Ministry of Transport
TE MANATŪ WAKA

BRIEFING

20 January 2021 OC201027

Hon Michael Wood
Minister of Transport

Action required by:
Thursday, 21 January 2021

Clean Car Standard - Cabinet Paper

Purpose

This briefing provides an updated Cabinet paper on the Clean Car Standard for lodgement and consideration by Cabinet on 26 January, together with an explanation of changes made since the previous version and advice on related topics you have requested.

Key points

- We have amended the Cabinet paper to include a recommended year of 2026 for the 105g target, with alternative options of 2028 and 2025.
- An ambitious date of 2026 to reduce vehicle emissions by 40% to 105g is achievable assuming it is complemented with strong support policies including a Clean Car Discount.
- We have made other minor amendments to the proposals in the paper including to create flexibility for you around reviewing targets, to give the industry more flexibility in how it reaches the target, and to allow finalisation of the weight-adjustment limit at a later date.

Recommendations

We recommend you:

1 **Authorise** the attached Cabinet paper for lodgement Yes / No

2 **Note** the changes to the Cabinet paper including the recommended headline target year of 2026 Yes / No

Personal details

[redacted]

Ewan Delany
Manager, Environment, Emissions and Adaptation

20/01/21

Hon Michael Wood
Minister of Transport

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Minister's office to complete: ☐ Approved ☐ Declined

☐ Seen by Minister ☐ Not seen by Minister

☐ Overtaken by events

Comments

Contacts

Personal Details

Name	Telephone	First contact
Ewan Delany, Manager, Environment, Emissions and Adaptation	[redacted]	✓
Sigurd Magnusson, Senior Advisor		

Clean Car Standard - Cabinet Paper

We consider the Cabinet paper ready to lodge, it has been updated to provide rationale for your recommended 2026 target year

1 We understand the Prime Minister will make a public announcement about the Clean Car Standard on 29 January 2021.

2 This document seeks to finalise key design elements to enable Cabinet to give approval to the design of the Standard on Tuesday 26 January 2021.

3 A draft Cabinet paper was sent to you late December 2020. The attached version contains several changes, including the recommendation that the 105g target apply to 2026.

4 The wording of the recommendations in this version of the Cabinet paper enable you to make minor adjustments to the cut-off for the weight-adjusted target and other minor design decisions. This design feature would subsequently be confirmed through the process of implementing the relevant legislation and regulation.

5 Waka Kotahi, EECA, and MBIE have been re-consulted on these latest changes and their input factored in.

We recommend the headline emissions target remain at 105 grams

6 We recommend you maintain the emission targets discussed to date. These are 105 grams of CO_2 per kilometre as the headline emissions target, split between 102 grams for cars and SUVs and 132 grams for utes and vans, adjusted for weight.

7 This maintains consistency with discussions and consultation with the industry and wider public, election commitments, our modelling, and because it has been shown to be achievable internationally in jurisdictions that have strong vehicle CO_2 emissions policy. Latest figures show Europe attained 105g in 2020 and is targeting 95g this year for cars and SUVs. Japan attained 105g in 2014 for cars and SUVs. Global leader Norway reached 50g for cars and SUVs in 2020 and 156g for utes and vans in 2019.

A 2025 or 2026 target is ambitious and thus relies on supporting policy interventions

8 The ability of the industry to reach the target soon (i.e. 2025 or 2026) will depend on strong demand-side measures. That view is expressed by the MIA, various suppliers such as Toyota and Tesla, and is also the Ministry's view.

9 Without demand-side measures, a target year of 2028 is more realistic, because the high purchase price of low and zero emission vehicles will reduce consumer demand for them.

10 Independent advice from the International Council on Clean Transportation (ICCT) advised us that New Zealand setting a target requiring a 40 percent reduction in CO2 emissions from new vehicles over 6 years (2020 to 2026) is:

- too short a period of time to both impose a very ambitious level of CO_2 reduction and give industry sufficient time to adjust to operating in a regulated environment
- plausible but unlikely to be achievable without extremely strong vehicle policies beyond the Clean Car Standard and the Clean Car Discount.

