

Advice on NZ ETS unit limits and price control settings for 2026–2030

Technical annex 3: Assessment of accordance

April 2025



Introduction

This document is published by He Pou a Rangi Climate Change Commission as a supplementary document to our Advice on NZ ETS unit limit and price control settings (NZ ETS settings) for 2026–2030 (the advice report).

He Pou a Rangi Climate Change Commission is an independent Crown entity established by the Climate Change Response Act 2002 (the Act) to provide expert, evidence-based advice and monitoring to successive governments on how to reduce emissions and adapt to the effects of climate change.

About this document

As part of its responsibilities under the Act, the Commission is required to provide the Government with annual advice on the unit limits and price control settings for the New Zealand Emissions Trading Scheme (NZ ETS settings) for five years into the future.

The Commission’s recommendations must adhere to the same requirements in the Act that apply to the Minister, which are set out in section 30GC of the Act.¹ This means that we must be satisfied that the recommended unit limits and price control settings accord with emissions reduction targets – emissions budgets, nationally determined contributions (NDCs) and the 2050 target (see next section for more information).

This document sets out in detail our assessment of how our recommendations comply with the accordance requirements in section 30GC of the Act.

This document should be read alongside the Commission’s advice report on NZ ETS settings for 2026–2030. The report includes *Appendix A*, which summarises how the Commission has addressed the wider set of requirements and matters in the Act relevant to the NZ ETS settings advice. *Appendix A* documents how the Commission has fulfilled its broader obligations under the Act, whereas this document focuses on the specific issue of how the Commission’s recommended settings accord with emissions reduction targets.

¹ Section 5ZOA also requires us to adhere to the requirements of s30GB that apply to the Minister. That section sets out the scope and timing of the unit limits and price control regulations, and when regulations may be changed. It is addressed in the main report.

According NZ ETS settings with targets

When recommending the unit limit and price control settings for the NZ ETS, the Commission must be satisfied that either:

- the settings strictly accord with all emissions budgets and NDCs currently in place, and with the 2050 target (collectively, ‘emissions reduction targets’) (section 30GC(2)); or
- if the settings do not strictly accord with the emissions budgets or the NDC, that they nevertheless still accord with the emissions budget or NDC, and that the discrepancy is justified after considering prescribed statutory matters (section 30GC(3)).

For clarity, the specific obligations from sections 30GC(1)-(3) are set out in Box 1 below.

Box 1. Requirement that NZ ETS settings accord with emissions reduction targets

Section 30GC Requirements for regulations about limits and price control settings for units

- (1) The Minister must comply with this section in—
 - (a) recommending under section 30GB(2), (3), or (4)(b) the making of regulations that prescribe individual limits, overall limits, or price control settings; and
 - (b) considering under section 30GB(4)(a) whether to recommend prescribing new individual limits, overall limits, and price control settings for the 2 calendar years before a further calendar year.
- (2) The Minister must be satisfied that the limits and price control settings are in accordance with—
 - (a) the emissions budget, and the nationally determined contribution for New Zealand under the Paris Agreement, that applies to—
 - (i) the period for which the limits or price control settings are being prescribed; or
 - (ii) any period after that, if a budget or contribution exists for that period; and
 - (iii) the 2050 target.
- (3) However, they need not strictly accord with the budgets or contributions as long as the Minister is satisfied that the discrepancy is justified, after considering the other matters under this section.

Approach to accordance

We understand that ‘strict accordance’ equates to settings with a high probability of constraining emissions to the levels required for meeting emissions reduction targets. The Commission is permitted to recommend settings that do not provide this, with respect to the emissions budgets and NDCs in place, but in such case the settings must nevertheless

accord – i.e. there must still be a good probability that the settings will achieve what is necessary, or the discrepancy must be one that can be made up for elsewhere. The deviation from strict accordance must also be justified, after considering the matters set out in sections 30GC(5) and (6).

Assessing accordance must be done by considering the whole package of settings, i.e. the unit limits and the price control settings together, because their effects on emissions are interdependent.

