Investor Group on Climate Change

Investor Group On Climate Change (IGCC)

Submission to:

OUR CLIMATE YOUR SAY:

CONSULTATION ON THE ZERO CARBON BILL

19 July 2018

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CONTACT
Michael Mazengarb
michael.mazengarb@igcc.org.au
www.igcc.org.au

EXECUTIVE SUMMARY

The Investor Group on Climate Change (IGCC) supports robust, investment-grade policies to reduce emissions. Investors are looking for policy which delivers clear and transparent market signals which support investment confidence and improved risk management, and which brings private sector investment to market.

The IGCC has developed seven climate change priorities for investors, that can be used to inform an approach that builds upon international commitments under the Paris Agreement.

1. **The setting of long-term emission reduction targets**

   Long term targets which align to the goals supported under the Paris Agreement to limit global warming to well below 2°C and move to a net zero emissions economy.

2. **A durable policy framework grounded in broad political support**

   An integrated policy framework where the key elements are grounded in broad-based bipartisan support and able to deliver a level of investment stability.

3. **A market-based carbon pricing mechanism**

   A market-based carbon price which can be incorporated into investment decisions and is responsive to dynamic market conditions.

4. **An integrated approach to energy sector transition**

   A policy approach which manages carbon, changes in technology and energy markets in an integrated manner to deliver investor certainty and provide opportunities for just transition for workers in the sector.

5. **Support for clean energy public financing vehicles**

   A robust approach to the provision of public financing of emerging clean energy technologies provides long-term certainty necessary to unlock private sector investment.

6. **National adaption and resilience plans to manage the impacts of climate change**

   Adaptation and resilience planning, underpinned by scientific research, which delivers a roadmap for managing the costs and impacts of climate change for investors and the community.

7. **Establishment of disclosure frameworks for climate-related financial reporting**

   Financial disclosure frameworks which acknowledges the financial and economic implications of climate change and promote better risk management through more effective financial reporting practises of companies. This includes implementation of the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD).

It is crucial that climate change policies are shaped to support investment in low carbon and climate resilient development across the whole of the economy.

Introduction and overview

IGCC represents over 70 Australian and New Zealand institutional investors with more than $2 trillion of funds under management, along with members of the investment community focused on the impacts of climate and energy issues.

IGCC members are invested across all parts of the economy. As managers of retirement savings and pooled investments we are concerned with the evident and increasing impacts of climate change on the global and New Zealand economies and the flow through impacts for investment returns.

New Zealand's response to climate change needs be inclusive of considerations for the economic and investment implications of the global response to climate change. This includes the setting out a practical pathway for ensuring New Zealand's economic competitiveness in a carbon constrained global operating environment over the longer term.

Investors are calling for action

Investors are already taking action on climate change. A global, low carbon, transition is underway. Investors are leading the way through significant investments in low carbon technologies, climate resilient infrastructure and supporting the transition away from fossil fuels.

More needs to be done by Governments to accelerate the low carbon transition and build investor momentum and confidence. By putting in place credible policy, governments can unlock the significant amounts of capital required to drive this transition.

In June 2018, over 319 investors, responsible for more than USD $28 trillion in assets joined as signatories to the 2018 Global Investor Statement Governments on Climate Change ahead of the meeting of G7 heads of state.[1]

Through the statement, investors called on Governments to deliver on the three core principles:

1. Achieve the Paris Agreement's Goals;
2. Accelerate private sector investment into the low carbon transition; and
3. Commit to improve climate-related financial reporting.

Central to these principles was an acknowledgement by investors that we must proactively transition away from fossil fuels. Through the statement, investors called for a phase out of fossil fuel subsidies, as well as a phase out of thermal coal power by set deadlines.

Additionally, investors have collectively called on governments to address the "ambition gap". Implementation of the current emissions reduction commitments made by Governments is insufficient for meeting the Paris Agreement goal of limiting global warming to well below 2 degrees above pre-industrial levels.

