

Climate Change Response (Auction Price) Amendment Bill

Government Bill

Explanatory note

General policy statement

This Bill enables a confidential reserve price to be set for auctions in the New Zealand Emissions Trading Scheme (NZ ETS) to ensure units sold at auction cannot be sold significantly below the prevailing secondary market price and thereby avoid unduly influencing the secondary market.

The NZ ETS is one of New Zealand's main tools for helping to meet our climate change targets under the Climate Change Response Act 2002 and our international commitments under the Paris Agreement. Auctions provide a mechanism for the Government to manage the supply of emission units into the market in line with our climate change targets.

Auctions will commence in March 2021. Reforms to the NZ ETS enacted in June 2020 set out the types of decisions that the Minister of Climate Change (the **Minister**) needs to make when recommending that auctioning regulations be made. Regulations have subsequently set the schedule and rules for auctioning. The June 2020 reforms did not enable a confidential reserve price to be set.

Most of the trading in units takes place on the secondary market, which is open for trading daily. Therefore, it is the secondary market that sets the price for emission units. Auctions, on the other hand, occur infrequently and are designed to allow the Government to sell units into the secondary market without disrupting its operation.

Without a confidential reserve price, there is a risk that auction participants will strategically bid to undercut secondary market prices. This would undermine the integrity of the NZ ETS. The changes in the Bill address this risk and protect the Crown against the fiscal cost of such underpricing.

The Bill will amend the Climate Change Response Act 2002 (the **Act**) and the Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020 (the **regulations**).

The Bill will enable the Minister to specify a methodology for the auction operator to set a confidential reserve price, based on the secondary market price, in addition to existing price controls. The confidential reserve price, and methodology used to set it for each auction, must be kept confidential to ensure they do not become the target of bidding strategies that may disrupt the market. The methodology must be set in consultation with the Minister of Finance.

The Bill means that the confidential reserve price only applies to auctions whose clearing price is between the 2 price controls already set by the regulations, because it only applies to auctions that are operating in normal circumstances. Therefore the confidential reserve price will never be higher than the lowest trigger price for the auction (set at \$50 for 2021).

Specifically, the Bill will amend the Act and regulations to—

- empower the Minister to make regulations to set a confidential reserve price methodology to enable the auction operator to set confidential reserve prices at auction:
- require the Minister to consult with the Minister of Finance on the methodology:
- prevent the sale of units at auction if the final auction clearing price does not match or exceed the confidential reserve price:
- require the auction operator and any other person to keep the methodology and calculated prices confidential.

Departmental disclosure statement

The Ministry for the Environment is required to prepare a disclosure statement to assist with the scrutiny of this Bill. The disclosure statement provides access to information about the policy development of the Bill and identifies any significant or unusual legislative features of the Bill.

A copy of the statement can be found at <http://legislation.govt.nz/disclosure.aspx?type=bill&subtype=government&year=2021&no=7>

Regulatory impact assessment

The Ministry for the Environment produced a regulatory impact assessment in March 2020 to help inform the main policy decisions taken by the Government relating to the contents of this Bill.

A copy of the regulatory impact assessment can be found at—

- <https://www.mfe.govt.nz/more/briefings-cabinet-papers-and-related-material-search/regulatory-impact-statements/impact-5>

- <http://www.treasury.govt.nz/publications/informationreleases/ria>

Clause by clause analysis

Part 1 of this Bill amends the Climate Change Response Act 2002 (the **principal Act**). *Part 2* amends the Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020 (the **principal regulations**). The amendments commence on **15 March 2021**.

Amendments to principal Act

Section 30GA of the principal Act provides for regulations to be made by which the Minister may sell New Zealand units by auction and appoint auction operators to conduct the sales (under section 6A). Section 30GA is amended so that the regulations may let the Minister set a methodology that an auction operator must use to calculate a price (which may become a confidential reserve price). A confidential reserve price is the price below which New Zealand units must not be sold at a particular auction, overriding any lower minimum price prescribed under section 30GB(2)(e)(iii) (for all auctions that year). Its purpose is to prevent auction sales at prices significantly below the prices of New Zealand units sold on secondary markets so that the auction sales do not unduly affect secondary markets.

Section 30GB is amended to clarify the effect of a minimum price prescribed under that section.

Amendments to principal regulations

Regulation 15 of the principal regulations is amended to clarify that, if there is a confidential reserve price at an auction, that price (rather than the prescribed minimum price) is the lowest price at which New Zealand units may be sold at the auction.

New regulations 15A to 15C are inserted.