Determining the extent to which potential NZ ETS settings accord with emissions reduction targets requires considering the likelihood of achieving targets, including assessing the risks and mitigations. This necessarily involves considering projections of emissions and factors affecting emissions for some years into the future, which are inherently uncertain. This requires us to make reasonable judgements and assumptions about Aotearoa New Zealand's future emissions trends, and the effects of policies and other factors on emissions, based on the best available evidence.

We have therefore assessed the accordance of our recommended settings by drawing on a range of analysis and evidence, and considering all matters prescribed by the Act.

For determining unit limits that align with emissions reduction targets, we have applied the seven-step methodology that has been developed over several years for this purpose. This methodology has been designed to factor in various matters that we must consider under the Act. For example, it incorporates consideration of projected emissions trends, including those to which the NZ ETS does and does not apply (s30GC(5)(a)) (in steps 1 and 2); the proper functioning of the NZ ETS (s30GC(b)) (there are several aspects to this, one example being how industrial allocation rules apply, in step 4); international climate change obligations and contracts for accessing emissions reductions in other carbon markets (s30GC(c))(in steps 1 and 6); and the forecast availability and cost of ways to reduce emissions (s30GC(d)) (in steps 1 and 2).

For the price control settings, we have drawn on modelling, both that commissioned by us from Concept Consulting and modelling undertaken by the government, to inform our judgements about the emissions prices needed to meet targets. We considered the government's recent emissions projections (s30GC(5)(a)), and research and analysis of the cost of specific mitigation options such as afforestation and the decarbonisation of industrial process heat (s30GC(5)(d)). We looked at how the NZ ETS was functioning (s30GC(5)(b)), including by gathering information and insights from engaging with NZ ETS market participants. We examined evidence available about international emissions prices and the cost of offshore mitigation (s30GC(6)(b) and s30GC(5)(c)), and about the impacts of emissions prices on households and the economy (s30GC(6)(a)). We also factored forecast inflation into the price levels of the price control settings, and considered the effect of the NZ ETS emissions price itself on inflation (s30GC(6)(c)).

These are examples, not an exhaustive account of how these matters have been considered as required by the Act. For more information, see *Part 3: Te herenga utu – Unit limits*; *Part 4:*

Te ritenga taura-utu – Price control settings; and Appendix A: Summary of how legislative requirements and considerations under the Act have been addressed in the advice report, as well as *Technical Annex 1: Unit limits* and *Technical Annex 2: Price control settings*.

Where possible, we have incorporated uncertainty into our consideration of these matters and our judgements about the settings.

In determining our recommendations, we applied an adaptive management lens to consider the uncertainties inherent in the data and information we use, and how the settings could be updated as this information changes over time. This can be seen throughout the advice. Examples include how we considered risks and sensitivities in step 7 of the unit limits method, and with respect to the price control settings, how uncertainties about the emissions prices needed to meet the third emissions budget might resolve with time. We consider this to be consistent with the system for managing the settings established by the Act, which provides for the settings to be extended and updated each year.

Accordance assessment of the recommended settings

Table 1 below contains our assessment of how the Commission’s recommended unit limits and price control settings for the NZ ETS accord with emissions budgets, the NDC and the 2050 target. Where relevant, it provides our justifications for discrepancies from strict accordance, and cites the most important matters from the Act supporting the justification. As noted in the previous section, our consideration of all required matters in the Act can be understood by consulting the Commission’s full advice, particularly the advice report and its *Appendix A*.

Table 1: Assessment of accordance of the Commission’s recommended settings with emissions reduction targets as per section 30GC

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
Emissions budget 1 (2022–2025)	
Not applicable. The recommended settings apply to 2026-2030, so by the time they enter into force, the first emissions budget will have finished.	Not applicable.
Emissions budget 2 (2026–2030)	
<p>The recommended unit limits have been derived from the emissions level (and NZ ETS emissions cap, representing the level of effort required from sectors covered by the NZ ETS) for 2026-2030 given by the emissions projections in the Government’s second emissions reduction plan. This is lower than the notified level of the second emissions budget. Aligning the settings with an emissions constraint that is more stringent than the budget increases the probability that the budget will be met.</p> <p>There is a surplus of units in the NZ ETS, which poses a risk of allowing emissions from NZ ETS sectors that exceed the second emissions budget (discussed in <i>Part 3: Te herenga utu – Unit limits</i> in the advice report). To mitigate this risk, our recommended unit limit settings reduce the auction volumes in a way that is designed to reduce the surplus units to zero by 2030, the final year of the budget. This is based on our central estimate of the surplus, calculated in step 5 of the unit limits</p>	The settings strictly accord with meeting the second emissions budget. The settings provide a high probability of limiting emissions to the necessary level.