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[1] The Investor Agenda, *2018 Global Investor Statement to Governments on Climate Change,* 4 June 2018 - https://theinvestoragenda.org/wp-content/uploads/2018/06/GISGCC-FINAL-for-G7-with-signatories_-update-4-June.pdf

Investors are seeking the introduction of credible policies to build momentum and maintain investor confidence, and to set emissions reduction targets that reflect an appropriate level of ambition to support work towards decarbonisation of the economy.

Priorities for Investors

In recent years, a significant shift has been occurring in how business and the financial community views climate change and the need to reduce greenhouse gas emissions. Specifically, carbon has moved from being seen solely an environmental issue to being understood more as an economic risk. Whether physical, regulatory, market-driven or technological, climate change has financial implications for business and for investors.

With a view to establishing a trajectory towards decarbonisation under the *Zero Carbon Act,* New Zealand needs to be managing carbon risk as an economic and a financial risk and working to facilitate an economically efficient transition to a net zero emissions economy in line with global commitments under the Paris Agreement.

Continuing to build expertise, skills and capacity to manage climate change related financial risks and opportunities will underpin New Zealand's future economic profitability in a net zero emissions global economy. The need to integrate climate science scenarios into policy decisions is critical to future-proofing our economy. The establishment of an ambitious, long-term investment signal towards decarbonisation must be a core principle in the development of the *Zero Carbon Act*.

A robust and stable policy framework will drive greater levels of investment into low carbon solutions and will help smooth the economic risks associated with structural decarbonisation of the New Zealand economy.

The impact on investment flows must be a key consideration for policy decisions.

2050 Target

1. *What process should the Government use to set a new emissions reduction target in legislation?*

The setting of ambitious, long-term emissions reduction targets that are to be achieved by set deadlines is crucial for both creating investor confidence and allowing for a carefully planned transition to a zero-carbon economy.

The New Zealand Government should legislate a specific 2050 target, with a view to tasking the Climate Change Commission to develop an achievable trajectory to meeting that target, including providing advice on interim, sectorial, targets to support that trajectory.

By locking in a specific 2050 emissions reduction target of reaching zero emissions, the New Zealand Government would establish a clear and meaningful signal that would support investor confidence. A long-term signal, complemented with short to medium term targets that are reviewed regularly, is more likely to drive investment into the cost-effective emissions reductions while allowing for a flexible approach to managing economic impacts and changed market conditions.

2. *If the Government sets a 2050 target now, which is the best target for New Zealand?*

IGCC supports the setting of a net zero greenhouse gas emissions target for 2050, that covers all types of greenhouse gas emissions and all sectors of the New Zealand economy.

Nationally Determined Contributions, as set and revised under the Paris Agreement, must include details of the scope and coverage of the economic sectors and greenhouse gases covered by a specified emissions reduction level. The New Zealand Government must seek to be consistent across both its domestic and international commitments to avoid confusion and uncertainty.

IGCC notes the significant role that the agricultural sector plays within the New Zealand economy, being both the largest contributor overseas exports by value, as well as the largest sectorial contributor to greenhouse gas emissions. However, the agricultural sector and land-use management also provide significant opportunities for the management of national emissions.

There is every reason to believe that the opportunity for sustainable finance in the agricultural sector will continue to grow, including through investments from superannuation funds. Starting from a relatively low base, the investment market in forest conservation, sustainable forestry, and sustainable agriculture is growing rapidly. Doubling in the last decade, the market is attracting more and more mainstream investors.[2]

Between 2004 and 2015, an estimated $8.2 billion of private capital was investment in conservation and sustainable land-use projects globally, including US$6.5 billion of investment in sustainable food and fibre production. The estimated total market for conservation and deforestation-free supply chain investments range between US$160 and US$400 billion by 2020 [2,3], highlighting the potential scale of market value to be achieved through sustainable land-use management practises.