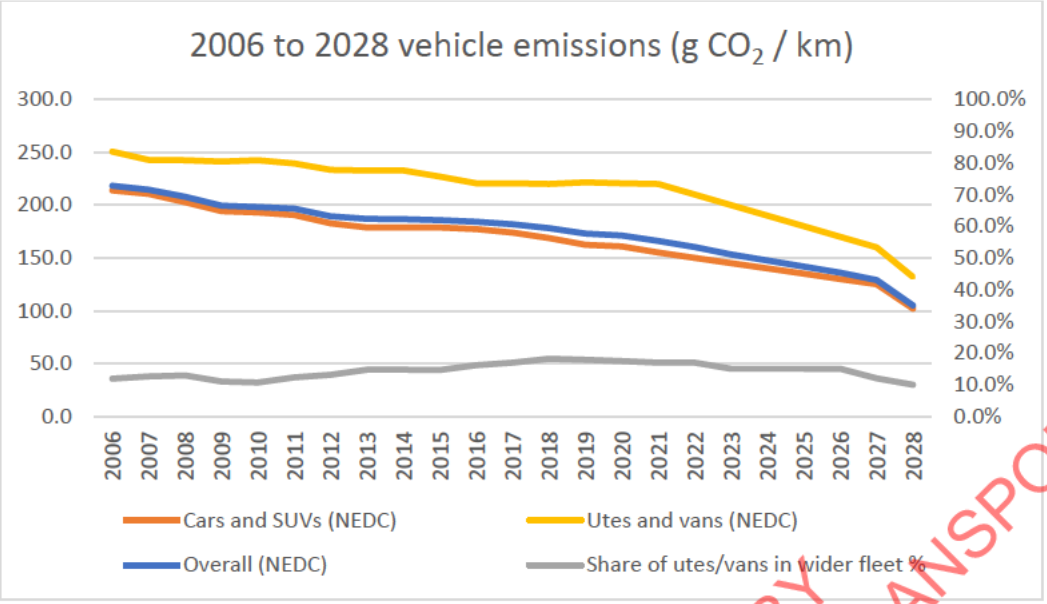
11 Therefore the industry is likely to view a target of 2025 or 2026 as roughly equivalent in terms of difficulty to achieve a 105g target. It is the level of demand side supporting measures rather than the 12 month timeframe that makes a bigger difference to reaching a target quickly. some manufacturers and either 2025 or 2026 very challenging and are likely to push back on such a timeframe.

12 There is apparent public support for Clean Car policies. An AA member survey on carbon costs was carried out in September 2020 and received 1079 responses. The AA survey showed 2:1 support in favour of a Clean Car Standard with a range of views on policy outcomes and price impacts. A total of 75.3% of respondents supported the principle of raising prices on vehicles that are above an emissions target, with a quarter answering that such fees should fund the lowering of prices on more fuel efficient cars.

A 2028 target year would still require a large change in buying behaviour

13 Noting that a 2028 target is suboptimal in terms of the emissions reductions it would generate, it is important to note that it would still represent change from the current trajectory. On average, there has only been a 1% reduction in vehicle emissions for the past decade. In certain segments, such as utes, there has been no emission reduction at all for several years. In order to reduce emissions from 171g today to 105g by 2025, the annual rate of emission reduction would need to increase fourfold, and we would expect the market share of utes and vans (currently 17%) to reduce to levels found earlier this decade (10%), at least until such time as low or zero emission variants of such vehicles are widely available.

