Submission on Draft Second Emissions Reduction Plan

22 August 2024 Emailed to ERPconsultation@mfe.govt.nz

Thank you for the opportunity to submit on the draft Second Emissions Reduction Plan.

This submission is contributed to by the Combined Community Trusts of Aotearoa, Climate Action Working Group on behalf of **Climate Action Aotearoa**: **Funders Commitment on Climate Action.** It aims to address the support required from the central government for the Second Emissions Reduction Plan as related to the Philanthropic sector.

We stress that as a significant holder of community funds in managed trusts the philanthropic sector in Aotearoa New Zealand is ready to mobilise capital but needs leadership, direction, prioritisation and collaboration from the Government as set out in this submission

About Climate Action Aotearoa

Climate Action Aotearoa is a collective of Community Trusts of Aotearoa New Zealand and other signatories to Climate Action Aotearoa's Funder's Commitment. Its purpose is to provide a platform for funders in Aotearoa to better understand climate action needs, issues and opportunities, show leadership and undertake individual and collective action on these issues accordingly. It aims to accelerate a just (tika) transition to a low carbon society in Aotearoa, in partnership with iwi/hapu/Māori.

Thank you again for the opportunity to submit.

Yours sincerely,

Esther Whitehead

Climate-Action Co-Lead CAA

Climate Action Aotearoa
The Funders Commitment on Climate Action.

Summary of General Concerns:

ERP2 is critical for enabling Aotearoa New Zealand to comply with its upcoming emissions budgets under the the Climate Change Response Act 2002 (CCRA) but is ultimately not ambitious enough. **Lacking significant detail, it does the bare minimum of what might enable the next emissions budget to be met, and likely takes New Zealand off course for meeting future emissions budgets and our 2050 statutory target.**

Mitigation and adaptation pathways must consider the Crown-Māori relationship, Te Ao Māori, and the specific effects of the transition to a low-emissions economy and climate change for Iwi and Māori. **ERP2 needs to present much more detailed and robust strategies and plans for how the Crown will work with Māori/Iwi, uphold Te Titiri o Waitangi, and meet its obligation under the CRCRA to ensure ERP2 contains a strategy to mitigate the impacts that reducing emissions will have on iwi and Māori.**

We are concerned that the information provided in the consultation is inadequate to assess whether it is plausible that ERP2 will enable EB2 to be met. **We are also concerned whether there has been sufficient specificity to enable adequate consultation on the government's proposed strategy to recognise and mitigate the impacts of reducing emissions on iwi and Māori, as required by the Climate Change Response Act 2002.**

We are concerned that the Government is disregarding ERP1 without making the changes required to "maintain its currency", in order to make substantial (more than "minor or technical") changes to the existing emissions reduction plan, the Minister must use the same process as required to prepare the plan.

This is a safeguard that aims to prevent successive governments from taking New Zealand off-course in terms of our emissions reduction plans and strategies, providing for a degree of scrutiny and consultation. It also reflects the overall purpose of the CCRA: to provide a "framework by which New Zealand can develop and implement clear and stable climate change policies". This intention was also reflected in the Parliamentary debate leading to the passing of the Zero Carbon Amendment Bill

We consider that there are problems with the amendments to ERP1 and the way they have been presented in the consultation:

First, as a matter of sequencing, ERP1 should have been amended *before* the Government made decisions that were inconsistent with it. It appears that some decisions on climate policies were made without any modelling on their climate and emissions impacts, which left the Government flying blind in terms of whether New Zealand was still on track to meet its emissions budgets.

Second, all the Discussion Document does is list all of the policies and plans which the Government has cancelled and/or has no intention of following. However, this leaves ERP1 as a somewhat incoherent document.

Key theme 1: "least cost" net-based approach to emissions reductions

The ERP2 proposals take a "net-based approach" to emissions reductions, which involves reliance on both reductions in gross emissions and incentivisation of removals (e.g. through forestry). The primary reason identified in the ERP2 for this approach is that it is expected to be the most cost-effective way to reduce emissions and meet the second emissions budget.

