



# AGENDA

## Supplementary Reports Extraordinary Council Meeting Tuesday, 2 June 2020

**Date** Tuesday, 2 June 2020

**Time** 2.00pm

**Location** Council Chamber  
District Council Building  
King George Place  
Timaru

**File Reference** 1342397

**Order Of Business**

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## 1 Reports

### 1.1 Carbon Liability

**Author:** Donna Cross, Group Manager Commercial and Strategy

**Authoriser:** Bede Carran, Chief Executive

#### Recommendation

That Council:

1. Approves and adopts the proposed new Carbon Policy attached to this report;
2. Notes the requirement to surrender 36,539 New Zealand Units to meet its carbon liability for the calendar year ending 31 December 2019;
3. Approves the purchase of 36,539 New Zealand Units at a price of up to \$25 per unit (i.e. using the fixed price option), at a total price of up to \$913,475 to be met from Council's waste minimisation reserves;
4. Notes and approves the strategy to achieve policy compliance in 2020, based on the proposed new policy.

#### Purpose of Report

- 1 To:
  - 1.1 Provide confirmation of Council's compliance with the New Zealand Emissions Trading Scheme (NZ ETS);
  - 1.2 Obtain Council's approval to the proposed amendments to the Carbon Policy;
  - 1.3 Obtain Council's approval to the strategy to maintain policy compliance through 2020, based on the proposed new Carbon Policy; and
  - 1.4 Obtain Council's approval of the transactions required for Council to meet its surrender obligations in relation to the year ending 31 December 2019.

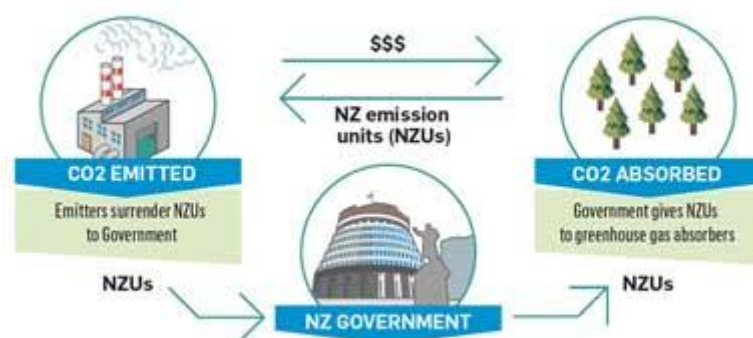
#### Assessment of Significance

- 2 The matter of carbon liability affects all of Council's ratepayers who receive kerbside rubbish collection and all users of its landfill and waste transfer stations. However, it is not considered that the matters contained within this report require consultation.

#### Background

- 3 This report contains:
  - 3.1 Background information about the New Zealand Emissions Trading Scheme (NZ ETS) and Council's participation in it.
  - 3.2 Confirmation of Council's compliance with the NZ ETS.
  - 3.3 Recommended changes to Council's Carbon policy which has been under review.

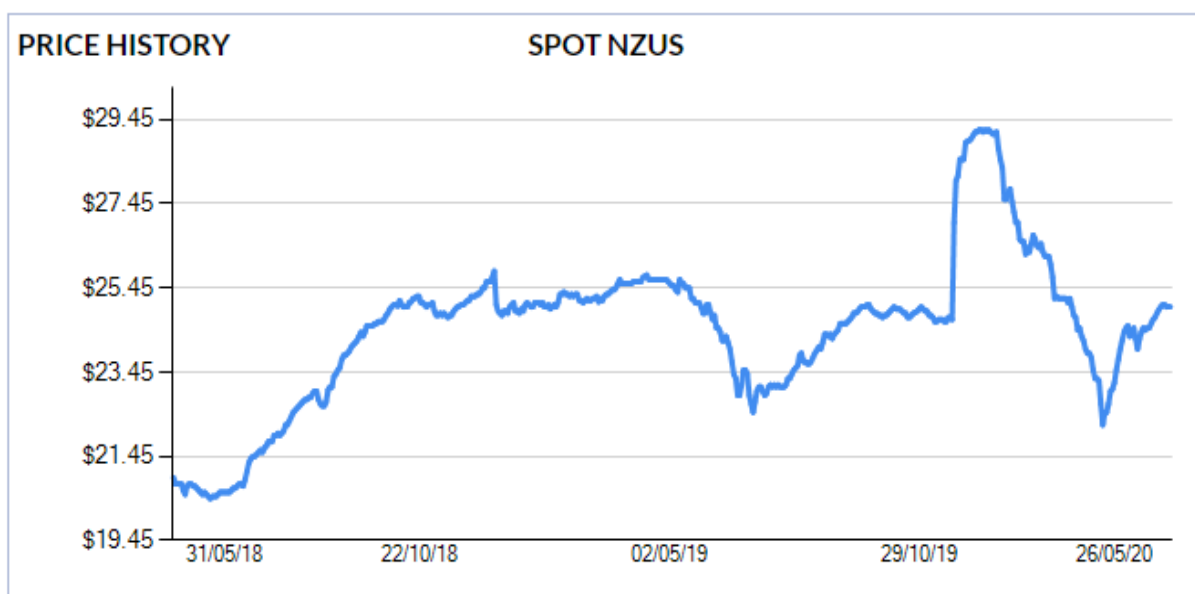
- 3.4 Recommendations in relation to Council's current surrender obligations in relation to the calendar year ending 31 December 2020.
- 4 The New Zealand Emissions Trading Scheme (NZ ETS) is the Government's main tool for meeting domestic and international climate change targets. The scheme aims to encourage people to reduce greenhouse gas emissions.<sup>1</sup>
- 5 The NZ ETS puts a price on greenhouse gas emissions. It creates a financial incentive for:
- 5.1 businesses to reduce their emissions
- 5.2 landowners to earn money by planting forests that absorb carbon dioxide as the trees grow.
- 6 One emission unit, the New Zealand Unit (NZU), represents one metric tonne of carbon dioxide or carbon dioxide equivalent (i.e. the amount of another greenhouse gas, such as methane, that does as much damage as one tonne of carbon dioxide).
- 7 Businesses with surrender obligations (legal obligations to hand over units) must purchase enough units to cover their emissions. These units are then surrendered to the Government.
- For example, a business emitting 2,000 tonnes of greenhouse gases would need to purchase 2,000 emission units on the NZ ETS market. If the emitter reduced their emissions by 500 tonnes of greenhouse gases they would only need to purchase and surrender 1,500 units.
- 8 It is up to the emitter to decide whether they wish to reduce their emissions or purchase units. The price which the emitter pays for units, sometimes called the carbon price, is set by supply and demand. Where demand for units increases and supply remains constant, the price of units will generally increase. The price will decrease where there is an abundant supply of units.
- 9 In terms of forestry, NZ ETS participation is mandatory for some types of forest land and voluntary for others. The Government gives eligible foresters units for carbon dioxide that is absorbed by their trees. The foresters can sell these units on the NZ ETS market.
- 10 The following illustrates how NZU trading can take place:



