

SUBMISSION ON

Market Governance of ETS

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To: Ministry for the Environment

Name of Submitter: Horticulture New Zealand

Supported by: Vegetables New Zealand Inc, Tomatoes
New Zealand Inc,

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OVERVIEW

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Our submission

Horticulture New Zealand (HortNZ) thanks the Ministry for the Environment for the opportunity to submit on the Market Governance of the New Zealand Emissions Trading Scheme and welcomes any opportunity to continue to work with the Ministry for the Environment and to discuss our submission.

HortNZ could not gain an advantage in trade competition through this submission.

HortNZ wishes to be heard in support of our submission and would be prepared to consider presenting our submission in a joint case with others making a similar submission at any hearing.

The details of HortNZ's submission and decisions we are seeking are set out in our submission below.

HortNZ's Role

Background to HortNZ

HortNZ represents the interests of approximately 5,500 commercial fruit and vegetable growers in New Zealand who grow around 100 different fruits, and vegetables. The horticultural sector provides over 40,000 jobs. The value of the horticulture industry is 6.9 billion.

There is approximately, 80,000 hectares of land in New Zealand producing fruit and vegetables for domestic consumers and supplying our global trading partners with high quality food.

It is not just the direct economic benefits associated with horticultural production that are important. Horticulture production provides a platform for long term prosperity for communities, supports the growth of knowledge-intensive agri-tech and suppliers along the supply chain; and plays a key role in helping to achieve New Zealand's climate change objectives.

The horticulture sector plays an important role in food security for New Zealanders. Over 80% of vegetables grown are for the domestic market and many varieties of fruits are grown to serve the domestic market.

HortNZ's purpose is to create an enduring environment where growers prosper. This is done through enabling, promoting and advocating for growers in New Zealand.

Executive Summary

HortNZ supports a robust market governance framework with a regulator to ensure the efficiency, integrity and confidence in the NZU (New Zealand Units) market.

Our growers are concerned that extra regulation of a market to trade NZU's will result in an extra administrative burden. Growers receiving free industrial allocations of NZU's who wish to trade these in a market situation need to be able to do so without an overly burdensome administrative process.

Our submission is structured around the four topics and are focused on the following:

- HortNZ would like growers, particularly those growers receiving free industrial allocations to be able to continue the current practice of surrendering units to genuinely off-set carbon costs direct to energy suppliers.
- Growers receiving free industrial allocations of NZU's may need to purchase additional units to off-set total emissions. Minimum NZU bundles need to be small enough to facilitate practical use for growers that works within their current business practice and cashflow. This is especially important if smaller growers are unable to transfer industrial allocations direct to suppliers and need to sell units through a separate process.
- HortNZ believe horticultural businesses who receive free allocations and participate in the scheme have dedicated in-house knowledge, such as accountants and finance teams, or use external specialist consultants. To require trades of units to occur via a financial advisor places an additional cost and process, growers should be able to trade NZU's in their own right.
- HortNZ supports the position that no further AML/CFT Act obligations would apply to the NZU market beyond what already applies today. This highlights how the AML/CFT Act already captures activities of interest within the NZU market to deter money laundering and financing of terrorism.

Submission

1. Market governance of the Emissions Trading Scheme

1.1. Overview

HortNZ supports a robust market governance framework with a regulator to ensure the efficiency, integrity and confidence in the NZU market.

HortNZ is mindful that there needs to be some level of regulation to prevent the abuse of a new market and provide security for those participating in the purchase and sale of NZU's. HortNZ wants to ensure the administration associated with the trade of NZU's – particularly those received as free allocations is simple, transparent and easily accessible for growers.

Feedback from growers with experience with ETS has been that the scheme needs to be accessible for smaller minimum number of NZU's to trade and any market governance framework designed, needs to be able to cater to transactions of all sizes. Feedback from growers is the initial set up of the scheme required a lot of work, but there was a seminar held which was helpful. There seems to be concern that the volume threshold for trade of units (sale and purchase) is structured towards 10,000 units at a time. Smaller transactions of either singular or bundles of 100 units would be more practical and accessible for growers and easier for budgeting and cashflow.

Not all growers eligible to receive free allocations have participated in the scheme. Feedback from some growers is the administration involved with accessing free units has been, in some cases, a barrier to participation in the scheme. It is important to understand the minimum trade amount of NZU's and administrative burden plays a role in enabling or preventing participation in the scheme. In effect, growers eligible to access free allocations, who do not because the administration is complex and expensive, are financially penalised which is counter to the intention of the free allocation process for EITE¹ crops.

EITE growers accessing free industrial allocations of units are using these as per the intention of the free industrial allocation, to genuinely off-set energy input costs. This is commonly done through a process of surrendering units to energy providers each month. This system works well, has less administrative burden than trading NZU's on a market situation and supports those eligible growers to use free allocations for their intended purpose. It is important that growers continue to access free industrial allocations and can use these easily.

There has been concerns raised from growers that there may be tax implications if NZU's are only able to be traded as a financial product and want to emphasise the importance of the continued ability to surrender free allocations to energy companies, as is a current, open, transparent and fair practice.

¹ Emissions Intensive Trade Exposed

There are concerns that the EPA are slow with their processing. This combined with the legislated cut-off for applications of 30 April with no allowance for late submissions or amendments. A constant in business, especially horticultural businesses, is change. Company structures, acquisitions, sales, size is constantly changing depending on the business environment. Feedback has been that EPA struggles with the natural changes in the business world and this creates delay in processing causing stress to growers trying to meet the legislated timeframes.