A bare minimum approach is not the least-cost approach. It simply pushes the costs of climate change onto future governments and generations. It risks leaving Aotearoa New Zealand behind the international community and vulnerable to trade sanctions, carbon border tax adjustments, and access to markets and finance. Additionally, New Zealand will need to pay for every megatonne of greenhouse gas emissions not reduced domestically by purchasing offshore offsets to meet our NDC. The Treasury has estimated the cost of these offsets as between $3-$24B.[1]

While New Zealand's legislation and international commitments are all net-based, The Climate Change Commission and others has asked for a greater focus on reductions in gross emissions through decarbonisation initiatives. Indeed, the last Government had announced a review of the ETS last year with a view to better incentivising gross emissions reductions, while still recognising the role that forestry removals can play.

We expect New Zealand to show greater leadership on gross emissions reductions over the remaining half of this decade, and we're looking for Government support for gross emissions reduction initiatives.

---

[1] NZ Treasury and Ministry for the Environment, "Climate Economic and Fiscal Assessment 2023" at p. 86.

ERP2 does not present a convincing "way for us to achieve future budgets".

While we recognise the role that removals will play in achieving New Zealand's climate goals, the Government's over-reliance on emission removals comes at the expense of prioritising gross emissions reductions.

This proposed change in focus is explicit: the Discussion Document presents a "net-based approach" and "focus on reducing gross emissions" as *alternatives*, ultimately favouring a focus on carbon removals on the basis that it is the least cost and most flexible option.[2] It claims that removals can be "treated as equivalent to preventing the emission of one tonne of carbon dioxide in the first place".[2]

ERP2 has been set on the assumption that the Government will proceed with current emission budget levels, rather than the Climate Change Commission's draft recommended changes. Although the Minister is not required to follow the Climate Change Commission's advice[3], it is important that emissions budgets remain ambitious and can effectively provide the stepping stones towards meeting the 2050 target. In our view, that is best achieved by adopting the Climate Change Commission's draft recommended changes to emissions budget levels.

Key theme 2: a credible ETS

In line with previous indications, the ERP2 proposals emphasise the ETS as the primary tool for incentivising "least cost" emissions reductions in Aotearoa New Zealand. The Government has committed to aligning New Zealand emission unit (NZU) supply and the NZ ETS cap with the second emissions budget through annual updates of the ETS settings, and recently closed consultation on the settings for the period 2025 – 2029.

---

[2] Discussion Document, p. 24.

[3] Climate Change Response Act 2002, s 5ZE(4).

Given the Government has already scrapped the review of the ETS commenced by the last Government last year, it is unsurprising that the discussion document emphasises that forestry removals will continue to be treated as equivalent to emissions (with 1 tonne of CO_2e emitted equivalent to 1 tonne of CO_2e sequestered). The only significant change that the Government is proposing to the treatment of forestry under the ETS is the introduction of new limits on the entry of forests into the ETS where these are on productive farmland. This is the only concrete policy proposed by the Government in ERP2 with respect to the NZ ETS.

However, in advice on the Second Emissions Reduction Plan, the Climate Change Commission warned that “limiting the incentives for permanent forests could reduce the area of permanent forest planted, but it would not prevent further planting of production forests from displacing gross emissions reductions.” They also noted that this reform will not address the core problems with the NZ ETS.

The "net-based approach" proposed does provide some certainty to the forestry sector, which has faced low market confidence in light of the last Government's ETS review and other regulatory interventions. In terms of forestry offsets, carbon captured by trees is part of the fast carbon cycle, which is measured in a lifespan and consequently the risk of reversal is high.[4] Trees (and particularly exotic monocultures) are vulnerable to forest fires, disease and pests, and further, as the Commission has noted, “changes in climate may affect tree growth rates, increase wind throw and wildfire, and enable more pathogens to spread.”[5] The costs of maintaining or replanting these forest carbon sinks fall on future generations, while the ‘savings’ of not curtailing current emissions are enjoyed by the current generation.

[4] NASA. *The Carbon Cycle*. www.nasa.gov. See also Hoglund et al. 2022. *Nature restoration and carbon removal are not the same*. www.climatechangenews.com.

[5] Climate Change Commission *Ināia tonu nei: a low emissions future for Aotearoa* (Climate Change Commission, 31 May 2021) at 316.

Climate Action Aotearoa
The Funders Commitment on Climate Action.