The Low Carbon Investment Registry, launched in 2014 by the Global Investor Coalition on Climate Change, details examples of real-world low-carbon investments being made globally by institutional investors, including in the agricultural and forestry sectors.[4] An analysis of the results submitted to the registry found that agriculture, forestry and land-use management was the second largest recipient of green investment by value, with significant growth in investment flows targeting the sector.

In this context, the New Zealand Government should establish a net zero emissions target that covers all sources of greenhouse gas emissions, including the methane that is predominantly produced by the agricultural sector. It has been long established that methane

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[2] F Huwyler, J Käppeli & J Tobin. *Conservation Finance from Niche to Mainstream: The Building of an Institutional Asset Class* (Credit Suisse Group AG and McKinsey Center for Business and Environment, 2016).

[3] Tropical Forest Alliance 2020, 2017, Ibid.; F Thompson and A Charlton, *Better growth with forests—economic analysis*. Background paper for TFA 2020 General Assembly, 10–11 March 2016 (Jakarta, Indonesia) (Jakarta: Tropical Forest Alliance, 2016);

[4] Low Carbon Investment Registry - http://globalinvestorcoalition.org/form-registry/

is a significant contributor to global warming, and therefore should be covered by national climate change targets.

3. *How should New Zealand meet its targets?*

IGCC supports a market-based price on carbon. IGCC members have long supported a price on emissions as the most effective and efficient way to provide a long-term, transparent and certain regulatory framework to address carbon risks in investment portfolios.

Market based responses allow business and the market to respond flexibly and effectively. They support greater innovation and competitiveness. They promote the efficient allocation of capital and investment and generate longer term prosperity. Policy responses which are short term, fixed and finite, or which have involved direct intervention in the market by Government, have usually proven to be less effective in supporting longer term structural change.

The IGCC supports robust, investment grade policies to reduce emissions. IGCC members believe that a price on emissions is the most effective and efficient way to provide a long-term, transparent and certain regulatory framework to address carbon risks in investment portfolios. Impacts on pricing for households (and wholesale price markets) can be explicitly addressed via scheme selection and market design.

Emissions reductions driven by a price on carbon should be complemented by sector specific measures. These may include targeted public finance vehicles for low carbon development, fuel and energy efficiency standards for buildings and transport, and research and development funding to support emerging technologies and innovations to come to market.

IGCC in principle supports the inclusion of high-quality offsets as a means of providing flexibility under an ambitious emissions reduction target. However, the allowance of offsets under the must not detract from investment in meaningful emissions reductions in the New Zealand economy.

The inclusion of offsets under the Zero Carbon Act should focus on suitable domestically generated offsets, such as high-quality reforestation projects. It is important that an appropriate regulatory regime is established to assess the quality of offset projects and ensure proper safeguards are in place to ensure environmental integrity.

To ensure emitters are incentivised to seek out cost-effective actions within the New Zealand economy to reduce the emissions, the use of offsets should be capped to a certain portion of any emissions reduction liability.

Potential mechanisms that would facilitate the introduction of internationally sourced offsets under the Zero Carbon Act, while being consistent with the Paris Agreement are still under active negotiation. In light of this, there is insufficient information available to allow IGCC tod definitively support international offsets at this time.

More broadly, IGCC remains supportive of the use of international units in principles and at such time in the future as the rules for issuance and fungibility become clearer, including arrangements being negotiated under Article 6 of the Paris Agreement.

4. *Should the Zero Carbon Bill allow the 2050 target to be revised if circumstances change?*

The long-term investment signal that an ambitious 2050 target provides is crucial for investor confidence and it is therefore important that such a target is established by legislation.

The setting of interim carbon budgets, that can be set and revised through regular timelines, should provide sufficient flexibility for the New Zealand Government to set a carbon reduction trajectory that is mindful of national, and global, circumstances.

The Climate Change Commission should be tasked with determining appropriate interim sectorial targets, allowing an expert independent body to provide recommendations to government on achievable actions that are consistent with the best available science. By allowing the emissions trajectory to be adjusted in this way, New Zealand's emissions reduction trajectory can be both responsive to issues including changes in economic conditions and the costs of technologies without losing sight of the overall long-term goal of decarbonisation.