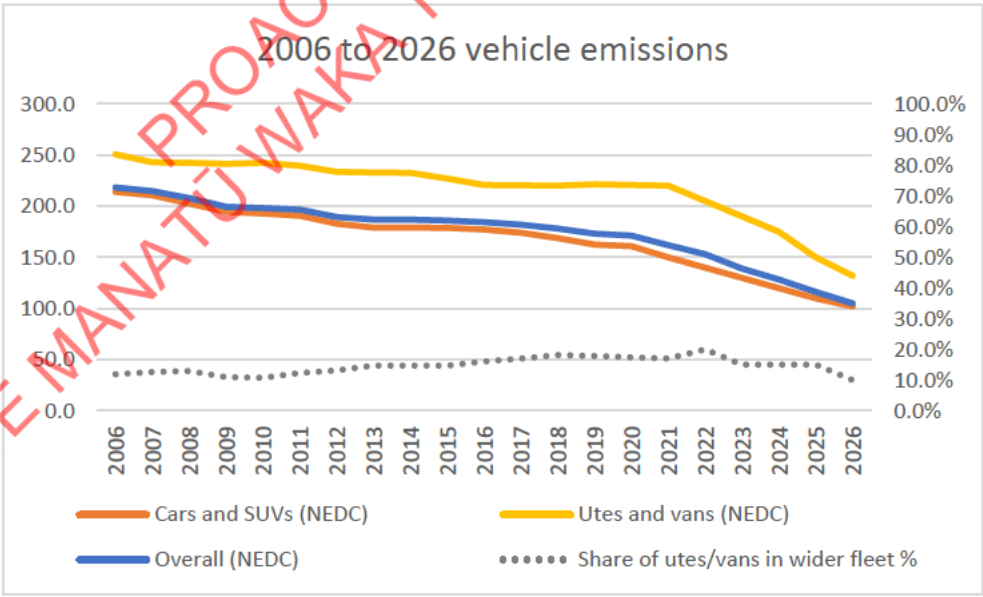
14 The chart below shows actual vehicle emissions up to the end of 2020 followed by a scenario achieving 105g by 2028. This model assumes Government support is limited toa Clean Car Standard with no or minor additional policies, meaning the industry is given time to make incremental progress initially and has to make a large jump in the final year.



A 2026 target requires a major shift

15 The following graph shows the effect of compressing the target year to 2026 and helps to illustrate the importance of supportive policies that assist with pricing. The historical 1% rate of improvement would need to raise to 8%.

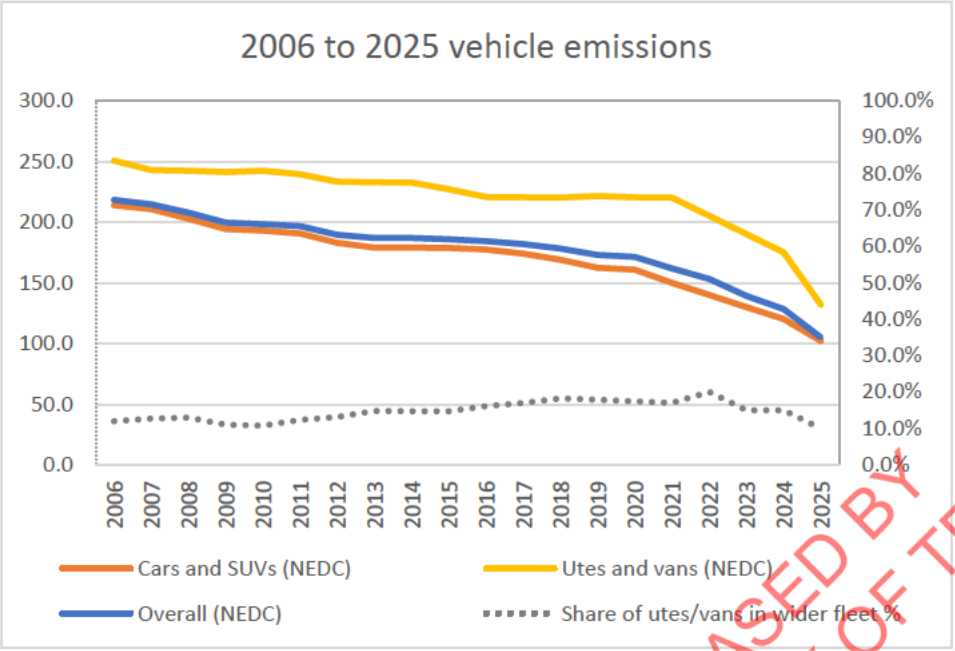
16 Despite utes and vans having a more generous grams/km target, the level of improvement they are forced to make is striking compared to the current, flat trajectory in recent years (refer yellow line). This scenario is likely to generate a spike in purchasing of utes before there is downward pressure on their market share to reduce emissions.