<sup>1</sup> Paragraphs 4 – 10 of this report contains information created and published by the Ministry for the Environment.

- 11 Sectors that Timaru District Council participates in, specifically waste and forestry, have surrender and reporting obligations under the NZ ETS. Council has obligations under NZ ETS in relation to its landfill activities, as well as its management of certain forestry land.
- 12 Each year, Council incurs a liability in relation to greenhouse gas emissions from its landfill activities. This has historically represented a cost of between approximately \$600,000 and \$700,000 each year (for the 2019 year this will be over \$900,000 due to increased volumes), with that cost projected to increase significantly in the future.
- 13 Council would also incur a liability if deforestation was to occur in relation to any Council forest that is subject to the ETS.
- 14 Council files an emissions return each year and is required to surrender NZUs to meet its carbon liability. It needs to have purchased or otherwise accumulated sufficient NZUs to meet its surrender obligations.
- 15 The cost of Council's landfill activities, including carbon liability, are met through rates and user charges. Kerbside collection (and associated carbon liability) is funded through rates, whereas for users disposing of waste direct to landfill or via transfer stations (and associated carbon liability) are met through user fees and charges.
- 16 As rates are set annually in advance, and fees and charges are reviewed annually (although with some scope to amend fees and charges during the year if necessary), we are susceptible to market volatility in terms of the cost of meeting our emissions liability – if the cost of purchasing NZUs escalates, what we collect in rates and user fees may not be sufficient to meet the cost of our liability.
- 17 The graph below gives an indication of the price history for the New Zealand spot market:

© OMF 2019



- 18 Government has proposed to reform the NZ ETS to drive emissions reductions. These reforms aim to incentivise practice change and New Zealand's transformation to a low carbon economy.
- 19 In terms of the current market and where it is potentially heading because of the reforms currently proposed, there is a wide range of possible outcomes under the NZ ETS for where the price of carbon will be in the future:

- 19.1 The current spot price for an NZU is approximately \$25.05.
  - 19.2 The current Fixed Price Option (FPO) is \$25 per NZU which is expected to be only available to use to meet surrender obligations for emissions produced in 2019. This is proposed to increase to \$35 per NZU for emissions produced in 2020 then to cease and be replaced with a cost containment mechanism (where a trigger point of \$50 is reached, Government will place more units into the market as a way of easing the pressure between supply and demand).
  - 19.3 The current 5 year forward price is approximately \$29.30 per NZU.
  - 19.4 Market and proposed regulatory changes are expected to significantly increase the cost of purchasing NZUs to meet liability associated with greenhouse gas emissions. The Government low estimate is \$50 per NZU and the Productivity Commission estimates this could increase to as much as \$200 per NZU in future years. Such a price increase would have significant implications for Council and impact on the cost of providing landfill services.
- 20 Given the above factors, with assistance and advice from our external advisors, we have undertaken a comprehensive desktop review of our Carbon Policy.
  - 21 It's to be noted that Council is constantly exploring ways to minimise emissions and emission liability associated with its landfill. It does this through its strategy around waste minimisation and diverting waste from landfill. This includes looking at technologies and practices such as landfill gas flaring to reduce methane emissions (gas flaring can also be used for power generation). Council's future investment strategy in relation to forestry, to offset its carbon liability, also needs to be considered.