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>methodology.</p> <p>There are still risks to achieving the second emissions budget, but these risks can be managed. Key uncertainties relate to the forecast of emissions not covered by the NZ ETS, and to the estimated surplus units:</p> <ul style="list-style-type: none"> • If emissions outside the NZ ETS (mainly biogenic methane and nitrous oxide emissions from agriculture) turn out in reality to be higher than forecast, sectors within the NZ ETS would have to reduce emissions by more to enable the second emissions budget to be met. • If the surplus is higher than our central estimate, more units could be available for use by emitters, and could allow emissions above the emissions cap for 2026-2030. <p>As noted above, the emissions cap for the NZ ETS is based on emissions projections which, overall, are 2 Mt below the level of the second emissions budget. This provides some buffer for emissions outside the NZ ETS to be higher than expected while still meeting the second emissions budget.</p> <p>Additionally, our recommended unit limit settings backload auction volume into the later years of the period, with much of the available auction volume to be distributed in 2029 and 2030. Under the rules in the Act (barring special circumstances), the auction volumes in these years can be adjusted when the settings are updated in 2026 (can adjust both 2029 and 2030) and in 2027 (can only adjust 2030). This preserves the ability to adjust auction volumes downwards in future updates to the regulations, so that the settings can continue to accord with the second emissions budget if the surplus is later reassessed to be larger than our current central estimate.</p> <p>The auction reserve price (ARP) levels we recommend for 2026-2030 are in line with the minimum prices we have assessed as necessary to support achievement of the second emissions budget. This is based on the lower bound of the cost of gross emission reductions in Aotearoa New Zealand, rather than costs related to forestry – because by 2026 it will be too late for further forest planting to assist with meeting the second emissions budget. The ARP helps discourage the emissions price from dropping to levels below those likely needed for meeting the second emissions budget, by preventing additional units being sold into the market when prices are below the ARP level.</p> <p>The recommended cost containment reserve (CCR) trigger prices are above the likely cost of abatement needed to meet the second emissions budget. This is based on a range of evidence</p>	

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>generated by the Commission,¹ EECA,² and MfE³ (see the advice report for further information), which indicates that in Aotearoa New Zealand a significant amount of gross emissions reductions are economic at prices below \$200/tonne.</p> <p>The government’s modelling carried out as part of developing the second emissions reduction plan also provides assurance that the recommended CCR trigger prices are consistent with achieving the second emissions budget. This modelling projected that the second emissions budget could be met with an NZU price path rising to \$95.66 in 2030 (in 2024 dollars). This price is comfortably below the first trigger price applying in that year (\$219 in 2024 dollars), with substantial headroom for the price to range higher if necessary.</p> <p>Overall, we consider that the CCR trigger prices are at a high enough level that there is a very low risk that the CCR would be triggered and release more units to the market, which would be detrimental to accordance with the second emission budget</p>	
Emissions budget 3 (2031–2035)	
<p>The third emissions budget starts in 2031 and so is beyond the timeframe of the settings recommended in our advice, which cover 2026-2030.</p> <p>We nevertheless still need to consider how the unit limits until 2030 will enable future unit limits that are consistent with meeting the third emissions budget.</p> <p>The Commission’s recommended unit limit settings until 2030 are designed to eliminate the surplus units from the NZ ETS by 2030, based on our central estimate of the surplus. If successful, this will mitigate the risk that surplus units could enable emissions above the third emissions budget. Similar options exist to manage the risk of a larger surplus than the central estimate, as discussed in the previous section on the second emissions budget.</p> <p>Current projections of emissions are higher than the level of the third emissions budget over 2031-2035. Where relevant, in our application of the methodology to determine the unit limits, we have adjusted for this and assumed an emissions pathway requiring greater emissions reductions from NZ ETS sectors. For example, in step 5 in the unit limits methodology, to calculate the units that</p>	<p>The settings do not strictly accord, but nevertheless accord with a discrepancy, with the third emissions budget.</p> <p>We consider there is a good probability that the recommended settings will enable future settings that limit emissions to the required level over 2031-2035 to meet the third emissions budget.</p> <p>The discrepancy from strict accordance relates to the price control settings. There is some evidence that the CCR price triggers and ARP levels may be lower than the NZU prices needed to meet the third emissions budget in some scenarios of the future. However, this is a risk that may not materialize, because there is a high level of uncertainty about whether the future will play out in line</p>

