

20 May 2021

Cassidy McLean-House  
Ministry for the Environment  
By email to [mitigation@mfe.govt.nz](mailto:mitigation@mfe.govt.nz)

Dear Cassidy

### Phasing out fossil fuels in process heat

1. This is a submission by the Major Electricity Users' Group (MEUG) on the Ministry for the Environment (MfE) consultation document "Phasing out fossil fuels in process heat – National direction on industrial greenhouse gas emissions (GHG)," 8<sup>th</sup> April 2021.<sup>1</sup>
2. MEUG members have been consulted in the preparation of this submission. This submission is not confidential. Members may make separate submissions.
3. The consultation paper has a sub-section titled "The New Zealand Emissions Trading Scheme (NZETS) is the Government's primary intervention into process heat investment (the status quo)."<sup>2</sup> MEUG agrees the NZETS, now it is an effective cap-and-trade mechanism, should be the primary means to ensure efficient investment and divestment decisions across all sectors of the economy to achieve GHG policy objectives.
4. There are three rationale in the consultation document for proposing a new national direction instrument:
  - a) Preliminary modelling indicates non-ETS intervention is needed.
  - b) The presence of barriers at prevailing Carbon prices supports interventions.
  - c) Political election manifesto promises.
5. The following sections discuss each rationale.
6. The concluding section discusses the process to date and going forward.

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<sup>1</sup> Document URL [https://consult.environment.govt.nz/climate/phasing-out-fossil-fuels-in-process-heat/supporting\\_documents/phasingoutfossilfuelsinprocessheat.pdf](https://consult.environment.govt.nz/climate/phasing-out-fossil-fuels-in-process-heat/supporting_documents/phasingoutfossilfuelsinprocessheat.pdf) at <https://consult.environment.govt.nz/climate/phasing-out-fossil-fuels-in-process-heat/>.

<sup>2</sup> Consultation document, p16-17.

### Preliminary modelling indicates non-ETS intervention is needed

7. Page 15 of the consultation document reports results of MfE “preliminary modelling” indicate non-NZETS intervention is needed. That modelling assumed a C-price of \$35/t. MEUG believes that price should be reviewed in the light of most (if not all) expert views that C-prices will increase substantially above \$35/t. Therefore, preliminary modelling results have materially underestimated the effect of actual increases and expectations of future increases in C-prices on the divestment/switching/investment decisions of existing and new process heat businesses. Accordingly, MEUG recommends:
  - a) MfE reconsider the best mix of proposed RMA interventions after new evidence and updated modelling with higher C-prices are available. The final report of the Climate Change Commission should also provide further evidence and modelling of the relative future effect of NZETS and non-NZETS interventions.
  - b) As a default, less interventionist options should be chosen because the modelling to date is likely to have materially understated the effectiveness of the NZETS in facilitating the phase out of fossil fuels in process heat.

### The presence of barriers at prevailing Carbon prices supports interventions

8. The first sentence on page 17 of the consultation document states:

“But there are also many emissions reductions options available that are not responsive to the NZ ETS price signal, due to the presence of barriers at the prevailing price level.”
9. There is no discussion of what those perceived barriers are. If there were “barriers,” then for those to be considered a justification for a national direction instrument:
  - a) They must be clearly defined and the detriment they cause quantified.
  - b) All feasible policy options to address the detriment should be identified, including a national direction and the expectation of rising Carbon prices using the NZETS.
  - c) A robust analysis of the pros and cons of those options identifying the specific benefit that only a national directive will achieve compared to other policy options.
10. MEUG is concerned the use of the phrase “barriers” to infer a market failure has frequently been used in either a naïve fashion through to a deliberately deceptive manner when there are no explicit market failures other than whether current and expected future C-prices reasonably reflect the economic externality cost. The “barriers” often talked about are not true economic barriers; rather they are barriers for some parties, but not other parties, found in normal commercial markets from time to time.
11. There are many commercial factors that investors consider when investing in new, retrofitting or modifying existing process heat applications or switching fuels. An important commercial barrier to electrification is the current price for spot and hedge contracts and observed high prices of futures contracts. Removing non-market barriers to improve supply in the electricity sector, such as RMA consenting barriers and undue time delays, would be a far better topic to consider for a new national direction.

## Political election manifesto promises

12. The last rationale for the consultation document is the political promise in the opening message from the Minister that,

“The Government is delivering on a key election commitment to tackle climate change, by banning new low and medium temperature coal-fired boilers.”<sup>3</sup>

This appears to be the primary reason for the paper.

13. The Minister’s election commitment has four elements. Comments on each follow:
- a) First a ban. MEUG does not support a ban when other policy instruments might achieve the same outcome. This leads back to the discussion beforehand that until we see the final modelling using a realistic expectation of rising C-prices, it is too early to be sure the NZETS alone will not achieve an appropriate rate of phasing out coal use for process heat.
  - b) Second the ban is to apply to new boilers. If you must ban an activity, then constraining that to new activities is a least-harm approach. MEUG does not support the consultation document expanding the ban to re-consenting existing boilers. Again, the primary policy instrument, the NZETS, may have a greater impact than expected in the preliminary modelling undertaken by MfE. Other factors will also be driving existing users to switch fuels including lower capital and fuel costs for alternatives and a diminishing service support ecosystem for maintaining old coal-boilers. And as mentioned in paragraph 11 above, the current and near-term expected high cost of electrification.
  - c) Third the ban is to apply to new low and medium boilers. The consultation document excludes high temperature boilers and MEUG supports that approach.  
  
A hard and fast rule for what is a high temperature versus medium temperature fossil fuel boiler would inevitably lead to anomalies. For this reason, consenting agencies should be given more guidance to make decisions than arbitrary demarcation rules.
  - d) Fourth the new boilers to be banned are coal-fired. MEUG notes that many of the options considered in the consultation document go beyond the election commitment to focus on coal-fired boilers and other fuels are also considered. MEUG does not support a new national direction instrument covering other fuels because they are not in the election commitment. Other government policies, such as the ban in new offshore and onshore petroleum exploration will also affect the price of other fuels, namely gas and LPG.  
  
Notwithstanding the point in this sub-paragraph that other fuels other than coal were not mentioned in the election promise; we iterate MEUG does not support measures that explicitly ban coal either.

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<sup>3</sup> Ibid, p5.

### Comments on process to date and going forward

14. MEUG looks forward to MfE considering submissions and consulting on the s.32 evaluation report in drafting a recommendation for Ministers to consider promulgating a national direction instrument. Separately we have requested two things. First advice from the Ministry on the background and decisions on how to progress a new national direction given options available in the Act. Second early publication of submissions in this consultation round to allow rebuttal evidence to be tabled where relevant to assist MfE consider this proposal.

Yours sincerely



Ralph Matthes  
Executive Director