## Discussion

### *Current compliance*

- 22 The NZ ETS works on a calendar year basis. Council has met its reporting requirements to NZ ETS in relation to emissions for the 2019 calendar year.
- 23 Council is required to surrender 36,539 NZUs by 31 May 2020 (with 31 May falling on a weekend and with 1 June being a public holiday, Council is able to surrender on but no later than 2 June 2020).
- 24 Council currently holds 61,622 NZUs, of which 16,081 are forestry units. Current holdings are consistent with Council's traditional approach under the Carbon Policy, which is a 50% hedge for the relevant emissions year and 30% hedge for the next 4 years which has then been offset by forestry units held.
- 25 The Carbon Policy can be interpreted in different ways which affect its application. We have sought to address through the policy review.
- 26 Note that Council has the option of meeting its surrender obligation for 2019 through utilising the Crown's Fixed Price Option (FPO) of \$25 per NZU. This is only able to be used to meet its surrender obligations in relation to its 2019 emissions. At \$25 per NZU this would cost \$913,475 which will be met from waste minimisation reserves. Council's waste minimisation reserves have a current balance of circa \$1.9m. Further details on this are included below.
- 27 Please note that Council is not able to buy NZUs at the FPO for the purpose of meeting its surrender obligations in relation to its 2020 or future emissions – the reforms propose a FPO

of \$35 per NZU for 2020 emissions however the possibility of extending the current FPO of \$25 per NZU for 1 year is currently under consideration.

### *Policy review*

- 28 A review of the existing Carbon Policy has been undertaken to:
- 28.1 Confirm that the Policy is fit for the purpose of meeting Council's obligations under the New Zealand Emissions Trading Scheme (NZ ETS);
  - 28.2 Ensure that the Policy is effective and efficient in identifying and recognising risks, measuring and managing risk exposures, considering approved instruments and supports decisions to re-profile risk positions. The Policy review has been mindful of the present uncertainty relating to the NZ ETS;
  - 28.3 Evaluate the Policy against local government sector peers; and
  - 28.4 Recommend an appropriate carbon price risk and counterparty credit policy based on the unique requirements of the NZ ETS to ensure policy objectives are met and transactions are not unduly restrictive.
- 29 Council's existing policy is very comprehensive and in a better state of maturity than many. It covers most of the areas that a risk management framework would be expected to include. However, there are some conflicting and ambiguous provisions within the policy that affect its application, and some other material changes that are recommended moving forward.
- 30 Carbon exposures are becoming increasingly significant to the local government sector given the impending legislative changes that will require New Zealand to meet its obligations under the Paris Agreement (which comes into effect in 2020). The expectation that carbon prices will rise over the coming years (as NZU demand exceeds NZU supply) will likely increase this materially. A number of councils which do own or control landfills are becoming attuned to these risks and are beginning to review their exposures and risk management frameworks.
- 31 The following recommended changes have been incorporated in the proposed new policy:
- 31.1 Reducing the risk management horizon from 10 years to five years. This change is predominantly driven by the underlying market itself - as hedging beyond five years is largely impractical;
  - 31.2 A focus on layering up carbon holdings to ensure a high degree of cost certainty for Council relative to its financial year. There are challenges with managing budgets on a financial year and aligning this with the calendar year used by the NZ ETS; and
  - 31.3 Providing a policy framework that is dynamic, and will be able to move with Council from one year to the next (rather than referencing specific hedging percentages for specific years).
- 32 Other changes include:
- 32.1 Identification of risk (section 4.1):**
- We have included a brief comment on the materiality of carbon exposures to Council and the risk if these are not managed.
  - We have removed reference to the estimated number of units within the policy. We recommend not stating what the forecasted obligation will be, but rather point to a forecast that can be adjusted outside of the policy review cycle.

- We have removed the reference to using forestry units as available to offset landfill obligations. Without a strategy to grow units allocated to forestry units this allocation of units should be kept whole to meet any obligation that may arise from deforestation. While some larger councils, or those that have a larger portfolio of forestry units have been investigating how these can be used strategically to manage carbon price risk, Council at this point in time does not have a portfolio of forestry units that could realistically be used as a strategic reserve. Therefore, the proposed policy now clearly states that these two are separate and there is no co-mingling or netting between the two sources as a prudent management approach.

### 32.2 Management structure and responsibilities (section 4.2):

- The proposed policy provides that the CFO reviews the emissions return before it is filed. There are to be onerous penalties applied under the updated legislation (from May 2020) and a review process for the emissions return has been included to ensure Council is not penalised under the NZ ETS for incorrect surrenders.
- We have included a requirement for a report on non-compliance to be initiated (similar to that typically seen in treasury policies) to ensure that any non-compliance is escalated and an action for mitigation is put in place (where appropriate).
- We have included some changes to the management responsibilities to better reflect where these tasks more appropriately sit in practice. We would transition to this over the next 2 months so that current practices can be maintained for the purpose of administering the surrender obligations for the 2019 emissions, and any transactions required to maintain policy compliance through to 30 June 2020.