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>emitters will need for hedging in 2030, we have used an emissions path that is consistent with the third emissions budget, rather than the government’s latest emissions projections.</p> <p>Due to the forward-looking nature of price formation in the NZ ETS, we also need to consider the emissions prices that may be needed to meet the third emissions budget.</p> <p>We commissioned modelling from Concept Consulting that used different scenarios in the <i>Energy and Emissions in New Zealand</i> (ENZ) model to generate shadow emissions prices necessary to meet the third emissions budget. These scenarios took into account the Government’s second emissions reduction plan (ERP2), but varied some assumptions to examine the effects of policy uncertainty, as well as uncertainty in baseline emissions and mitigation costs. We also examined, through a desktop analysis, the effect that different afforestation rates between now and 2031 could have on the emissions prices needed to meet emissions budget three.</p> <p>Examining this evidence showed that, in some scenarios of the future, the Commission’s recommended price control settings could be too low to be consistent with meeting the third emissions budget. These are scenarios where afforestation before 2031 is in line with the levels assumed in the government’s ERP2 emissions projections, so further gross emission reductions are needed over 2031-2035 to meet the third emissions budget, and where fossil gas prices are relatively low. In these scenarios, the Concept Consulting modelling suggests an NZU price range of around \$190 to \$350 in 2035 (in 2024 prices). When discounted back to the present, the upper and lower bounds of this price range are well above the trajectories of the current ARP and CCR trigger price levels. This can be seen in figure 4.1 in the advice report.</p> <p>However, the current CCR and ARP levels, if extended along their existing trajectories, could be sufficient if gas prices in the future are higher than assumed in ERP2, and/or if afforestation rates are higher than assumed in ERP2 over the period until 2031.</p> <p>A key insight from the Concept Consulting modelling was that high fossil gas prices were a key factor that could significantly reduce the emissions price needed to meet the third emissions budget. Recent material declines in fossil gas production and reserves saw high fossil gas prices through winter 2024. How the fossil gas price will develop is very uncertain, but it seems more likely over coming years that the prices could be higher rather than lower.</p>	<p>with these high emissions price scenarios.</p> <p>We have considered all the relevant matters in the Act. We consider that this discrepancy from strict accordance is justified, by the following considerations in particular:</p> <ul style="list-style-type: none"> • s30GC(5)(d) – the forecast availability and cost of reducing GHG emissions to meet targets. Specifically, there is large uncertainty over the costs of reductions to meet the third emissions budget, and, due to timeframes, increasing the CCR price triggers and ARP can be delayed until this uncertainty has reduced, without jeopardising achievement of the third emissions budget. • s30GC(5)(b) – the proper functioning of the NZ ETS. This includes considering the importance of regulatory predictability in supporting confidence in the market and to invest. We consider it important for the effectiveness of the NZ ETS that the price settings are not changed unnecessarily, and if there is a need to do so, the change should be signalled as much in advance as possible. Our advice supports this by not recommending changes to the price control settings when it is highly uncertain that this is needed, but rather signalling that depending on how key factors (such as afforestation rates) evolve over the coming years, these settings may need to be increased in future. • s30GC(5)(f) – any other matter the Commission

