Submission

By

Business NZ

to the

Ministry of Economic Development and the Ministry for the Environment

on the

Transitional Measures discussion paper

March 30, 2007

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‘TRANSITIONAL MEASURES’ DISCUSSION PAPER
SUBMISSION BY BUSINESS NEW ZEALAND[1]
MARCH 30, 2007

1 INTRODUCTION

1.1 Business New Zealand welcomes the opportunity to make a submission on *‘Transitional Measures: Options to move towards low emissions electricity and stationary energy supply and to facilitate a transition to greenhouse gas pricing in the future – a discussion paper,’* (referred to as “the paper”).

2 SUMMARY OF RECOMMENDATIONS

2.1 Government must ensure that no measure adopted in the transition phase should have a significant detrimental impact on the international competitiveness of New Zealand’s key producers.

2.2 Government should introduce a broad price-based measure through participation in an international emissions trading regime post-2012.

2.3 Government must commit now to a post-2012 greenhouse gas emissions allocation methodology, but only implement this when there is consistent international action.

2.4 Government must provide certainty of future obligations to sustain investment levels in new plant or technologies.

2.5 Government should adopt an intensity based allocation methodology based on benchmarking to world best practice rather than an absolute level of emissions.

2.6 Government should stimulate the introduction of a “public” voluntary emissions reduction programme with the top 300 businesses.

2.7 Government needs to determine a future path for energy supply, not only to minimise our emission levels but also to ensure a secure, low cost and sustainable supply.

2.8 Government must ensure that there are no perverse outcomes from policies intended to minimise our emission levels as these impact our future electricity prices at the same time.

[1] Background information on Business New Zealand is attached as Appendix 1.

3. BACKGROUND

3.1 The Draft New Zealand Energy Strategy to 2050 has two related discussion papers: ‘Transitional Measures’, sets out some options to move towards low emissions electricity and stationary energy supply and to facilitate a transition to greenhouse gas pricing in the future; and ‘Measures to Reduce Greenhouse Gas Emissions in New Zealand Post-2012’.

3.2 Both papers state that no measure adopted should have significant detrimental impacts on the international competitiveness of New Zealand’s key energy producers. This is based on the assumption that most of our competitors would be doing something similar post-2012, and we would therefore be able to align our action with theirs.

3.3 However, the Transitional Measures paper advocates early action in the electricity and stationary energy sector through emissions trading or a greenhouse gas charge. It’s difficult to see how there would be no detrimental impacts if either of these options were implemented.

3.4 Business NZ supports intentions to introduce a broad price-based measure (by participating in an international emissions trading regime post-2012. It also believes early action during the transitional period would be beneficial. However, it’s clear that in order to achieve the target level of GDP set by government, businesses need certainty of future obligations to sustain their investment in new plant or technologies. This means government must commit to a post-2012 greenhouse gas emissions allocation methodology now, but only implement it when there is consistent international action.

3.5 Whether this methodology is based on intensity or absolute emissions, the outcome will be similar. With no further intervention, our key industries and thermal generators will evaluate the costs and benefits of early action or a do-nothing approach. The introduction of a “public” voluntary emissions reduction programme will encourage early action and while it would be targeted at our largest emitters, there’s no reason why the top 300 businesses in New Zealand cannot participate.

3.6 Business NZ supports an intensity based methodology based on benchmarking to world best practice rather than an absolute level of emissions, as it is easier to align with a benchmark than to decide on an absolute value with little or no objective historical information. This approach would not preclude moving to an absolute value at some future date if there are more stringent commitments negotiated under Kyoto CP2. This is because businesses would be regularly monitoring, measuring and reporting on their emission levels and be better positioned to agree on absolute targets.

3.7 Despite our long-term commitment to reduce greenhouse gas emissions, New Zealand also needs to look ahead to ensure a secure, low cost and sustainable supply. To this end, there are strategies that need to be implemented now, regardless of our action on emission levels.

3.8 Policies intended to minimise our emission levels will also impact on future electricity prices, so it's imperative there is no perverse outcomes.