### 32.3 Carbon risk management parameters (section 4.3):

#### *Risk management framework for unit holdings:*

- We have included a two stage approach to the framework for managing carbon price risk.
- The following two tables outline the approach recommended in the policy and the rationale for these changes, which are discussed below:

Obligation period	Compliance requirements as at (month of current year)	Minimum holding as a percentage of annual gross obligations
Current calendar year	by 30 June	75%
	by 31 December	100%
Next calendar year	by 31 December	50%

- The second stage of the framework is to set a minimum and maximum level of units to be purchased and held by Council to cover future years as shown below:

Period	Minimum unit holding	Maximum unit holding
Year 3 - Year 5	0%	50%



- Taken together, the policy aims to strike a balance between the following:
  - Timing of the obligation vs the timing of setting budgets for price allocation (landfill).
  - Price stability for the current budgetary period while retaining the ability to make strategic hedging decisions for the medium term (managing the carbon price risk).
  - Allow for some uncertainty in emissions forecasting (which will drive the financial obligation. This obligation needs to be collected by landfill and passed through to treasury/finance to settle with the crown. This will be done using NZU's (or equivalents) or by using the Fixed Price Option (FPO) while it is still available.

*Use of the fixed price option (FPO), or other alternative mechanisms:*

- We have maintained the ability for Council to use to the FPO. The FPO is an existing mechanism that can be used to settle Council's obligations at a fixed (known) price on the day of settlement (i.e. 31 May each year). The FPO provides an observable price that Council can utilise to give certainty and the market is currently trading around the level at which it is set (i.e. \$25.00). The FPO will ultimately be retired (and replaced with a different mechanism called the cost containment reserve – explained at paragraph 19.2 above), however we consider it beneficial for Council to include the option within the policy while it is available.

*Commentary*

- The recommended policy aims to provide a framework which balances strong carbon price certainty with the flexibility to make a small number of strategic decisions.
- To this end, it is recommended that Council builds up 50% of hedging in the preceding calendar year, with a requirement to be 75% hedged (the minimum) by the time the budget is finalised (in June). Council then has the remainder of the year to finalise the hedging for the calendar year (i.e. 100% by December of current obligation year). There is no maximum under this policy, given that 'overhedging' will only create an excess of credits that can be carried forward or allocated against future years' exposures.
- As well as managing the current and next calendar year's obligations, we also recommend including the ability to hedge longer-term risks out as far as five years. Relative to the existing policy, this framework is a shorter, simplified approach for managing carbon exposures beyond the next two calendar years. This is to ensure that Council is able to obtain units but is not forced to do so over that time.
- Overall, the policy ensures a prudent 'spreading and smoothing' approach to building up cover and forward managing pricing risk before the budget is set for the following financial year.
- This is in line with Council's current approach to managing the risks associated with the carbon exposure with some adjustments discussed below:

- Reducing the time horizon from 10 years to five years. This is due to the following reasons:
  - The five year horizon aligns with the Government's future requirement to set their unit supply volumes over a five year rolling period;
  - Managing the risk beyond that time horizon will likely prove to be difficult; and
  - Forward contracts are not offered beyond five years and contracts out that far would present a high level of counterparty credit exposure.
- This approach is similar to frameworks used to manage other treasury risks, such as commodities, currency or interest rate risk and provides flexible mechanisms to allow risk management without enforcing long dated hedging.
- We have incorporated the use of 'alternative mechanisms for settling obligations' in order to allow the use of the FPO and to allow flexibility for future changes that may be made to the NZ ETS rather than restricting Council to current mechanisms.

#### **32.4 Authorised instruments and counterparties (section 4.4):**

- We have removed the reference to green Certified Emissions Reduction units (gCERs) and replaced the use of ERUs with a generic international unit under the assumption that (based on the Government's forecasting models) there will be an allowance made for the use of approved international units within the scheme in the future. We have worded this to ensure that the use of units must be aligned with what is allowed by the Crown under the NZ ETS.
- For counterparties - we have added wording to the existing policy to include the use of registered exchange platforms (for spot exchanges only) and also to include the New Zealand Government/Crown. Direct contracts with other parties could be potentially used provided risk can be effectively managed such as through escrow arrangements.

#### **32.5 Reporting (section 4.6):**

- We have included an enhanced requirement for a reconciliation to ensure this agrees with external holdings records.
- Separately, we have included the use of an exceptions report (discussed earlier in the responsibilities section).

33 Overall, the recommended framework contained in the proposed new policy will provide a number of benefits over the existing policy:

33.1 It is more closely aligned to the latest NZ ETS changes and likely market characteristics from 2021 and beyond.

33.2 The near term has a higher level of fixing required to ensure that certainty is achieved over the shorter term while providing flexibility in managing the carbon risk in later years.

33.3 The policy aims to balance net exposures for Council against the gross exposure, allowing some flexibility for risk mitigation between the two.

33.4 This framework is more dynamic over time and allows Council to be proactive where there are market opportunities and allows the use of alternative mechanisms.

34 Note however, in terms of the minimum requirement, it may result in us holding less NZUs at any one time than is required by the current Carbon Policy.

*Ensuring policy compliance requirement, and strategy*

35 Based on an annual forecast surrender obligation of 35,000 (up from 33,200), here is how the proposed new policy would be applied if it was operational in 2020:

Obligation period	Compliance requirements as at	Minimum holding as a percentage of annual gross obligations	Units requirement (assuming no utilisation of forestry units to offset)
Current calendar year	by 30 June 2020	75%	Total 26,250 NZUs required to be held for landfill*
	by 31 December 2020	100%	Total 35,000 NZUs required to be held for landfill
Next calendar year	by 31 December 2020	50%	Total 52,500 NZUs required to be held for landfill
	<b>Total required by 31 December 2020</b>	100% of current year + 50% for next year	<b>52,500 NZUs*</b>

\*c.f. 59,500 NZUs if the current policy is applied (but on the basis that Council's forestry units are not used to offset).