If there was a significant change of national circumstances that would warrant a change in New Zealand's long-term emissions reduction target, normal parliamentary processes covering the amending of Acts would allow appropriate amendments to be made.

Emissions Budgets

5. *The Government proposes that three emissions budgets of five years each (ie, covering the next 15 years) be in place at any given time. Do you agree with this proposal?*

IGCC supports the setting of interim carbon budgets that are consistent with achieving the long-term goal of reaching zero net emissions in New Zealand by 2050.

With the establishment of a forward trajectory with interim targets at five-year intervals, New Zealand has the opportunity to align the review and ramping up of domestic action with the ratchet mechanism for Nationally Determined Contributions under the Paris Agreement.

The independent Climate Change Commission should be engaged to determine the appropriate, achievable and ambitious, interim emissions budgets, through engagement with industry and informed by the best available science. This will increase the credibility and robustness of the target setting process.

Additionally, the development of interim carbon budgets should facilitate the development of sectorial targets, likewise informed by each sector's ability to drive lowest cost abatement and ensure investment in domestic abatement can be prioritised over the sourcing of international offsets.

6. *Should the Government be able to alter the last emissions budget (ie, furthest into the future)?*

IGCC would support the ability to amend the last emissions budget, covering 10 to 15 years of a forward emissions trajectory, under the guidance of an independent Climate Change Commission.

A general principle of increasing ambition should be established to prevent "back-sliding" under a forward emissions trajectory. The New Zealand Government may seek to increase the effective ambition, by reducing the allocated budget for a period, however a stricter set of criteria would need to be developed to outline the circumstances under which interim carbon budgets may be increased.

7. *Should the Government have the ability to review and adjust the second emissions budget within a specific range under exceptional circumstances?*

IGCC would likewise support the ability to amend the second emissions budget, covering 5 to 10 years of a forward emissions trajectory, under the guidance of an independent Climate Change Commission, and within a limited range.

It is however crucial that the impact on investors be actively considered, and investments made in response to the *Zero Carbon Act*, especially in circumstances that result in a lessening of emissions reduction ambition. Consistent, long-term, emissions reduction targets are essential to provide investors the confidence to invest in low and zero carbon development.

8. *Do you agree with the considerations we propose that the Government and the Climate Change Commission take into account when advising on and setting budgets?*

Investors have a crucial role to play in tackling climate change. Investors are both concerned about the impact that climate change will have on their existing investments, and also looking to identify investment opportunities to support climate change action through investments in low carbon and climate resilient developments.

Significant barriers remain to low carbon and climate resilient investment, and ways to address these barriers need to be considered in the development of Government policy. The New Zealand Government should work with investors to understand these barriers, so that effective solutions and support can be put in place to adequately address them.

Government Response

9. *Should the Zero Carbon Bill require Governments to set out plans within a certain timeframe to achieve the emissions budgets?*

The development of national plans for meeting New Zealand's emissions reduction goals should plan an important part in shaping Government policy to support action on climate change. With a suite of climate change measures, such as the NZ Emissions Trading Scheme, and any sources of public finance for low carbon development, plans to meet national emission reduction targets should inform how these complementary measures are designed and operate.

The establishment of individual targets for each of the major economic sectors within the New Zealand economy are important for providing direction and certainty for where investment flows towards decarbonisation need to be directed and prioritised. This would need to be aligned with the signals provided by the NZ ETS across sectors.

Interim sectorial targets would also allow for the prioritisation of emissions reductions into areas where the cost of abatement is low. For example, early emissions reductions may wish to target the energy sector, where fuel switching can be a low-cost form of abatement, while other sectors, such as agriculture, can be provided more time to develop plans for future emissions reductions.