A 2025 target could cause significant disruption

17 While a 2025 target may have been appropriate when originally suggested by the Ministry's consultation in 2019, the delay in implementation means it would require

too rapid a shift, both for cars and SUVs, but especially in regards to utes and vans, for this to be a recommended scenario:



To support a 2025 or 2026 target year, additional demand-side measures will be needed

18 They demand-side policy with the strongest cost/benefit assessment and strongest effectiveness to reaching the 105g target soon is a Clean Car Discount. This policy would increase demand for zero and low emission vehicles by reducing their price. In its policy design, while discouraging the purchase of high emitting vehicles.

19 Further complementary light vehicle policies are also advisable to ensure the 105g target goal can be met. These are the subject of Budget initiatives and will be addressed further in future advice:

19.1 Road User Charge Exemption on Electric Vehicles, ideally until the target year or until such time as it is obvious the target level will be comfortably met. The exemption is to currently expire at the end of 2021;

19.2 A Fringe Benefit Tax or Tax Credit on Electric Vehicles, to further support business uptake;

19.3 Community-based initiatives to increase access to low emission transport options to all New Zealanders, including cars and e-bikes; and

19.4 The proposed biofuel mandate.

20 We also consider that the following proposed policies will be complementary because they build social awareness of and licence for cleaner vehicles:

20.1 Decarbonisation of the public transport bus fleet

20.2 Vehicle scrappage scheme pilot

The Cabinet paper now recommends a 2026 target and notes you will ask Cabinet to consider further interventions targeting light vehicle emissions

21 The Cabinet paper now outlines 2025, 2026, and 2028 as options, and seeks Cabinet to make a choice. It recommends 2026 as providing a little more time for industry than a 2025 target, while moving with sufficient urgency to align to the Government's wider climate commitments.

22 The Cabinet paper also notes that you will return to Cabinet with further policy recommendations, including as part of Budget 2021.

We have made some other minor changes to the recommended design of the Standard – as set out in the Cabinet paper

23 These changes will make it easier for the industry to reach the target, enable progress sooner, and ensure the reductions measured translate into actual emission reductions. These are now contained in the updated Cabinet paper.

Change 1: Replacing the Grouping mechanism with Transfers will offer greater flexibility

24 The Clean Car Standard is to have a flexibility mechanism allowing overachievers in the industry to support others that are underachieving. This creates larger fleets of vehicles over which the CO_2 from high emitting vehicles can be offset by low emitting ones.

25 Originally we proposed a grouping approach based on a model adopted in Europe and the USA. It would require formal agreements between suppliers, allowing their joint emissions to be averaged. Grouping arrangements would need to be approved by Waka Kotahi.

26 We now recommend a different approach: CO_2 transfers. Instead of formal grouping agreements, transfers would more flexibly allow suppliers to transfer overachievement of their CO_2 target to one or more other suppliers. A supplier would be able to perform transfers at any time during a year, and to any recipient they wished. The restriction that transfers could not occur between the new and used vehicle industry would remain. Government would not impose a fee for transfers or get involved in their pricing; that would be left to the industry to negotiate.

27 This gives increased flexibility as the industry is more likely to be able to avoid charges from underachievement, whilst ensuring the overall fleet targets are met.

28 It also provides benefits to Waka Kotahi. In the case of debt collection or enforcement activity Waka Kotahi would have needed to pursue multiple companies that are jointly and severally liable under a grouping system; such legal complexity is avoided by adopting transfers because each businesses remains individual. Waka Kotahi also advise that the IT systems needed to support transfers are faster to set up, reducing the implementation time by one or more months, and is cheaper to maintain.

29 As had been the case with grouping, limits on distributing or receiving transfers of CO_2 credits may need to be considered at a later point if unintended consequences are occurring.

Change 2: We recommend updating our Emission Standards, not just Test Cycles

30 The proposal to date has focussed on transitioning New Zealand from older to newer emission *test cycles*, which state how emissions are measured. We now also recommend that we tighten emission *standards*, because these will progressively narrow the wide gap between measured emissions and real world performance.

31 In the long term this will improve confidence that the emission reductions we calculate from vehicle tests are actually translating into lower emissions into the atmosphere.