36 *Longer term policy component:* In addition to the above activity, which would be required to meet compliance with the proposed new policy, Council would also be able to transact up to 50% of its forecast exposure, for the following three years as shown below.

Period	Minimum unit Holding	Maximum unit Holding
Year 3 - Year 5	0%	50%
Based on current forecast exposures	35,000 x 0% x 3 years = <b>0 NZUs</b>	35,000 x 50% x 3 years = <b>52,500 NZUs</b> (additional to the <b>52,500 NZUs above for</b>

		<b>Year 1 - 2)</b>
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- 37 Actively hedging longer-term exposures is not necessarily required at this time. However, if Council had a view that NZU prices were moving materially higher and there was a desire to forward manage this risk, the recommended policy framework allows this. Note that Government is expected to provide an update on the reforms after 31 May and this could result in a market response as we saw in late 2019 when the price increased quickly from \$24 to over \$28.
- 38 Assuming Council approves and adopts the proposed new policy, the strategy described at paragraph 39 is proposed, based on the following information regarding current holdings of units and utilising the new recommended framework:
- 38.1 Current holdings: 61,622 NZUs
  - 38.2 Current holdings for landfill use: 45,541
  - 38.3 Current holdings for forestry: 16,081
  - 38.4 Surrender obligation as at 31 May 2020: 36,539 NZUs
  - 38.5 Annual forecast exposure of 35,000 NZUs (up from 33,320)
  - 38.6 For the landfill, the holding requirement as at 30 June to achieve minimum policy compliance (based on the proposed new Carbon Policy) is 26,250 NZUs, and as at 31 December 2020 this is 52,500 NZUs.
- 39 Strategy: *Surrender obligation for the calendar year ending 31 December 2019*
- While on an individual transaction basis it would be cheaper to do so, rather than utilising NZUs currently held to meet Council's surrender obligations as at 31 May 2020, or current spot price which is slightly over \$25, we propose to utilise the \$25 fixed price option, which is available to Council to settle its 2019 emissions obligations (we've been advised this can be settled on 2 June).
- This would leave Council in the position of meeting and in fact being favourable to our minimum policy requirement at 30 June 2020 (assuming adoption of the proposed new policy) and we can then look to build up forward cover in the secondary market (for next year's surrender by 31 December 2020, or sooner, particularly if we can achieve pricing around the \$25 level).
- It is possible that the spot price could drop following 31 May 2020 as the current demand for NZUs to meet 31 May surrender obligations will be impacting the market to some degree, but there is certainly no guarantee of this.

### **Options and Preferred Option**

- 40 *Proposed new policy:* The preferred option is for Council to adopt the proposed new Carbon Policy. This does materially change our policy approach. While the current policy has been advanced in terms of carbon policy maturity generally within the sector, it requires amending to enable us to better integrate our budgeting process with liability management.
- 41 *Approach to meeting surrender obligation of NZUs in relation to 2019 emissions year:* The preferred option put forward is to utilise waste minimisation reserves to enable Council to meet its 2019 emissions year surrender obligations utilising the fixed price option of \$25 per

NZU. This would leave Council in a positive position in terms of policy compliance heading towards 30 June.

The alternative would be for Council to use all or part of its current landfill NZUs (perhaps combining this with some use of the fixed price option) but then have to purchase additional NZUs following the surrender to achieve policy compliance by 30 June 2020. While we could achieve compliance, there is an element of speculation in this approach.

### Consultation

- 42 We have received external advice on the policy review, but have otherwise not consulted externally.

### Relevant Legislation, Council Policy and Plans

- 43 The legislation and policies relevant to this report include:
- 43.1 Timaru District Council Carbon Policy
  - 43.2 New Zealand Emissions Trading Scheme (currently under review)
  - 43.3 Climate Change Response Act 2002 (currently under review)
  - 43.4 Climate Change Response (Emissions Trading Reform) Amendment Bill
  - 43.5 Climate Change Response (Zero Carbon) Amendment Bill
- 44 Paris Agreement
- 45 Kyoto Protocol (expired)

### Financial and Funding Implications

- 46 The cost of surrendering 36,539 NZUs using the fixed price option for Council to meet its obligations in relation to the 2019 emissions year, will be \$913,475. This would be met from Council's waste minimisation reserves (which has a current balance of approximately \$1.9m, with the projected actual at year end being \$2.4m) as the budget for the year has been applied to maintain compliance with the current Carbon Policy.

### Other Considerations

- 47 n/a

### Attachments

1. **Carbon Policy - Proposed Amendments - May 2020 (draft, tracked)**  

**Carbon policy**



<b>Approved by:</b>	Council
<b>Date Approved:</b>	2 June 2020 (Also ratified by the Commercial & Strategy Committee on 9 June 2020)
<b>Keywords:</b>	Carbon, Emissions Trading Scheme

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**1.0 Purpose**

The Carbon policy outlines the management of carbon risk and management of obligations under the New Zealand Emissions Trading Scheme (NZ ETS).