The administrative rigidity needs to be addressed in any market governance framework and some flexibility allowed to ensure amendments or late requests can be submitted. The difficulty is that the submission is based on a calendar year and requires a forecast of weight of product

1.2. Topic 1: market governance options: regulating the market based on financial legislation

HortNZ believes option two² or option three³ would provide better legislative support for regulating the market.

HortNZ believes there needs to be more recent legislative tools to help regulate the NZU market. Option two, using the FMC Act (2013) with suitable modifications would be a preferred option. Alternatively, Option three⁴ (Crimes Act 1961 and market manipulation prohibitions. Use the Crimes Act to manage insider trading risks. Market manipulation would be addressed using prohibitions like those in the FMC Act. There would be no licensed market operators), would provide flexibility to address concerns around insider trading and market manipulation, while ensuring growers could participate in the scheme without having transactions facilitated by a financial advisor.

Growers, as businesses, tend to invest in financial expertise. Those growers who have participated in the scheme have dedicated in-house knowledge, such as accountants and finance teams, or use external specialist consultants. To require trades of units to occur via a financial advisor places an additional cost and process.

For growers to participate in the scheme effectively both through surrender of free allocation of NZU's and purchase of additional NZU's, there needs to be the ability to purchase smaller bundles, directly. These size transactions are needed to ensure growers can access ETS market, and are likely to be of a size or value smaller than the indicated minimum bundle size. For cashflow

² Financial Markets Conduct Act 2013 (FMC Act) with suitable modifications. Apply market manipulation prohibitions and offences to the NZU market like those in the FMC Act. Licensing requirements would apply to any facility for the trading of NZUs that met the definition of a financial product market (a licensed NZU exchange).

³ Crimes Act 1961 and market manipulation prohibitions. Use the Crimes Act to manage insider trading risks. Market manipulation would be addressed using prohibitions like those in the FMC Act. There would be no licensed market operators

⁴ Crimes Act 1961 and market manipulation prohibitions. Use the Crimes Act to manage insider trading risks. Market manipulation would be addressed using prohibitions like those in the FMC Act. There would be no licensed market operators

purposes, it is better if growers are able to access the units needed to cover their requirements for a month or remainder of a year.

1.3. Topic 2 : Regulating NZU Financial advice, transactional and/or custodial services

Option two and three provide a simpler framework for regulating the financial advice provided for retail clients participating in the trade of NZU's.

It is important to note that horticultural businesses such as covered crop growers, are likely to purchase credits in addition to the free allocations⁵ to offset emissions produced from heating their operations. Some of these growers are considered emissions intensive trade exposed (EITE) and receive free allocations of NZU's. These businesses will still be involved in the purchase of further NZU's to off-set emissions as the free allocations received partially off-set emissions generated through the production of covered crops. Currently a monthly system of surrendering units to fuel supply companies⁶ to offset emissions works well for horticultural businesses receiving free allocations. Once free allocations have been transferred, growers are likely to need to purchase additional units to offset total emissions. Minimum NZU bundles need to be small enough to facilitate practical use for growers that works within their current business practice and cashflow. This is especially important if smaller growers are unable to transfer industrial allocations direct to suppliers and need to sell units through a separate process.

HortNZ has also received feedback that the current administrative process and legislative deadlines are very difficult to work within. The EPA currently administer industrial allocations and there is no discretion to accept late or amended submissions. A constant in business is change, whether it be through acquisition, sale or restructure. This means industrial allocations can change year to year and can be difficult to estimate. The EPA as the administrative body, appears to struggle processing submissions and this creates considerable stress for EITE growers applying for their industrial allocation as time frames can be at risk of being exceeded resulting in a loss of industrial allocations for growers. Any market governance system needs to consider free industrial allocations, processing and reconciliation for these businesses, especially those with EITE crops.

HortNZ believes growers participating in the trade of NZU's, particularly those that are eligible for free allocations need to be able to participate easily and without additional barriers such as the requirement to trade through a financial advisor. Allowing a transfer of units to fuel suppliers, as is current practice, without the need for a financial advisor to facilitate the trade is sensible and practical.

Another option is to register EITE growers as authorised parties to participate in the trade of NZU's as of the free allocations process. This would enable growers to trade NZU's within a market framework or continue to transfer units.

HortNZ believes the FMA would be an appropriate regulatory body to regulate the NZU market. As part of this, it is important that any regulators provided

⁵ EITE growers receive free allocations under the current ETS. The following crops: tomatoes, capsicums, eggplant and cucumber are the only crops eligible for free allocations under ETS currently.

⁶ Heating fuels like coal and gas

with powers to investigate and enforce the rules and requirements of the NZU market

1.4. Topic 3 : Improved transaction reporting

HortNZ believes there should be an open and transparent reporting system to support the fair trade of NZU's. On this basis option two or three would provide more transparency with reporting. HortNZ would like to reiterate the importance of having any market accessible and are mindful one of the barriers to participation by growers, including those with free allocations, is the administrative burden associated with the current scheme.

Reporting) Regulations 2016 (AML/CFT Regulations). This would apply to transaction and customer details.

1.5. Topic 4 : Applying the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT) framework

Proposal: (status quo). No further AML/CFT Act obligations would apply to the NZU market beyond what already applies today. This highlights how the AML/CFT Act already captures activities of interest within the NZU market to deter money laundering and financing of terrorism.

HortNZ are supportive of an open and transparent system to support the NZU trading market. While there is a risk of any market being used inappropriately, HortNZ believes the risk of the NZU market being used inappropriately, it is still important to 'close the loop' and believe the status quo already sufficiently captures the interest within the NZU market to deter money laundering and financing terrorism adequately.