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>ERP2 assumed afforestation averaging around 35,000 hectares annually over the period leading up to 2030, but how much land will actually be afforested is uncertain. In particular, ERP2 included two key forestry-related policies, one about afforestation on Crown land and another on limiting, by land use capability (LUC), the land that can register into the NZ ETS for forestry. It is unclear how these policies will affect afforestation rates over the coming years. Our desktop analysis suggests that if afforestation is 15,000 hectares per year higher than assumed in ERP2 over 2027-2031 (i.e around 50,000 ha per year), this would deliver the higher levels of CO₂ removals by forests over 2031-2035 needed to fill the abatement gap to meeting the third emissions budget. A planting rate of 50,000 hectares per year is high, but not implausible. Afforestation rates were 40,000 – 70,000 per year over 2021-2023.^{ii, 4}</p> <p>Government estimates of the marginal cost of afforestation centre around \$50/tonne CO₂ within a range of \$25-\$75/tonne CO₂.⁵ Higher planting rates, even if not reaching the full further 15,000 hectares per year, could significantly bring down the emissions prices needed to meet the third emissions budget, especially if also combined with fossil gas prices that are higher than the government’s assumptions. See <i>Part 4: Te ritenga taura-utu – Price control settings</i> in the advice report for more information about these issues.</p> <p>We considered whether the evidence above, about higher prices potentially being needed to meet emissions budget three, justifies increasing the price control settings. Our judgement was that it would be premature to increase the price control settings now, when it is very uncertain that this will actually be needed. Factors influencing this assessment included:</p> <ul style="list-style-type: none"> • That NZU prices are currently low compared to the price control settings (with the spot price at the time of writing being around \$60, below the \$68 ARP for 2025). The current settings provide significant room for the market price to range higher to help meet the second emissions budget and lay the foundations for meeting the third emissions budget. Given uncertainty, as well as the current state of the market, it appears unlikely that the potential need for higher prices in the 2030s could start to be reflected in current NZU 	<p>considers relevant. We consider it relevant that the framework of the Climate Change Response Act does not require a plan be in place to meet the third emissions budget yet, and that policies will continue to evolve over time. This supports our assessment that it is acceptable to wait until some uncertainty is resolved before making a judgement that the price control settings need to increase, despite some evidence that they could be too low.</p> <p>We have considered the other matters included in section 30GC, and consider them to be less relevant:</p> <ul style="list-style-type: none"> • s30GC(5)(a) – projected trends of emissions over the next five years. Projections of emissions inside and outside the NZ ETS over the next five years do not cover the third emissions budget period. Projections of emissions beyond this period have identified a gap to meet the third emissions budget. This gap can be addressed in unit limits that apply to the period. • s30GC(5)(c) – international climate change agreements and offshore mitigation. Offshore mitigation is less relevant to meeting the third emissions budget, since budgets must be planned to be met domestically (s5W and s5Z), although it is relevant to the price control triggers that may be

ⁱⁱ The afforestation rate for 2023 is a provisional estimate.

Summary analysis of accordance of the recommended settings for 2026-2030 with targets

Conclusion, with justification for any discrepancies

prices, causing the CCR to be triggered.

- Government policy to meet the second emissions budget and contribute to meeting the third emissions budget is still evolving, with uncertainty over the details of key policies (such as that on afforestation on Crown land). The Government is also not required to have a plan for meeting the third emissions budget until 2029.
- The mix of actions and the associated emissions prices needed to meet the third emissions budget are currently very uncertain, but this uncertainty will reduce over the coming years.
 - The impact of recent high fossil gas prices on emissions trends, and the potential for continuing high fossil gas prices, will become clearer.
 - Potentially more importantly, the likely afforestation rates until 2031 will be much clearer in two to three years' time, after key forestry-related policies have been finalised and more data about planting in the years to 2031 becomes available, for example from afforestation intentions surveys.

We will monitor the risk that higher prices may be needed to meet the third emissions budget. If adjustments are required to the price controls so that the NZ ETS settings can continue to accord with the third emissions budget, we can still recommend that they be made well ahead of 2031, the beginning of the budget period.

needed.

This discrepancy relates to the price control settings, to which the additional considerations in section 30GC(6) also apply:

- s30GC(6)(a) – impacts on households and the economy. We have considered the impacts on households and the economy in recommending price control settings. We consider that these impacts can best be managed using policies separate from the NZ ETS.
- s30GC(6)(b) – level and trajectory of international emissions prices. We consider that the recommended price triggers are not out of step with the level of and trajectory of international emissions prices. The NZ ETS is not currently linked to any international emissions markets.
- s30GC(6)(c) – inflation. We considered the impact of inflation in recommending the price control settings. We adjusted our recommended ARP and CCR price triggers for forecast inflation. We have considered the likely impacts of the NZ ETS on inflation in recommending the price control settings.