10. *What are the most important issues for the Government to consider in setting plans to meet budgets? For example, who do we need to work with, what else needs to be considered?*

It is crucial that interim emissions budgets that are established under a Zero Carbon Act are consistent with the commitments that have been made by Governments under the Paris Agreement. Investors are looking to Governments to establish a strong and credible investment signal that will support the continued decarbonisation of the global economy.

The setting of carbon budgets must provide an effective trajectory towards zero net emissions in 2050 and facilitate a smooth and efficient transition. A gradated reduction in emissions allows for the economy to appropriately adjust to operating on the basis of low and zero emissions.

This trajectory will also avoid the extra costs that come with unpredictable and a rapid transition that may occur if emissions targets are set or changed with minimal notice to the market.

Climate Change Commission

11. *The Government has proposed that the Climate Change Commission advises on and monitors New Zealand's progress towards its goals. Do you agree with these functions?*

IGCC supports the establishment of an independent expert body to oversee the setting and revision of New Zealand's emissions reduction targets, and assessing the progress being made towards the achievement of those targets.

The United Kingdom's Committee on Climate Change, which has specific responsibility for advising the UK Government on appropriate emissions reduction targets, as well as reporting to the UK Parliament on progress being made in reducing emissions and preparing for the impacts of climate change serves as a potential model for how a New Zealand equivalent body made operate.

12. *What role do you think the Climate Change Commission should have in relation to the New Zealand Emissions Trading Scheme (NZ ETS)?*

The Climate Change Commission should serve in a monitoring and advisory role, reporting to Government on the performance of the NZ ETS in the context of the overarching Zero Carbon Act.

The Climate Change Commission should be tasked with the following in relation to the NZ ETS:

- Monitoring the performance of the ETS
- Advising on the volume of allocations under the ETS
- Monitoring and advising on the price signal sent by the ETS and how this is driving investment
- Monitoring the evolution of international carbon market frameworks under Article 6 of the Paris Agreement and implications for the NZ ETS
- Recommending to Governments where reforms may be necessary

Market conditions can change quickly, and it is important that while a market-based mechanism is maintained to drive economic development towards decarbonisation, that a body such as the Climate Change Commission has an oversight role to ensure policies are meeting their intended aims.

13. *The Government has proposed that Climate Change Commissioners need to have a range of essential and desirable expertise. Do you agree with the proposed expertise?*

The membership of the climate change commission should reflect the diversity of the New Zealand community, as well as knowledge and expertise required to transition the New Zealand economy to net zero emissions. A crucial consideration when setting targets is to ensure ambition is determined with the best available science and such expertise should be reflected in the membership of the commission.

The view of investors, as key provider of capital that will support the transition to a low carbon economy, should be considered as part of the independent climate change commission processes. In particular, knowledge and understanding of the barriers to low carbon investment, and how these barriers can be addressed, along with the economic implications of decarbonisation trajectories should be reflected in the membership of the Climate Change Commission.

Adapting to the impacts of Climate Change

14. *Do you think the Zero Carbon Bill should cover adapting to climate change?*

The impacts of climate change are being felt right around the world, and it is now crucial that Governments begin the preparation of detailed plans for how these impacts are going to be managed in New Zealand. National Adaption Plans are an essential tool for the management of critical infrastructure, planning for extreme weather events and for the future design of the built environment.

IGCC notes that a full and complete assessment of the infrastructure at risk to the effects of climate change should also be a key consideration for climate change policy frameworks.

In April 2017, IGCC published '*Risk to Return: Investing in Climate Change Adaptation*'.[5] Developed through a multi-stakeholder climate adaptation finance consultation process, it aims to identify real world investment barriers and recommend potential solutions, with the goal of enabling the finance sector to access adaptation investment opportunities. It also sets out a pathway forward with specific recommendations.

The report builds on IGCC's 2015 publication, 'Investing through an adaptation lens – A practical guide for investors', which described the risks, opportunities and associated interdependencies related to climate change that investors need to consider in order to adapt. The guide addressed these issues for investment in three sectors: direct property investments, direct infrastructure investments and listed equities.