32 The Land Transport Vehicle Exhaust Rule already regulates these standards and updating this is a straightforward regulatory change which can be done as part of a Bill for the Standard in 2021 or early 2022. This gives us the first half of this year to confirm the phase-in dates.

33 Thought needs to be given to progressive dates in terms of differentiated treatment of the used and new market, and vehicles originating from Europe, Japan, and, in particular, vehicles that are sold via suppliers that treat Australia and New Zealand as a single market.

34 Suppliers who treat Australia and New Zealand as a single market may find it challenging to supply New Zealand with more modern vehicles until such time as Australia updates their emission standards later this decade. Such suppliers could choose instead directly supply New Zealand with the best vehicles available. The issue of some suppliers being tied to Australia's lower quality fuel and similar lack of emissions regulation is leading to New Zealand receiving vehicles with higher fuel consumption (thus CO_2 emission) and other harmful pollutants than other developed markets.[1]

35 In general we would look to adopt the latest Euro 6 standards in a staggered approach this decade, and equivalent steps for Japanese and other standards. New Zealand currently allows Euro 4 vehicles for used imports (banned 11 years ago from sale in Europe) and Euro 5 vehicles for new vehicles (banned 6 years ago). China and India have recently adopted an equivalent to Euro 6, meaning New Zealand is behind globally, not just by OECD standards.

36 While the rationale for this is focussed on CO_2 emissions, modernising our vehicle emission standard will substantially reduce harmful NOx, carbon monoxide, and particulate emissions, particularly for diesel vehicles.

37 Ford Ranger and Toyota Hilux diesel utes available in the UK have long been sold to Euro 6 standards, however we have not reviewed the impact on their supply should New Zealand adopt the same.

38 We recommend that officials discuss this with the industry and provide recommended phasing during the first half of 2021, allowing the relevant Rule to be updated in 2022 to support the introduction of the Standard.

[1] Australia had indicated in 2011 it would adopt Euro6 in 2017 but this was pushed back 10 years to 2027. The industry is currently being consulted on that date. Part of Australia's delay is due to having to perform costly upgrades to their oil refining sector. Currently Australia's fuel is incompatible with modern vehicle emission standards. New Zealand's fuel is already compatible with modern standards.

Change 3: More generous 2022-2024 phase in makes 2025/2026 easier

39 A final tweak to make a 2025/2026 target easier to achieve is by setting less onerous targets for the early years (2022 to 2024). This gives more time for the industry to source cleaner vehicles whilst protecting the overall target ambition. The phase-ins recommended are graphed at the end of this briefing and are in numerical form in Appendix 1 of the Cabinet paper.

40 It would be possible to revise the phase-in periods even more generously (e.g. having no emission reductions in 2021 and 2022) if you conclude the first year where targets apply should be easier for the industry to achieve.

Change 4: you asked for advice on strengthening the 2024 review mechanism to take account of officials concerns if we proceed with a more ambitious 2025/6 target.

41 In general, we are comfortable with the review mechanism as it stands. The first review occurs in 2024, meaning it is soon enough to revise the 2025 target before final-year fees apply. It is late enough to maximise the time for the global and local industry to show what is possible in terms of emission reduction. Finally, it already invites the Minister to determine the terms of reference for the review, which allows for flexibility, advice to be supplied at the time, and a holistic approach to be taken.

42 We recommend three minor changes in terms of the approach to review. These are now incorporated into the Cabinet paper:

42.1 The timing of the review be clarified to occur “in the first half” of 2024 rather than at any time in 2024. This ensures there is sufficient time to change the 2025 target if necessary.

42.2 Note that the 2024 review, in addition to vehicle CO_2 emission reduction, take into account the “impacts on vehicle safety, affordability, and availability”. While this is likely to occur in any case, it provides the industry some assurance now that emission reductions won’t be so strongly focussed on to eliminate the industry’s ability to feasibly supply sufficient diversity and quantity of vehicles needed by the market.

42.3 Make explicit that the review include the two split targets and evaluate changes in the proportion of cars, SUVs, utes, and vans in the New Zealand vehicle market. This reduces risk around assumptions we have make today.