New regulation 15A requires the Minister to set a methodology that an auction operator must use to calculate a price that may become a confidential reserve price (if greater than the prescribed minimum price for auctions that year). The methodology can be changed at any time.

New regulation 15B requires an auction operator to calculate the confidential reserve price for an auction using the relevant methodology.

New regulation 15C requires the methodology and calculated prices to be kept confidential so that they are not disclosed to auction bidders.

Regulation 16 is amended so that a pre-auction notice must also state that the auction may have a confidential reserve price.

Regulation 33 is amended to provide that no bids are successful, and no units may be sold to bidders, if an auction's final clearing price is less than its confidential reserve price. Regulation 30 is amended for consistency with that change.

Regulation 36 is amended so that, if no bids were successful at an auction because the final clearing price was less than the confidential reserve price, then the only published auction result is a statement to that effect.

New regulation 36A is inserted. It requires an auction operator to provide information relevant to confidential reserve prices to the chief executive after an auction.

Schedule 1 is amended to insert more transitional provisions. The provisions ensure that new requirements in the principal regulations can be satisfied, or not breached, when the amendments first commence.

Hon James Shaw

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The Parliament of New Zealand enacts as follows:

- 1 Title**
This Act is the Climate Change Response (Auction Price) Amendment Act **2021**.
- 2 Commencement** 5
This Act comes into force on **15 March 2021**.

Part 1
Amendments to principal Act

- 3 Principal Act**
This Part amends the Climate Change Response Act 2002 (the **principal Act**). 10
- 4 Section 30GA amended (Regulations for auctions to sell New Zealand units)**
- After section 30GA(2), insert:
- (2A) If regulations are to be made under this section,— 15
- (a) the Minister may recommend the making of regulations that provide for the Minister to set a methodology that the person who conducts an auction must use to calculate a minimum price that,—

- (i) if the price is greater than the lowest trigger price prescribed under section 30GB(2)(e)(ii), must be recalculated as that trigger price (despite the initial calculation); and
- (ii) if the price (as recalculated or, if not, as initially calculated) is greater than the minimum price prescribed under section 30GB(2)(e)(iii), becomes the **confidential reserve price** below which New Zealand units must not be sold at the auction; and 5
- (b) the Minister must, if recommending the making of regulations under **paragraph (a)**, also recommend that the regulations—
 - (i) specify criteria for the Minister’s decision to set the methodology, including a requirement to consider the purpose of confidential reserve prices; and 10
 - (ii) specify that the purpose of confidential reserve prices is to prevent sales by auction under section 6A at prices significantly below the prices of New Zealand units sold at the time in other ways (on **secondary markets**) so that the sales by auction do not unduly affect secondary markets; and 15
 - (iii) require the methodology and any calculated prices to be kept confidential so that they are not disclosed to any potential buyer who participates in an auction; and 20
 - (iv) require the auction operator to provide the following information to the chief executive at a specified time after 1 or more auctions:
 - (A) details of the calculation of the price or prices using the methodology; and
 - (B) details of the auction bids in a form that does not identify any bidder, so that the chief executive can assess how any confidential reserve prices are working; and 25
 - (v) include any appropriate transitional provisions.

5 Section 30GB amended (Regulations about limits and price control settings for units) 30

Replace section 30GB(2)(e)(iii) with:

- (iii) the minimum price below which units must not be sold by auction, which may be zero.

Part 2

Amendments to Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020

6 Principal regulations

This Part amends the Climate Change (Auctions, Limits, and Price Controls for Units) Regulations 2020 (the **principal regulations**). 5

7 Regulation 3 amended (Interpretation)

In regulation 3(1), insert in its appropriate alphabetical order:

confidential reserve price, in relation to an auction, has the meaning given in **regulation 15A(1)(b)** 10

8 Regulation 15 amended (Price control settings for units)

In regulation 15, insert as subclause (2):

- (2) To avoid doubt, if there is a confidential reserve price at an auction, that price (rather than the prescribed minimum price) is the lowest price at which New Zealand units may be sold at that auction. 15

9 New regulations 15A to 15C and cross-heading inserted

After regulation 15, insert:

Methodology and calculation of confidential reserve prices for auctions

15A Minister must set methodology for calculating confidential reserve price

- (1) The Minister must set a methodology that an auction operator must use to calculate a price that,— 20
- (a) if the price is greater than the lowest trigger price for the auction, must be recalculated as that trigger price (despite the initial calculation); and
 - (b) if the price (as recalculated or, if not, as initially calculated) is greater than the prescribed minimum price for the auction, becomes the **confidential reserve price** below which New Zealand units must not be sold at the auction. 25
- (2) In setting the methodology, the Minister must consider—
- (a) the main matters and additional matters in section 30GC(5) and (6) of the Act; and 30
 - (b) the purpose of confidential reserve prices, which is to prevent sales by auction under section 6A of the Act at prices significantly below the prices of New Zealand units sold at the time in other ways (on **secondary markets**) so that the sales by auction do not unduly affect secondary markets; and 35
 - (c) the need for the methodology to include—