First nationally determined contribution (2021–2030)

The proposed settings align with achieving the domestic emissions reductions and removals set out in the Government's second emission reduction plan. This level is 84-89MtCO₂e higher than the

We consider that the settings generally accord with the first NDC as they align with the planned domestic contribution to it. We consider that the discrepancy from

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>level of the first NDC.</p> <p>The Government, in submitting the first NDC in 2016 and in revising it in 2021, expected to use reductions of gross emissions, carbon dioxide removals by forests, and offshore mitigation to meet it.⁶</p> <p><u>Role the NZ ETS plays in meeting the first NDC</u></p> <p>The NZ ETS provides a financial incentive to limit domestic net emissions in covered sectors – stationary energy, industry, transport, waste and forestry. The Government has said in ERP2 that the NZ ETS is the Government’s main policy tool to reduce net emissions to meet emissions budgets. The Government expects that the NZ ETS, in combination with other policies, will limit net emissions over the NDC1 period to 663-668 Mt CO₂e.</p> <p>The allowed emissions for the first NDC are estimated at 579 Mt CO₂e.⁷ The Government expects to need 84-89Mt of offshore mitigation to meet the first NDC.</p> <p><u>Viability of accessing offshore mitigation</u></p> <p>Offshore mitigation to meet NDCs can be accessed in two ways:</p> <ul style="list-style-type: none"> • Through bilateral agreements with other parties to the Paris Agreement under Article 6.2 • Through a central mechanism for trading mitigation outcomes established under Article 6.4 <p>So far, the Government has not announced any completed arrangements that would deliver offshore mitigation towards the first NDC. The Government has said it is working to acquire this mitigation, and there is evidence that work is indeed underway.⁸ The Biennial Transparency report released in December 2024 details relationships the Government is fostering with several countries Aotearoa New Zealand could partner with for mitigation.⁹</p> <p><u>Article 6.2 bilateral agreements for cooperating on offshore mitigation</u></p> <p>Accessing offshore mitigation under Article 6.2 requires parties to establish bilateral arrangements between themselves for the funding, implementation and verification of mitigation. Any mitigation credited (internationally traded mitigation outcomes – ITMOs) to one party requires a</p>	<p>strict accordance is justified since it can be made up for elsewhere, and the Government has stated its intention to do so via offshore mitigation.</p> <p>While there is limited time remaining within the period of the first NDC, we consider that it is viable for the Government to acquire the offshore mitigation needed to meet the first NDC.</p> <p>Having considered all of the relevant matters in the Act, we consider that continuing to align the settings with achieving emissions budgets reflects a discrepancy from strict accordance with the first NDC that is justified by the following considerations in particular:</p> <ul style="list-style-type: none"> • s30GC(5)(d) - the forecast availability and cost of reducing GHG emissions to meet targets. Attempting to meet the first NDC domestically would require emission reductions at a scale and pace that would impose severe economic and social consequences on people, businesses, iwi/Māori and communities. • s30GC(5)(b) - the proper functioning of the NZ ETS. The NZ ETS does not currently cover all of Aotearoa New Zealand’s emissions. The NZ ETS does not cover enough emissions, and there is not enough time remaining in the first NDC period, for the NZ ETS to deliver the scale of emissions reductions to bridge the gap to meet it. In addition, design features of the NZ ETS mean that restricting auction volumes to a high degree in the short-term would be unlikely to deliver an equivalent amount of emission reductions

