gas emission reductions, while continuing to incentivise forestry removals, we need to know what that balance looks like over time, and how this will affect existing and future investments.



15. We agree with others, like Business NZ and Energy Resources Aotearoa that conducting a comprehensive quantitative analysis to determine the level of gross emission reductions intended up to 2050 is required before any options are decided. This analysis should guide policy development by providing clarity on the required gross reductions, which is essential for achieving a balanced approach in the ETS.
16. The options, as presented, remain too broad and non-specific. We expect further assessment of a gross emissions reduction pathway (and the implications for each option) as these fundamental changes need to be well understood before the Government commits to a way forward.

The Government buying NZU's adds to the expense of meeting New Zealand's already ambitious Nationally Determined Contribution

17. Option 2 in the consultation document would see the Government purchase NZUs to influence demand in the market. This creates an opportunity cost for the Government in that specific budget provision would be needed, presumably foregoing other non-climate related priorities.
18. We note that in 2022, the Commission estimated that if the Government achieves its first and second domestic emissions budgets, 99 Mt CO₂e of offshore mitigation would still be needed to meet the NDC¹. Treasury has estimated this as costing anywhere between \$3,300,000,000 to \$23,700,000,000², describing this as “a significant fiscal risk” (this works out to be roughly \$4,700 per person in New Zealand). These costs to taxpayers and businesses should be quantified to better understand the choices and trade-offs associated with targets, carbon budgets, ETS unit supply settings and the options in this consultation document.

Multiple problems require multiple tools, not a “one-stop shop” Emissions Trading Scheme

19. The consultation document presents a variety of challenges with the current policy settings. These include:
 - A gap between emissions and New Zealand's 2030 target (page 17)
 - Excess offsetting and not enough gross emissions reductions (page 19)
 - The negative social and economic impacts of inappropriate afforestation (page 19, page 69)
 - The negative environmental impacts of inappropriate afforestation (page 19)
 - Current prices potentially not being sufficient to reduce gross emissions from energy, transport and industry (page 20)
 - Levels of indigenous afforestation lower than Climate Change Commission recommendations (page 20)
 - Limited removal alternatives (page 20)
 - Projected falls in New Zealand emissions prices (page 26)
 - Reduced export revenue due to large land-use change to permanent forestry (page 29)
20. It is difficult, and perhaps heroic, to see how reform of the ETS alone would be able to ‘fix’ all these issues – the ETS may instead become misguided and bogged down in trying to achieve multiple objectives. We believe that solving for externalities (be they positive or negative), that don't relate to

¹ NZ ETS settings for 2023-2027 (climatecommission.govt.nz)

² Ngā Kōrero Āhuarangi Me Te Ōhanga: Climate Economic and Fiscal Assessment 2023 (treasury.govt.nz)



the core function of the ETS (to reduce emissions) should be addressed through other mechanisms e.g. other regulation and/or schemes.

Remove the ETS Backstop for Agriculture – It won't work in New Zealand's best interests.

21. The NZ ETS remains the legislated 'backstop' for pricing agricultural emissions if an effective and workable alternative is not delivered. This provision can be 'turned on' at any time.
22. DairyNZ does not support agriculture going into the ETS. The ETS is neither appropriate nor sensible for farmers, rural economies, or the New Zealand economy. Significant modelling undertaken through the He Waka Eke Noa (HWEN) Partnership and the government's own work programmes have shown the detrimental impact of pricing agricultural emissions through the ETS. Ministers have also spoken in recent months about the inappropriateness of the ETS for agricultural greenhouse gas emissions - but the ETS backstop option remains.
23. Through the 'backstop' option:
 - Processors (dairy and meat) and synthetic fertiliser manufacturers and importers would be responsible for reporting and paying for methane and nitrous oxide emissions.
 - Emissions would be calculated using national average emissions factors for relevant products, e.g. milk, meat, and synthetic fertiliser.
 - The way emissions are calculated for a processor-level price would not reflect any differences in on-farm practices that change an individual farm's emissions. This would fail to incentivise behaviour change on farm to drive emissions reductions.
 - Short and long-lived gases would be treated the same with a carbon equivalence metric (GWP100) – contrary to split gas domestic targets and our latest science understanding.
 - Methane does not need to get to net zero like the other bundled gases in the ETS.
 - Emissions reductions modelled indicated reductions in total agricultural emissions of less than 1% reduction in both CH₄ and N₂O below 2017 levels, additional to reductions as a result of other environmental policies (the alternative pricing proposal recycled revenue to help innovate and drive a transition).
24. Modelling by the HWEN Programme Office in 2022 showed that putting agriculture into the ETS would result in modest emissions reductions, a drop in production, and a loss of profits (most heavily to the sheep and beef sector).³

	CH₄ price (\$/kg CH₄)	LLG Price (\$/t CO₂-e)	CH₄	N₂O	Milk	Sheep & Beef Meat	Dairy Profit	Sheep & beef profit	Gross levy revenue (\$m)
2025	\$0.11	\$4.25	-0.2%	-0.2%	-0.5%	0.0%	-1.7%	-5.9%	\$136
2030	\$0.35	\$13.80	-0.8%	-0.5%	-1.8%	-0.1%	-5.5%	-17.5%	\$426

25. A farm-level levy has been agreed by Government, following extensive analysis and development work by HWEN, consultation with farmers, input from the Climate Change Commission, and the Government's own engagement processes. Therefore, we seek urgent removal of the ETS backstop to

³ FINAL-Pricing-agricultural-GHG-emissions-sectoral-impacts-and-cost-benefit-analysis.pdf (hewakaekenoa.nz)

Modelling is based on the assumed NZU prices in 2025 (\$85/t CO₂-e) and 2030 (\$138/t CO₂-e), with 95% and 90% allocations in 2025 and 2030 respective.



price agricultural greenhouse gas emissions. The ETS is not fit for purpose for agricultural emissions and does not make sense practically, scientifically, nor economically.

Nāku iti noa, nā

David Burger

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DairyNZ