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[5] IGCC, *From Risk to Return: Investing in Climate Change Action, April 2017, https://igcc.org.au/wp-content/uploads/2017/03/Adaptation_FINAL.pdf*

A requirement for private owners and managers of infrastructure to assess, report and act on identified risks from climate change should be considered, to complement any National Adaptation Plans prepared that are to be prepared by the New Zealand Government.

15. *The Government has proposed a number of new functions to help us adapt to climate change. Do you agree with the proposed functions?*

IGCC supports the inclusion of requirements for the New Zealand Government to development an assessment of climate change risk and a National Adaption Plan.

IGCC likewise sees the ongoing review and updating of the climate change risk assessment and adaptation plans as crucial. The Climate Change Commission should be tasked with assessing the progress of National Adaption plans and providing recommendations to Governments in this regard as it sees fit.

16. *Should we explore setting up a targeted adaptation reporting power that could see some organisations share information on their exposure to climate change risks?*

Carbon risk disclosure should be focused on ensuring that financially material carbon risks are adequately measured and disclosed to allow investors, the market and the wider community to assess impact and performance.

While existing emissions and financial reporting frameworks have proven to be useful building blocks in carbon disclosure, they no longer comprehensively serve the needs of investors who are seeking to understand and price the financial implications and effective management of carbon risk.

For investors assessing company performance, key dimensions of carbon risk are chronically underreported, ill-defined, immaterial, out of date or inconsistently disclosed.

Under the oversight of the G20, the Financial Stability Board Task Force on Climate related Financial Disclosures (TCFD) was established with the potential to profoundly reshape corporate disclosure on climate change.

In June 2017, the TCFD released their recommendations, setting out a framework for disclosure within financial reporting. The TCFD has structured its recommendations around four key areas of disclosure: governance, strategy, risk management, and metrics and targets.

This is supported by additional guidance for all sectors, as well as supplementary guidance for non-financial sectors (energy, transport, buildings and materials, agriculture, food and forest products) and financial sectors (banks, insurers, asset owners, asset managers.

In addition, one of the TCFD's key recommendations relates to reporting the potential impacts of climate related risks and opportunities on an organisation's businesses, strategies, and financial planning under different potential future states (scenarios), including a 2° Celsius scenario.

Many of these recommendations can, and should, be incorporated into the corporate reporting obligations for companies and can serve to significantly improve the ability of investors to understand and account for the impacts of climate change on their investment portfolios.

Conclusions and Recommendations

Through the proposed Zero Carbon Act, the New Zealand Government has the opportunity to establish world leading and best practise policy on tackling the causes and impacts of climate change.

This opportunity presents both challenges and enormous opportunities to place sectors of the New Zealand economy at the forefront of low carbon and climate resilient technologies, practises and development.

A robust and stable policy framework will drive greater levels of investment into low carbon solutions and will help smooth the economic risks associated with transitioning the New Zealand economy to one with zero net emissions.

A stable policy environment is attractive to capital. This includes both ensuring that policy settings are capable of achieving New Zealand's ambitious, long-term, emission reduction goals, but also one which establishes a serious of interim emissions reduction targets that can deliver an emissions trajectory consistent with the Paris Agreement and to limit global warming to less than 2°C.

As the global economy transitions in line with the Paris Agreement, New Zealand can and must take steps to remain economically competitive. Failure to effectively manage climate change creates the risk that New Zealand will become increasingly uncompetitive as investors look to manage down climate change risk and pursue new low carbon finance opportunities in other markets.

In this submission, IGCC has sought to provide responses against each of the questions pose by the Ministry for the Environment in its consultation paper. IGCC would be happy to facilitate further discussion with investors on the design of the Zero Carbon Act, and related policies, as part of this review.

We look forward to continuing to constructively engage in further discussions with the Ministry for the Environment on these matters as consultation on the design of the act progresses.