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**2.0 Background**

The purpose of this document is to establish a framework and policy guidelines within which Timaru District Council ("TDC") will manage its obligation to report greenhouse gas emissions and surrender New Zealand Units ("NZUs") under the NZ ETS.

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- To ensure the obligations to surrender NZUs from the Redruth Landfill are managed in line with the requirements of the NZ ETS.
- To ensure the receipt of NZUs from the pre-1990 Forestry assets of TDC are managed in line with the requirements of the NZ ETS and for the benefit of TDC.
- To ensure that TDC's NZUs carbon surrender risk management process reflects the annual obligation to surrender NZUs as calculated by TDC's Waste Minimisation Manager ("WMM").
- To ensure a conservative approach is adopted to fulfil TDC's greenhouse gas obligations by a considered risk management approach that is not in any way speculative.
- To ensure TDC adopts a risk-averse approach to greenhouse gas risk management and that all activities relate to highly probable surrender obligations as agreed by TDC's senior management.

**2.1 Legislation / Framework**

Outline relevant legislation and agreements applicable to this policy document

- New Zealand Emissions Trading Scheme (currently under review)
- Climate Change Response Act 2002 (CCR Act) (currently under review)
- Climate Change Response (Emissions Trading Reform) Amendment Bill
- Climate Change Response (Zero Carbon) Amendment Bill
- Paris Agreement
- Kyoto Protocol (expired)

Note, several items remain outstanding on the NZ ETS agenda. This policy will need to be updated when these changes are finalised, the framework is in place and is operational.

#

### 3.0 Key Definitions

NZU – New Zealand Unit that can be traded.

ERU – Emission Reduction Unit.

ETR – Emission Trading Register which records all transactions of carbon credits.

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### 4.0 Policy

#### 4.1 Identification of Risk

Council has assessed that volatility in carbon prices present a material risk to Council, landfill users, and potentially rate payers. Significant movements in the price of carbon units that cannot be effectively met by landfill users will need to be absorbed or passed on to TDC's rate payer base. Accordingly, TDC actively manages the carbon price risk within the following framework to provide cost certainty and reduce the risk that volatility in carbon prices is passed on to rate payers.

TDC is a registered Participant on the New Zealand's Emission Trading Register ("ETR"). The registration is under Schedule 3, Sector Waste, Activity Part 6, Operating a disposal facility, and therefore it must submit an online Carbon Emissions return annually between January and March (this must be submitted by 31 March each year for the previous calendar period). Obligations must be settled with the Crown on or before 31 May following the end of each calendar year.

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TDC's account number is NZ5656 and the account type is a Holding Account.

Senior management of TDC, specifically the WMM, have the responsibility of calculating the annual greenhouse gas emissions from the Redruth Landfill, based on the default emissions factor calculation. It is the responsibility of the WMM to ensure measurement procedures are up to date and measurement frequency is sufficient to provide TDC with accurate actual and forecast exposures for risk management purposes. To provide some context, historical exposures have been estimated at 19,000 tonnes per annum.

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TDC has received NZUs from its pre-1990 forestry assets into its Holding Account at the ETR. TDC's policy is for these NZUs to be held in the Holding Account to offset any obligation that may arise from deforestation, for whatever reason. TDC's landfill carbon exposures are managed on a gross basis. There is no co-mingling or netting of forestry units for the purposes of measuring or relinquishing its annual carbon exposures.

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#### 4.2 Management Structure and Responsibilities

*[The management structure and responsibilities, provisions relating to the operation of the holding account and provisions relating to the authorising of transactions, as contained in the previous policy, may be utilised by the management team on a transitional basis in order to settle Council's surrender obligations as at 31 May 2020 in relation to the 2019 emissions year, and to achieve policy compliance where within budget or otherwise approved by Council prior to 30 June 2020]*

Council

- Approve the Carbon Policy.
- Receive reports on compliance with the requirements of the NZ ETS twice a year.

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#

**Management Team** (CEO, GM Commercial and Strategy, CFO, GM Infrastructure, GM Community Services)

- Approve strategies for carbon emissions surrender obligations risk management as proposed by GM Commercial and Strategy.
- Review quarterly reports on carbon activities from CFO.

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**Chief Executive (CE)**

- Authorised to approve purchase of NZ ETS approved carbon credits, within financial or other delegations;
- Authorised to execute carbon emissions unit transactions with authorised counterparties, within financial or other delegations.
- The CE is TDC's the secondary representative on the ETR, and is authorised to operate the Holding Account on the ETR as an approver.

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**Group Manager Commercial and Strategy**

- The GM Commercial and Strategy is TDC's primary representative on the ETR. As primary representative the GM Commercial and Strategy is authorised to operate the Holding Account on the ETR as an approver.
- Propose any amendments to the Carbon Policy for approval by Council.
- Provide oversight and monitoring of CFO in relation to CFO's duties below.
- Authorised to execute carbon emissions unit transactions with authorised counterparties, within financial delegations.