The evidence is clear that the ETS is not fit for purpose. This is one of the main reasons for the low market confidence and overall perceived lack of credibility in the NZ ETS. The last time an ETS auction cleared was in March 2024, and that was the first time the ETS auction had cleared in a year. Since the Government started consulting on its proposed price and unit settings, which included a proposal to "lower the price corridor", ETS auctions have not cleared.

The Government remains committed to a split-gas approach to achieving climate change targets, and has reiterated its commitment to pricing on-farm agricultural emissions by 2030 through a "fair and sustainable" system. In relation to this, the Government has recently promulgated a legislative change, which has just passed its first reading, that removes agriculture from the ETS altogether, including by removing the current obligation on agricultural processors to report their emissions. Should that proposal become law, there will be no legislative "backstop" for the pricing of agricultural emissions.

This failure is a symptom of the wider issues with the NZ ETS, which include the:

a) significant stockpile of carbon units, which ERP2 does not meaningfully engage with;[6]
b) continued provision for industrial free allocation;
c) symmetrical treatment of removals and gross emissions reduction, which is leading to an over-reliance on exotic afforestation and not appropriately or adequately incentivising gross emissions reductions; and
d) exclusion of agricultural emissions from the ETS.

There must be wholesale changes to the ETS, including:

a. to not treat emissions and removals equally;
b. address the existing oversupply of NZUs in the stockpile;
c. to constrain the supply of future units for auction to match emissions budgets;
d. reassess the industrial free allocation policy.

---

[6] While ERP2 highlights some risks of the stockpile, it does not appear the Government intends to meaningfully respond to these risks. After briefly discussing some potential risks, the Discussion Document merely says that "upcoming decisions on NZ ETS settings are a key vehicle for the Government to manage potential risks and deliver budgets and targets in a way that protects the credibility of the NZ ETS". The Climate Change Commission, however, has advised that merely using existing unit price and quantity levers will be "ineffective in the medium to long term" at reducing the stockpile.

Key theme 3: focus on emerging technologies

The ERP2 proposals heavily emphasise the role that emerging technologies might play in reducing emissions.

In addition to emphasising carbon capture and storage as an option to reduce emissions over the longer-term, the discussion document identifies other potential abatement opportunities such as vaccines and methane inhibitors to reduce agricultural emissions, while acknowledging that many technologies are not yet commercially available. The Government's work in this area will be focussed on a structured research and development programme to drive the development and commercialisation of tools to reduce emissions on-farm, streamlining the regulatory approvals process for new technologies, and the provision of informational "extension services" to support farmers with the transition.

While future climate technologies will undoubtedly play a role in New Zealand's climate response, the government should be more cautious about their prospective role. Rather than waiting for its agri-tech investments to pay off, the government should implement agricultural emissions pricing during the EB2 period.

If the ETS is going to be used to incentivise removals through other technologies, we suggest decoupling the market for emissions reduction from the market for removals. This would allow for decisions around removals to be made as needed to address the specific outcomes required by removals, such as for excessively hard-to-abate sectors of the economy

Key theme 4: spotlight on energy

The energy transition is a key component of the Government's response to climate change. ERP2 recognises that emissions from energy use comprise 37 per cent of New Zealand's gross emissions, making it the second largest source of domestic emissions.

While New Zealand's electricity system is highly renewable (with significant additional renewable generation also in the investment pipeline), the consultation document highlights that electrifying the economy depends on affordable and secure electricity. This reflects the "energy trilemma", whereby our energy system faces three interconnected (and often conflicting) objectives of being affordable, secure and sustainable.

The Government has already announced flagship policies relating to the energy transition. Most significantly, the National Party's Electrify NZ policy, announced prior to the General Election, involves a commitment to doubling renewable energy by 2050 and focuses on enabling electrification by removing regulatory barriers to private investment. The Fast-Track Approvals Bill currently making its way through Parliament, is a critical part of this strategy. The discussion document indicates that further details of the Electrify NZ programme are to be announced, and highlights work that the Government has underway relating to each of the three limbs of the energy trilemma.

One important change in the approach to the energy sector from the last Government is that the new Government places greater emphasis on an ongoing role for natural gas to support the affordability and security of electricity supply, and to incentivise electrification. Key policies from the last Government, including the ban on new exploration and the development of a gas transition plan, have been scrapped.