3.9 There appears to be a desire within government to stop any further building of gas fired thermal power plant, yet at the same time the government supports exploration for oil and gas. It's unlikely that international companies will see merit in exploring for oil or gas when government is sending a clear message that it wants no further use of these fossil fuels in New Zealand. If there are no further discoveries of on-shore or offshore gas, then existing gas fired power plant will be forced down the path of importing LNG. Significant investment will be required for LNG to become a viable and secure source of fuel. It is therefore likely suppliers will seek long term take-or-pay contracts, which will lock in even higher costs than existing gas supplies.

4 SPECIFIC QUESTIONS

4.1 It should be clear that Business NZ does not support the introduction of an arbitrary price on carbon ahead of our trading partners/competitors during the transition period to an international emissions trading scheme. This is reflected in our responses to the specific questions posed in paper.

4.2 Emissions Trading

4.2.1 As stated above, we do not support the early introduction of emissions trading and certainly not before our major trading partners, as this will place New Zealand exporters at a disadvantage. Nowhere else in the world are manufacturers facing the true cost of carbon and while exemptions are not explicit, as discovered at the end of the first period of the European Union Trading Scheme, an over-allocation of carbon credits ensured international competitiveness was not put at risk.

4.2.2 When an emissions trading regime is introduced there are likely to be different allocation methodologies adopted for different sectors of the economy, depending on the need to support growth and technological innovation and the ability to pass through any costs.

4.3 A CO_2 Charge (Narrow Based)

4.3.1 As with emissions trading, BNZ does not support the early introduction of a narrow based CO_2 charge as a transitional measure. The Negotiated Greenhouse Agreements, introduced by government as part of the proposed broad based carbon tax, demonstrated the gulf between economic purity and market reality when considering the actual impact of a CO_2 charge in the electricity sector.

4.3.2 Not only did this debate cover the ability to pass through, but the windfall gain accruing to existing renewable generation as well. It was clear there were insufficient funds available from a tax to compensate end users for the total cost incurred through increased electricity prices.

4.4 Renewable Obligations

4.4.1 Unlike most other countries where a renewable obligation has been introduced (and Australia is a good example of this), New Zealand has three generators who are 100% renewable and two generators who are partially renewable. This makes it extremely difficult to introduce a renewable obligation that can be realistically implemented and monitored. Add to this the fact generators and retailers are one in the same in New Zealand, and choosing where the obligation should be placed becomes a non-event.

4.4.2 In Australia, the great majority of generation was thermal and in the main coal fired. Regulatory separation between generators and retailers helps make renewable obligations placed on retailers a fairly straight-forward process that’s easy to monitor.

4.4.3 Conversely, there appears to be little value in considering renewable obligations for the New Zealand electricity market.

4.5 Incentives

4.5.1 Recent studies indicate that a capital grant is the least distortionary measure to incentivise the further development of renewable generation. Clearly, there are significant differences in the cost of renewable generation when considering, geothermal, wind, solar, hydro or marine options and over time, these relative costs will change.

4.5.2 In effect, any incentive scheme will tend to pick winners in the form of lowest cost options, but this may or may not be sensible in the longer term. It has to be appreciated that there are additional indirect costs such as frequency keeping for intermittent generation and transmission augmentation where generation is some distance from load.

4.5.3 In the same way there is a need to internalise the externalities for thermal generators it is equally important to take account of the delivered energy cost of intermittent renewable generation.

4.5.4 It is therefore clear that allowing the market to decide when, where and what type of generation is to be built is preferable to picking winners on the basis of emission levels alone.

4.6 Project-based measures

4.6.1 Project based measures are fraught with difficulty. It is inequitable to allocate credits based on the theoretical benefits to be derived from a project when, in reality, it may prove difficult or impossible to deliver on these benefits. Further, it seems inappropriate for the recipients of credits under such a scheme to on-sell these to a foreign government at a low value while our government is required to buy credits on the international market at some higher value to meet its ultimate Kyoto obligations.