Advice on why a weight-adjusted target is appropriate

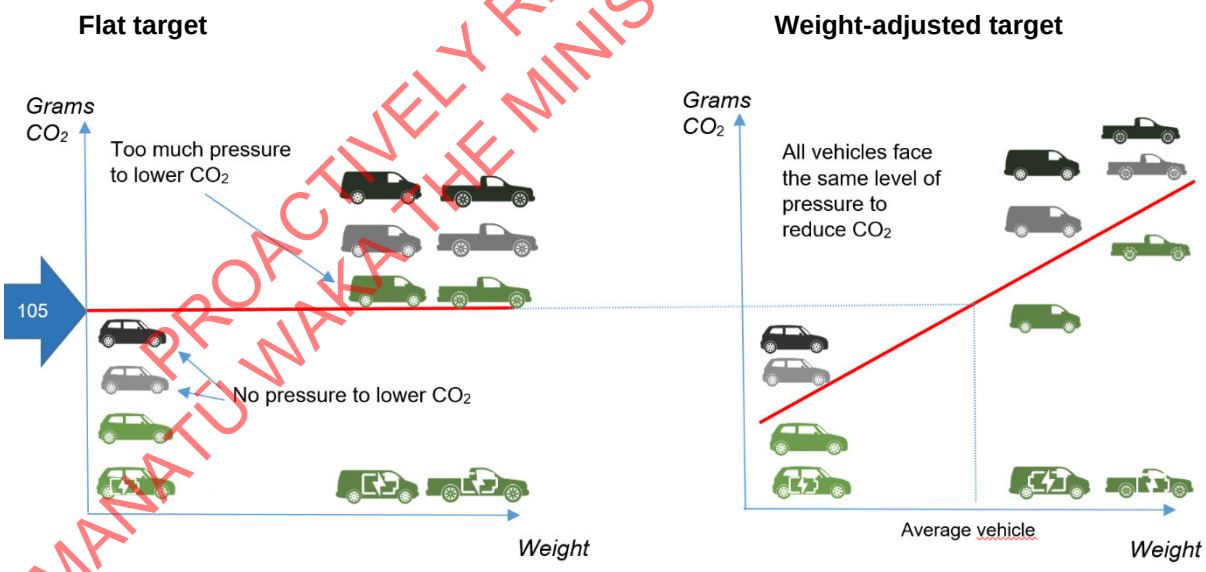
43 We understand you wish to discuss with colleagues why a weight-adjusted target is preferred to a flat target (as had been proposed by the Government in 2008) . This was outlined in briefing OC200968 and in summary is:

- A flat target puts too little pressure on small vehicles to reduce emissions, and too much pressure on large SUVs, utes, and vans. A weight-adjusted target ensures all vehicles, from small cars to large utes, face the same amount of pressure to reduce emissions.

- By ensuring all vehicle types face equal pressure to reduce emissions, a weight-adjusted target avoids supply constraints and price increases that could occur if some vehicle segments were restricted. Vehicle constraints will be a very real issue given the limited supply leverage New Zeland has on the global automotive market, coupled with the desire for rapid emission reduction this decade.

- A flat target would create equity issues and be counterproductive, by limiting the supply of larger vehicles, even when some of these vehicles have decarbonisation value, such as hybrid people-movers and hybrid SUVs. It could also limit the supply of utes and vans needed for a commercial purpose before they are affordable or available in low or zero emission format.

- A weight-adjusted standard will not influence the mix of vehicle types, for example, cars versus SUVs or utes. What it will do, is increase the supply of vehicles with lower CO_2 emissions across the spectrum of light vehicles. To make gains in emission reductions by encouraging consumers to move away from larger vehicles to smaller vehicles, a complementary demand side initiative, like a Clean Car Discount, is needed. A Discount would do this because its fees and rebates would be based purely on the level of a vehicle's CO_2 emissions and would not be weight-adjusted.



Accompanying this briefing:

1. A3 showing a 2025 target
2. A3 showing a 2026 target (your recommended approach)
3. A3 showing a 2028 target
4. Clean Car Discount Cabinet Paper