We agree that the Government should ensure that there are fewer barriers to investment in low-emissions technologies. While we support the focus on scaling up the building of renewable energy generation, this comes with three caveats:

First, decisions on whether to fast-track renewable energy projects should include consideration of climate change and environmental impacts, and these should be balanced against economic outcomes.

Second, in its Monitoring Report, the Climate Change Commission made clear that key barriers to electrification are capital cost and access to low-cost financing. This is not reflected in ERP2. For instance, to ensure these projects are adequately funded (and such improvements have appropriate resilience and redundancy), the Government should also ensure that financing rules are favourable to the development of critical infrastructure (such as bank risk ratings)

Third, ERP2 risks understating the role of complementary policies to incentivise electrification in the industrial sectors on account of the energy sectors being covered by the ETS. So long as the issues with the NZ ETS persist, there is a risk that the emissions price will be too low to drive gross emissions reductions across industrial sectors.

Key theme 5: unlocking private capital

An important overarching theme, to the philanthropic sector, in the ERP2 proposals is the Government's emphasis on mobilising private capital towards emissions-reduction initiatives by removing barriers to investment.

The consultation document highlights some initiatives already underway (such as the development of a sustainable finance taxonomy) – Taxonomy Regulation aims to inform investors on whether an economic activity is environmentally sustainable by setting common criteria. Two overarching criteria sit at the heart of what is considered an environmentally sustainable economic activity. Those two criteria are that an activity must:

- contribute to at least one of six environmental objectives listed in the Taxonomy; these are climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems.
- do no significant harm to any of the other objectives (while also meeting minimum safeguards relating to human rights and labour standards).

We support the goals of taxonomy regulation because it may go some way to achieve 'interopability' with international taxonomies and gives the Financial Markets Authority (FMA) the means to protect against greenwashing claims and support greater investment in Aotearoa New Zealand's climate resilient projects, including nature-based solutions.

Other ERP2 proposals remain at the exploratory phase. For example, the Government proposes to test which barriers to investment are a priority and implement them over the next 18 months, including through engagement with the private sector. The discussion paper P44. States that 'while we expect this investment (in lower emissions services and technologies) to come primarily from the private sector, the government has a role in addressing barriers to such investment and ensuring the settings are right to enable it'. We are concerned that the Government sees its role as increasingly less important than that of the private sector and is slowly withdrawing the necessary funds from climate- resilient projects that were previously being funded.

We are pleased to see recent developments relating to funding and financing the transition, including the Sovereign Green Bonds framework, Climate Emergency Response Fund, and the 2+2 Dialogue.

We Believe Government should develop a '*Whole of Government'* sustainable finance strategy. This strategy would seek to drive a broad spectrum of outcomes beyond emissions reduction, including unlocking adaptation finance, restoring nature and strengthening Aotearoa New Zealand's economic value proposition.

We believe that:

- **Collaboration is necessary and welcome. Major banks, insurers and investors have the appetite to collaborate more, and more meaningfully, to fund and finance both mitigation and adaptation through a blended finance method led by Government.**
- **A coordinated, transparent national strategy would help to provide certainty around principles and investment priorities.**
- **We need to see this action developed transparently in this term of Government.**

Key theme 6: the role of nature

The Government sees a role for nature-based solutions as part of the "least cost" transition to a low-emissions future. While exotic forestry is a central part of the ERP2 proposals, the discussion document also recognises potential for non-forest measures, including wetland restoration, coastal vegetation management and Predator Free 2050 to contribute to future emissions budgets. The Government also sees these options as potentially providing new options for landowners and businesses, incentivising land use change, and providing other environmental co-benefits.

In terms of which options to prioritise, the Government has stated it will make decisions based on affordability, scalability, scientific validation and overseas acceptance of the relevant non-forestry removals option.

The exact mechanism that will be used to deliver non-forestry removals has not yet been decided,

In our view, the development of a framework for recognition of additional nature-based solutions is likely to give rise to a number of complexities, whether delivered through amendments to the ETS, a separate voluntary carbon market or a biodiversity credit system. Any proposed solution will need to carefully consider the interaction of the system with other laws, including those relating to property rights and resource management, to ensure that the full benefits of non-forestry nature-based solutions are able to be realised.

Ends