4.6.2 As long as New Zealand remains in deficit under CP1 of Kyoto there is no justification for introducing a scheme that does nothing to improve that situation. If such a scheme was to be introduced, it should be directed at improving energy efficiency to reduce load growth rather than encourage renewable generation plant that, in the main, tends to be business as usual.

4.7 Regulatory measures

4.7.1 If the intent of the electricity market is to ensure security of supply at the lowest sustainable cost, then regulating to preclude certain methods of generation may deliver a perverse outcome. As indicated above, existing gas fired generators may be driven to long term take or pay contracts for LNG.

4.7.2 The Resource Management Act (RMA) has proved to be an impediment to the development of renewable generation, yet there are a number of pre-permitted sites for gas fired generation. The issue of emission levels is a global problem and government is responsible for ensuring New Zealand meet their commitments under Kyoto. Any attempt to devolve this responsibility to regional level could result in perverse outcomes dependant on the views of local authorities.

4.7.3 The RMA in its present form is neither cost effective nor capable of delivering consistent outcomes across the country. Primarily, this is due to the inability of those responsible for decision-making under the RMA to place a real cost on environmental issues. As a result, environmental issues are valued inappropriately and real economic benefits are disregarded. Tinkering with the RMA through National Policy Statements and National Environmental Standards is not the answer and neither is consolidated call-in. Either the RMA should operate as intended to weigh up the issues of economic benefit versus environmental impact at a regional level, or it should be amended to do so.

4.7.4 The issue of property rights associated with water resources is a major impediment to investment in hydro generation and the renewal process creates uncertainty for new investors and incumbents.

4.8 Voluntary measures

4.8.1 Business New Zealand supports a voluntary approach to emission reduction through the transitional phase to an international emissions trading scheme. More than 300 companies signed up publicly to the successful voluntary measures scheme run by EECA in the 1990's. This scheme targeted reductions in energy consumption rather than CO_2 emissions, but in theory the result at the time would have been the same due to the merit order dispatch methodology adopted by ECNZ. In this programme companies nominated their target reduction and in most instances achieved or exceeded that target.

4.8.2 While we accept that the current market does not guarantee thermal generation will always be on the margin in the way the ECNZ minimum fuel burn algorithm did, we believe there are benefits to encouraging businesses to voluntarily reduce their energy consumption and/or emissions.

4.8.3 To facilitate the success of a voluntary scheme during the transition phase it would be important to confirm the allocation of emission levels that would occur once an emission trading scheme was implemented post 2012. This would set the emission reduction target for individual businesses, which could then proceed with cost-benefit analysis of the options based on the likely international price of carbon.

4.8.4 Given that it's the government's stated intent to only support policy that is consistent with New Zealand's economic and sustainable development objectives and the longer-term international climate change framework, any proposal other than voluntary agreements would appear to be in conflict with that position

5 BUSINESS NZ POSITION ON CLIMATE CHANGE ISSUES

5.1 Focus on maintaining and enhancing competitiveness for all NZ businesses.

5.2 Support sustainable stewardship of the environment.

5.3 Support business moves to energy efficiency.

5.4 Support risk management approach to environmental issues.

5.5 Believe improved energy efficiency and reduced emissions make sound business sense.

5.6 Support government initiatives to participate in AP6.

5.7 Support government intent to improve energy efficiency in transport, residential and commercial sectors.

5.8 Do not support general or narrow based carbon taxes as an incentive for the development of renewable generation.

5.9 Do not support a cap on electricity generation and stationary energy plant emissions pre-2012.

5.10 Support market mechanisms to reduce emissions in step with our trading partners including the development of a methodology for a workable emissions trading scheme.

5.11 Support improvements to the RMA to achieve speedier and less costly resolution of issues impeding electricity generation, industrial and infrastructure projects necessary to sustain our economic growth and to contribute to energy efficiency.

5.12 Focus on cooperation on energy and climate change issues with local and international business organizations, individual businesses and government.

5.13 Advocate a focus for research funding in areas where New Zealand has expertise.

5.14 Promote development of an economically viable framework for selling small scale and domestically produced electricity into the market.