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>corresponding adjustment be made to the emissions and NDC of the other party to ensure double counting is avoided. Various parties have entered into arrangements to support other countries to reduce their emissions to generate ITMOs that can be credited towards their NDCs. These include Japan, Switzerland, Norway, Sweden and South Korea.¹⁰ Examples of these relationships reducing emissions in partner countries, and delivering ITMOs, can be seen with Switzerland’s Klik foundation that has been set up to acquire the offshore mitigation to meet its target.¹¹</p> <p>The New Zealand Government has not announced any formal agreements for the funding and transfer of ITMOs that would support meeting the international component of the first NDC. The New Zealand Government has been establishing relationships and building market capacity with a range of potential partner countries, as detailed in section 2.3.2.4 of the first Biennial Transparency Report. These include contributions to multilateral funds that bring countries with climate finance and countries with mitigation needs together to support mitigation under Article 6.2.ⁱⁱⁱ Participation in the market readiness activities in these funds allows New Zealand to be eligible to purchase ITMOs through the fund at a later stage.</p> <p>These bilateral relationships and/or multilateral funds could be developed into formal agreements for ITMOs to support the first NDC. However, the time remaining to do so while still delivering mitigation within the first NDC period (2021-2030) is short. Such negotiations are commercially sensitive and confidential – the Commission does not have visibility of how these may be progressing.</p> <p>We consider that it is still credible that the Government could deliver offshore mitigation for the first NDC via article 6.2.</p> <p><u>Article 6.4 Paris Agreement Crediting Mechanism (PACM)</u></p> <p>Under Article 6.4 of the Paris Agreement, parties agreed that there would be a central mechanism to support mitigation and sustainable development that would allow mitigation to be traded between parties. Up until recently, the way this central mechanism would be made operational was</p>	<p>towards to the first NDC. It may instead encourage the conversion of production forests to permanent forests.</p> <ul style="list-style-type: none"> • s30GC(5)(f) – any other matter the Commission considers relevant – in particular the viability of options for acquiring the necessary offshore mitigation to meet the first NDC. We consider the Government has options available to acquire the necessary offshore mitigation to meet the first NDC through bilateral relationships with other countries (Article 6.2) and/or the central mechanism for trading mitigation under the Paris Agreement (Article 6.4). While there is limited time remaining, it is still viable for the Government to acquire the necessary offshore mitigation to meet the first NDC. The Government’s statements in its formal submissions (such as the revised first NDC, the first emissions reduction plan, and the First Biennial Transparency Report) continue to assert that the Government intends to meet the first NDC with a combination of domestic emission reductions, domestic removals, and offshore mitigation. <p>We have considered the other matters included in s30GC and consider them to be less relevant:</p>

ⁱⁱⁱ In particular the Global Green Growth Institute’s Carbon Transaction Facility, and the Asian Development Bank’s Article 6 Support Facility.

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
<p>still being negotiated between parties.</p> <p>At COP29 in Baku in November 2024, parties agreed on the necessary guidance to enable the operation of the central mechanism, termed the Paris Agreement Crediting Mechanism (PACM). It is possible that this mechanism will be functioning in time that the Government could use it to help meet the first NDC.¹²</p> <p>The PACM could be a simpler avenue for the Government to acquire ITMOs to meet the offshore component of the NDC. It does not require establishing bilateral relationships with partner countries, will make it easier to connect with developers of mitigation options overseas, and could enable the scaling up of ITMOs more generally.</p> <p><u>Viability and impact of meeting the first NDC without offshore mitigation</u></p> <p>If the first NDC was to be met entirely domestically, net emissions would need to decline 61% from the forecast 2025 level over 2026-2030 (assuming new policies do not start until 2026). This is not feasible. For comparison, if New Zealand fully electrified all road transport, eliminated all industrial energy emissions, and eliminated half of all agricultural emissions, that would reduce emissions by approximately what is needed to meet the first NDC domestically. None of these three emissions reductions are plausible over a timeframe as short as 5 years, and attempting to do so via the NZ ETS would have severe economic and social consequences on people, businesses, communities and iwi/Māori because essential energy services would not be available. This is discussed in more detail the Commission’s 2021 advice Ināia tonu nei at pp363-364, and in the Commission’s first NZ ETS settings advice at pp32-33.</p>	<ul style="list-style-type: none"> • s30GC(5)(a) – projected trends of emissions over the next five years. Projections have been considered, and are how we can identify the gap, and estimate the ability of the NZ ETS to address it. • s30GC(5)(c) – international climate change agreements and offshore mitigation. As discussed, to the Commission’s knowledge the Government has not announced any formal agreements to deliver offshore mitigation. However, we consider it remains viable that it can do so. <p>With respect to the price control settings:</p> <ul style="list-style-type: none"> • s30GC(6)(a) – impacts on households and the economy; and Section30GC(6)(c) – inflation. We have considered the impact of emissions prices on households and the economy, and the impacts on inflation in deciding whether the discrepancy is justified. Under section 30GC(5)(d) above, we advised that attempting to meet the first NDC entirely domestically would have severe impacts on households and the economy, because there is insufficient time to reduce emissions by the necessary degree without significant disruption. This implies that emissions prices consistent with this outcome would also lead to severe impacts, and have high costs. Very high emissions prices would also contribute to inflation. See the Commission’s 2021 advice Ināia tonu nei (at p363-364) for more