**Chief Financial Officer (CFO)**

- Registered on Council's Holding Account of the ETR, as a preparer.
- Propose short, medium and long term strategies for carbon emissions surrender obligations risk management to the Management Team.
- Review the emissions return prepared by the WMM for submission each year by 31 March. Certify as correct with GM Commercial & Strategy.
- Ensure that the correct number of NZUs are surrendered by 31 May each year based on the emissions return filed by 31 March each year. Certify as correct with GM Commercial & Strategy.
- Prepare a semi-annual Carbon Compliance Report for Council.
- Prepare a quarterly report on carbon activities for the Management Team.
- Prepare an annual review for the Management Team on TDC's carbon risk management performance post 31 May.
- Report any non-compliance in relation to either the Carbon Policy or to the NZ ETS and the implications of this non-compliance.
- Oversees an audit of the level of NZUs held in the Holding Account at the ETR at the end of each financial year (post May relinquishment). This role may be delegated, but not to the GM Commercial and Strategy, who is the primary operator of the Holding Account.
- Authorised to execute carbon emissions unit transactions with authorised counterparties, within financial delegations.

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Deleted: authorised counterparties.

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Deleted: -#->Audit the level of NZUs held in the Holding Account at the EUR at the end of each financial quarter.¶

**Financial Accountant**

- Supporting the CFO in carrying out the CFO duties above.
- Registered on Council's Holding Account of the ETR as a preparer.

Deleted: -#->Council's Primary Representative on the Emissions Unit Register.¶  
-#->Authorised to operate Council's Holding Account of the Emissions Unit Register, subject to prior approval from the GMCS or CE.¶

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**Waste Minimisation Manager (WMM)**

- WMM is responsible for monitoring forecast levels of emissions over a 10 year horizon [in relation to Council's landfill activities](#).
- WMM is to advise the [GM Commercial and Strategy and CFO](#) should forecast emission levels increase or decline over a forecast 10 year horizon.
- [Prepare and File Annual Emissions Return with the Environmental Protection Authority \(via the New Zealand Emissions Trading Register by 31 March each year. Seek review by CFO prior to filing.](#)

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Deleted: <#>File greenhouse gas emissions report by 31 March each year.†

**4.3 Carbon Risk Management Parameters**

TDC's policy is that the pre-1990 forestry asset NZUs will be held in the Holding Account. Therefore, the following risk management parameters only apply to the surrender obligations due to the greenhouse gas emissions from the Redruth Landfill. [These calculations are made on a gross basis only.](#)

Purchasing NZUs ahead of an obligation surrender date for each year can be achieved by either buying NZUs at spot and then placing in TDC's Holding Account or transacting NZUs for forward delivery into TDC's Holding Account in the future. Forward delivery NZU pricing is a function of the cost of carry (financing cost) over a spot price for delivery (spot delivery is within 3 days). TDC's policy is to transact NZUs in the most financially efficient method based on comparing its cost of funds to the forward price quoted by an authorised counterparty.

[Where there is a compelling case to do so, a price fixing mechanism \(for example the Fixed Price Option\) may also be utilised and the units currently held for surrender for that year may be carried over to future period.](#)

The following table details the percentage of NZU's to be held against forecast surrender obligations over [the current budget period \(each 12 month period commencing 1 January and ending on 31 December\)](#):

Obligation <a href="#">Period</a>	Compliance requirements as at (month of current calendar year)	Minimum <a href="#">hedging as a percentage of annual gross obligations</a>
<a href="#">Current calendar year</a>	<a href="#">30 June</a>	75%
	31 <a href="#">December</a>	100%
<a href="#">Next calendar year</a>	31 <a href="#">December</a>	50%

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[Beyond the current and next calendar years, TDC's NZU holdings are also managed as follows:](#)

<a href="#">Calendar years</a>	<a href="#">Minimum NZU Holding</a>	<a href="#">Maximum NZU Holding</a>
<a href="#">Years 3 to 5</a>	0%	50%

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NZU purchases for Council's projected liability beyond 5 years must be approved by Council before being transacted.

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TDC's CE, GM Commercial and Strategy and CFO each have the authority to approve purchasing NZUs to comply with the policy parameters detailed above, where within their respective financial delegations. The GM Commercial and Strategy is authorised to seek independent NZU risk management advice.

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In developing strategies to manage obligations under the NZ ETS the GM Commercial and Strategy is expected to take into account the following:

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- Council approved types of unit.
- On-going amendments to the NZ ETS and the potential for regulatory change.
- To ensure that compliance at the obligation surrender date is achieved.
- The prevailing spot NZU price and cost of funding purchases.
- The availability of an alternative mechanism for settling obligations with the Crown which will enable price certainty (for example the availability of a fixed price option or cost containment reserve price).

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**4.4 Authorised Instruments and Counterparties**

Key objectives of TDC's Carbon Policy are to be conservative and risk averse, therefore, TDC's policy adopts a conservative approach to the type of carbon unit it is authorised to transact to achieve its surrender obligations. Given the uncertainty as to how the NZ ETS will develop in regard to the type of carbon unit(s) that will be allowed to be surrendered, Council officers are only authorised to transact units allowable under the NZ ETS.

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The Chief Executive can authorise purchase of approved International units where these units are specifically allowed by the Crown to be surrendered under the NZ ETS. These units are not to be held for a period beyond 2 years. If purchased, these units are to be transacted and reported on consistent with the NZU's listed in this policy.