5.15 Promote the use of NZ engineering skills & innovation to bring Kyoto *Clean Development Mechanisms* to 3rd world countries e.g. hydro plant, wind farms (& gain carbon credits to help meet our Kyoto commitments).

5.16 Promote New Zealand's economy as energy intensive but energy efficient thus delivering goods to the global market with the lowest possible level of emissions.

5.17 Defend NZ industries against other countries and global market competitors using climate change as a border protection mechanism.

6 CONCLUSION

6.1 The Draft New Zealand Energy Strategy and its companion discussion papers, including this paper, set a timeframe that at present has no substance. The first Kyoto commitment period was set as 2008-2012 but as yet there is no agreement on what should happen beyond 2012. This means that not only do we have no fixed time frame for transition but we have no agreed forward position to transform to.

6.2 It is acknowledged that some countries, noticeably in Europe, are setting high level goals on a voluntary basis but with most countries struggling to achieve their minor obligations under Kyoto it is difficult to accept that these worthy targets have any real substance.

6.3 Further, it is acknowledged that this is a global problem and without participation from USA, Australia and the large developing countries it will be impossible to achieve the targets being set by scientists to save the planet. It is understood that the USA would not be in a position to commit to the second period before 2015 and it is doubtful that China or India will be willing to forgo their current growth rate in a short time frame. We are not proposing that we do nothing but simply pointing out that we have no set timeframe and no set target, therefore it would be prudent to ensure that any action taken in New Zealand was cost effective for business as usual as well as contributing to the global requirement to reduce emissions.

6.4 Business NZ will strongly oppose any moves to introduce regulation that focuses on one sector of the economy yet has a cost impact economy wide. Business NZ does not support the proposal to impose an artificial and totally unsubstantiated cost of carbon on both new and existing thermal generators in New Zealand when no other developed country is contemplating such a move. Any rational cost benefit analysis will demonstrate that the cost of such a proposal relative to the potential reduction in emissions is such that it would be cheaper to commit to an international buying programme.

6.5 Assuming there is an agreed framework for emissions trading at some time in the second commitment period, then the transitional period should be used to set up measuring and monitoring protocols, establish a registry to record emission levels, record emission permit allocations and trades, reach agreement on the value of plantation forests as carbon sinks and allow all sectors of the economy to road test their participation in a multi sector emissions trading scheme.

6.6 While this activity may be of assistance to government in meeting their commitments during the first Kyoto period it is clear that any liabilities should be taxpayer funded and not devolved down to businesses that had no say in the level of commitment entered into at that time. In fact, it should be remembered that this government entered the Kyoto process on the basis New Zealand had a significant surplus (NZ$500 million) and later discovered that a perverse outcome from land use policy combined with some miscalculation left a significant deficit (NZ$656 million). On that basis it would seem inequitable to impose any of that cost onto business.

APPENDIX

7 ABOUT BUSINESS NZ

7.1 Encompassing four regional business organisations (Employers' & Manufacturers' Association (Northern), Employers' & Manufacturers' Association (Central), Canterbury Employers' Chamber of Commerce, and the Otago-Southland Employers' Association), Business New Zealand is New Zealand's largest business advocacy body. Together with its 64-member Affiliated Industries Group (AIG), which comprises most of New Zealand's national industry associations, Business New Zealand is able to tap into the views of over 76,000 employers and businesses, ranging from the smallest to the largest and reflecting the make-up of the New Zealand economy.

7.2 In addition to advocacy on behalf of enterprise, Business New Zealand contributes to Governmental and tripartite working parties and international bodies including the ILO, the International Organisation of Employers and the Business and Industry Advisory Council to the OECD.

7.3 Business NZ's key goal is the implementation of policies that would see New Zealand retain a first world national income and regain a place in the top ten of the OECD (a high comparative OECD growth ranking is the most robust indicator of a country's ability to deliver quality health, education, superannuation and other social services). It is widely acknowledged that consistent, sustainable growth well in excess of 4% per capita per year would be required to achieve this goal in the medium term.