(i)	a way to determine a representative price for New Zealand units sold on secondary markets recently before the auction, taking into account any volatility in prices; and	
(ii)	a way to determine a price below the representative price that will achieve the purpose of confidential reserve prices.	5
(3)	In setting the methodology, the Minister must consult the Minister of Finance.	
(4)	The Minister—	
(a)	must ensure that the methodology is set from the commencement of this regulation; but	
(b)	may change the methodology by setting it differently at any time.	10
15B	Auction operator must calculate confidential reserve price	
(1)	The chief executive must provide the methodology to an auction operator as soon as is reasonably practicable after it is set under regulation 15A .	
(2)	The auction operator must use the methodology to calculate a price that, if greater than the prescribed minimum price for the auction, is the confidential reserve price.	15
(3)	The methodology that must be used is the one that, 2 working days before the start of the day of the auction, had been most recently provided by the chief executive.	
15C	Methodology and calculated prices are confidential	20
(1)	The auction operator, or any other person, must keep confidential the methodology and the calculated price so that they are not disclosed to any potential buyer who participates in an auction.	
(2)	To avoid doubt, as long as that information is not disclosed to any potential buyer who participates in an auction, this regulation does not prevent information from being provided (for example, under regulation 36A or to an auction monitor as defined by section 30GD of the Act).	25
10	Regulation 16 amended (Auction operator must make auction notices publicly available)	
	After regulation 16(2)(d), insert:	30
(da)	a statement that there may also be a confidential reserve price for the auction that is not known to bidders:	
11	Regulation 30 amended (Process for determining auction results)	
	Replace regulation 30(5)(b) with:	
(b)	sell units at that price if required by regulation 33 (if there are successful bids under that regulation).	35

- 12 Regulation 33 amended (Requirement to sell at final clearing price)**
In regulation 33, insert as subclause (2):
- (2) However, no bids are successful, and no units may be sold to bidders, if—
- (a) there is a confidential reserve price at the auction; and
 - (b) the final clearing price is less than the confidential reserve price.
- 13 Cross-heading above regulation 36 replaced**
Replace the cross-heading above regulation 36 with:
- Publication of auction results and provision of certain information*
- 14 Regulation 36 amended (Requirement to make auction results publicly available)**
- (1) In regulation 36(2), replace “In this regulation, **auction results** means” with “The **auction results** are”.
- (2) After regulation 36(2), insert:
- (3) However, if no bids were successful because the final clearing price was less than the confidential reserve price, the **auction results** are solely a statement to that effect.
- 15 New regulation 36A inserted (Requirement to provide information relevant to confidential reserve price)**
After regulation 36, insert:
- 36A Requirement to provide information relevant to confidential reserve price**
- The auction operator must, as soon as is reasonably practicable after an auction, provide the following information about the auction to the chief executive:
- (a) details of the calculation of the price using the methodology set under **regulation 15A**; and
 - (b) the bid volume and bid price of each bid in a form that does not identify the bidder.
- 16 Schedule 1 amended**
In Schedule 1, after Part 1,—
- (a) insert the Part set out in **the Schedule** of this Act as the last Part; and
 - (b) make all necessary consequential amendments.
- 17 Schedule 3 amended**
In Schedule 3, table of price control settings, column 2, replace the heading with “**Minimum price below which units must not be sold by auction (\$)**”.

Schedule
New Part 2 inserted into Schedule 1 of principal regulations

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	Part 2	
	Provisions relating to Climate Change Response (Auction Price) Amendment Act 2021	5
3	Meaning of amendments	
	In this Part, amendments means the amendments made to these regulations by the Climate Change Response (Auction Price) Amendment Act 2021 .	
4	Setting and providing first methodology	10
	Actions done for the following purposes are taken as having been done under the amendments, even if they are done before the amendments commence or are enacted:	
	(a) setting the first methodology under regulation 15A , to ensure that regulation 15A(4)(a) is satisfied; and	15
	(b) providing the first methodology to an auction operator under regulation 15B , to ensure that regulation 15B is satisfied.	
5	Auction notice for early auction	
	If an auction is held within 30 days after the amendments commence, the notice under regulation 16 need not include the statement in regulation 16(2)(da) .	20