Deleted: The GMCS will review pricing differentials on an annual basis to establish the discount/premium that exists between Green Certified Emission Reduction Units ("gCERs"/Emission Reduction Units ("ERUs") and NZUs to check whether a recommendation to amend the authorised carbon instruments to include non NZUs is justified.

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TDC will assess the most efficient method to purchase NZUs as counterparties are able to provide long term pricing of NZUs, or TDC could purchase on the spot market and finance the holding cost over a long-term period. A key decision as to the preferred option would be the respective 'funding cost' of TDC compared to the yield curve utilised by the authorised counterparty to calculate the forward price of NZUs:

- ⇒ TDC can transact spot NZUs.
- ⇒ TDC can transact forward contracts on NZUs.
- ⇒ TDC may utilise other mechanisms to settle obligations that are permitted under the NZ ETS (e.g. the Fixed price option or once the auction system becomes available).

TDC's exposure to counterparty credit risk will be managed by entering into NZU transactions, spot or forward, with only approved counterparties. Approved counterparties are defined as follows:

- An approved counterparty must be a New Zealand Registered Bank with a long term credit rating of A+ or above by Standard & Poor's ("S&P"), or the Moody's Investor Services or Fitch Ratings equivalents.
- For spot transactions (that will not cause counterparty credit risk) TDC may make use of the services of a registered exchange platform to obtain NZU's on the open market.

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- [New Zealand Government](#)

**4.5 Operations and Procedures**

Arranging and agreeing transactions with external counterparties are required to occur in a framework of control and accuracy. It is vital to the internal control of TDC that all NZU transactions are captured, recorded, reconciled and reported in a timely fashion within a process that has the necessary checks and balances, so that unintentional errors and/or fraud are identified early and clearly.

*Transaction Origination NZUs*

The following authorities shall apply in respect of the execution of NZU transactions with bank dealers at authorised counterparties on behalf of TDC that can commit TDC to all the related contractual obligations under these transactions.

- Transacting NZUs spot or forward, with an approved bank counterparty entails the [CE, GM Commercial and Strategy](#) or [CFO](#), where authorised to undertake these activities, verbally or by email agreeing with the bank or other approved dealer the number, value date and price accepted.
- Once the deal is agreed details of the transaction shall be entered on the relevant internal system.
- Once the bank or other approved dealer confirmation of the transaction is received the details should then be checked to ensure that the bank confirmation is in accordance with the details on the internal system.

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Any discrepancies in the above procedures should be immediately communicated to the bank or other approved dealer so that the correct details of the deal can be agreed on. Where the [GM Commercial and Strategy](#), [CE](#) or [CFO](#) has transacted the deal in the first place the deal shall be ratified and signed off by a [separate](#) bank signatory for Council. In this way there is a clear division of responsibility and a self-checking system.

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[Direct contracts with other holders of NZUs may be considered, and will be permitted, but only where the credit risk is able to be reduced to negligible levels, such as through escrow arrangements.](#)

*Settlement Procedures*

All NZU transactions are to be confirmed and reconciled to external confirmations before settlement.

All NZUs must be delivered into TDC's account ([number NZ5656](#)) held on the [ETR](#).

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**4.6 Reporting**

The following reports will be prepared by the [CFO and authorised by the GM Commercial and Strategy](#) and will include the following:

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*Semi Annual Council Report*

- Forecast greenhouse gas emissions for next 10 years and percentage of NZUs held against forecast obligation.
- Commentary on strategy to achieve compliance with [NZETS](#).

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*Quarterly Management Team*

- Current level of NZUs held on the [ETR](#) against forecast surrender obligations for the next 10 years, to include forward carbon purchases.

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- Quarterly reconciliation [between](#) the Holding Account (ETR) and internal records detailing NZU's held and contract for receipt under forward agreements (reconciling items) and how these will meet surrender obligations set out within this [policy](#).
- Quarterly transaction report.
- Statement of carbon policy compliance, to include any [breaches](#) of policy.
- Weighted average cost of carbon credits to be utilised for landfill pricing.
- Commentary on the outlook for [carbon](#) prices and potential regulatory amendments to [NZ ETS](#).

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5.0 Delegations, References and Revision History					
5.1 Delegations - Identify here any delegations related to the policy for it to be operative or required as a result of the policy					
5.2 Related Documents - Include here reference to any documents related to the policy (e.g. operating guidelines, procedures)					
5.3 Revision History – Summary of the development and review of the policy					
5.1 Delegations					
Delegation				Delegations Reference	Register
Approve purchase of international carbon credits – Chief Executive Operate the Emission Unit Register – Chief Financial Officer (with prior approval of Group Manager Commercial and Strategy or Chief Executive) Execute carbon emission transactions with authorised counterparties – Group Manager Commercial and Strategy				9.6 - Carbon Emission Unit	
5.2 References					
Title				Document Reference	
5.3 Revision History					
Revision #	Policy Owner	Date Approved	Approval by	Date of next review	Document Reference
1	Group Manager Commercial and Strategy	14/10/14	Policy and Development Committee	October 2017	#901671, F335 #902165, F545
1.1 (minor amendments)	Group Manager Commercial and Strategy	11/06/19	Policy and Development Committee	TBC	#1250405, F545
<u>1.2</u>	<u>Group Manager Commercial and Strategy</u>		<u>Council</u>	<u>June 2023</u>	

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