Summary analysis of accordance of the recommended settings for 2026-2030 with targets

Conclusion, with justification for any discrepancies

details of these impacts.¹³

- s30GC(6)(b) – level and trajectory of international emissions prices. We have assessed the level and trajectory of international emissions prices, and consider that it remains viable for the Government to meet the offshore mitigation component of the first NDC. Singapore’s recent request for proposals resulted in bids offering ITMOs at prices in a cost range of \$32-\$72/tonne.¹⁴ Switzerland expects that costs for the remaining offshore mitigation for its NDC will cost around \$78/tonne.¹⁵ Given the potential mitigation costs for gross emissions in Aotearoa New Zealand, using offshore mitigation to meet the first NDC will almost certainly be lower cost than attempting to meet all of it domestically.

Second nationally determined contribution (2031–2035)

The Government announced the second NDC on 30 January 2025, of a 51-55% reduction of net emissions below 2005 gross emission levels by 2035.¹⁶ This results in a target range for 2035 of 39-42 Mt CO₂e.¹⁷

The emission trajectory to limit emissions to the second NDC level is very similar to that required to meet the third emissions budget. We consider that if the NZ ETS cap continues to be set with reference to emissions budgets, future settings that apply to the second NDC period (2031-2035) can be aligned to the level of the second NDC with only a minor adjustment.

Therefore, we consider that our assessment of how the unit limit and price control settings accord with the third emissions budget can also be applied to the second NDC. Please see the assessment earlier in this table for more detail.

The settings do not strictly accord, but nevertheless accord with a discrepancy, with the second NDC.

The second NDC is closely aligned with the third emissions budget, so the reasons for the discrepancy from strict accordance are the same as those relating to the third emissions budget. See the explanation provided above in relation to the third emissions budget for further information.

Summary analysis of accordance of the recommended settings for 2026-2030 with targets	Conclusion, with justification for any discrepancies
2050 target	
<p>The recommended unit limits and price control settings are in line with what is needed to meet the first and second emissions budgets. The emissions budgets act as interim targets that step down to the 2050 target level over the coming decades. The emissions budgets that have been set were based on the Commission’s 2021 advice on the pathway to achieving the 2050 target. By according the NZ ETS settings with meeting emissions budgets, we consider that the settings also strictly accord with meeting the 2050 target.</p> <p>Despite the recommended settings according, but not strictly according, with the third emissions budget, we still consider that there is strict accordance with the 2050 target. This is because the emissions projections set out in the second emissions reduction plan meet the 2050 target, despite them not meeting the third emissions budget.</p> <p>In addition, we note that considering effects of the NZ ETS settings on meeting the 2050 target involves looking 25 years into the future, and so involves high levels of uncertainty. There are many factors that will influence emissions over that period that the settings recommended for 2026-2030 cannot influence, due to their limited scope in time and the limited scope of the NZ ETS. There are key uncertainties about the effectiveness of the NZ ETS past the mid-2030s as its emissions cap approaches zero and industrial allocation may start to exceed the cap. There are also uncertainties about the policies applying to emissions outside the NZ ETS and the trajectory for those emissions, which are mostly methane and nitrous oxide from agriculture.</p> <p>The risks that these present to the achievement of the 2050 target are issues that cannot be addressed or corrected for by amending the NZ ETS unit limit and price control settings for the 2026-2030 period. Therefore, we do not consider that these future challenges or policy gaps undermine the recommended settings’ accordance with the 2050 target.</p>	<p>We assess that the recommended settings strictly accord with the 2050 target.</p>

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