

Professional Paper

Forestry and climate change

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The Select Committee report on the Climate Change (Emissions Trading and Renewable Preference) Bill has recently been circulated together with a revised Bill.

In this article we focus on some of the detail of the changes to the Bill with implications for the forestry sector. We also provide a brief update on other aspects of the Government's climate change initiatives as they relate to forestry. In particular the Afforestation Grant Scheme and the Permanent Forest Sinks Initiative.

Background

The ETS is an integral part of the Government's package of policy initiatives aimed at climate change and greater sustainability. By establishing a framework to put a price on greenhouse gas emissions, the ETS seeks to "support global efforts to reduce greenhouse gas emissions" by reducing New Zealand's net emissions below business-as-usual levels.

Under the ETS a core obligation is imposed on parties carrying out specific activities (for example, deforestation of pre-1990 forest land). That obligation is to report and surrender to Government a tradable emission instrument, either a New Zealand Unit (NZU) or, other Kyoto Compliant Units (such as an AAU) for each tonne of CO₂ equivalent emissions for which that party is responsible over the relevant period.

Under the ETS the ability of a forest to remove CO₂ from the atmosphere is recognised by allocating NZUs to participating owners of eligible forest (post-1989 forest land) for each tonne of CO₂ so removed. Those persons whose activities are deemed to generate reportable greenhouse gas emissions can purchase NZUs from the likes of such holders to meet obligations to surrender units under the ETS.

From a forestry perspective the ETS effectively divides forest land into three categories: land planted in exotic forest species prior to 1990 and still in forest as at 31 December 2007 (pre-1990 forest land), land that was first planted in forest from the beginning of 1990 or was covered in forest at that date, but subsequently deforested between 1 January 1990 and 31 December 2007 (post-1989 forest land) and "natural" indigenous forest. The Select Committee was of the view that the last category should remain outside the ETS at this point.

We now make some comments and observations in relation to the amended Bill by reference to the categories of pre-1990 forest land and post-1989 forest land.

Pre-1990 Forest Land

Allocation of Free NZUs

Owners of pre-1990 forest land will, in most situations, be required to account for deemed emissions on conversion of such land from forestry to another land use (eg conversion to dairy farms). Under the Bill, in partial recognition of this restriction on owners of such land, there will be an allocation of free NZUs to such land owners.

Understandably, such land owners made vigorous representations to the Select Committee (and via the media) about the impact of this Government policy on their property rights. In response, the Select Committee has recommended a number of changes to the Bill in relation to the proposed allocation of free NZUs for pre-1990 forest land. The free allocation process requires an allocation plan to be arrived at following a process of public submission. This approach is still to be followed, but the Bill now contains additional detail as to the process. Under the revised Bill, the previously indicated approach of a simple pro rata allocation of NZUs based on land area has been dropped.

The allocation for pre-1990 forest landowners remains capped at a total allocation of 55 million free NZUs (in two tranches with different effective usable dates). However, some landowner groups have been singled out for varied treatment in any allocation of free NZUs under the revised Bill.

The first group are owners of pre-1990 forest land who acquired the land prior to a date to be stipulated (some time in late 2002). We understand the rationale for singling out this group is because they would have purchased their land prior to indications in 2002 that some form of deforestation liability may be imposed and so would not have factored into their buying decision the restriction on land use. Their allocation is to be increased from 39 NZUs to an estimated 60 NZUs per hectare. At a carbon price of, say, \$20 per tonne of CO₂ equivalent, this equates to a change from \$780 per hectare to \$1,200 per hectare. Other owners of pre-1990 forest land who acquired their land after the 2002 date continue to receive 39 NZUs per hectare, on the basis that they ought to have been aware of potential restrictions on land use. The 2002 date is seen by some as being arbitrary and unjustified.

The second group are Treaty claimants who receive Crown forest licence land under a Treaty settlement at any time from 1 January 2008 up to the allocation date or, having received such land prior to 1 January 2008, that

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land is identified as eligible land in the allocation plan. The allocation in respect of such land and parties is to be 18 NZUs per hectare. In essence, the flexibility to achieve the above increased allocation comes from the Crown (as owner in its own right of pre-1990 forest land - Crown forest licence land) reducing its share from 39 NZUs to 18 NZUs per hectare.

As can be appreciated, the changes to the Bill still leave some of the detail of this relatively complex re-juggling exercise to the appropriate allocation plan. In particular, we see potential issues around clarifying what is meant by “eligible land” in the context of an allocation to pre-1990 forest land, the 2002 cut off date and what does, or does not, constitute a change of ownership.

Offsetting of Deforestation Liability

Pre-1990 forest landowners, including members of the Flexible Land Use Alliance (which includes companies such as Blakely Pacific Ltd, Carter Holt Harvey Ltd, Fonterra Co-operative Group Ltd, Forest Enterprises Ltd, Landcorp Farming Ltd, the New Zealand Forest Owners Association Inc., PF Olsen Ltd and Wairakei Pastoral Ltd), also vigorously lobbied the Select Committee with a proposal for an offset scheme.

In essence they suggested that in the interests of fairness pre-1990 foresters be allowed to change the use of their land without attracting the potentially quite large liability for deemed CO₂ emissions by planting an equivalent new forest on other bare land (offsetting).

Following consideration of their submissions, the Select Committee noted that under the Kyoto protocol there is no provision for offset planting without incurring deforestation liabilities. However, the Select Committee was of the view that the Bill should contain a mechanism such that if the international rules for the second commitment period (commencing in 2013) changed to allow such a scheme, then there should be suitable flexibility within the Bill to allow such a scheme. Namely, that an owner of pre-1990 forest land could apply to offset any liabilities for deforestation of an area of pre-1990 forest land by planting an equivalent area of bare land.

The Select Committee saw merit in laying the foundations for such an offsetting scheme in the Bill to enable both Government and affected landowners to be able to make decisions quickly should the international rules change. In other words whilst the detail surrounding what is compliant offsetting land has been left for later regulations there will be no need to amend the primary legislation.

As can be appreciated this concession is something of a “wait and see”, but it goes some way to recognise the concerns raised by pre-1990 forest landowners as to the adverse impact

of the proposed ETS on their property rights.

Post-1989 Forest Land

Owners of post-1989 forest land can choose to participate in the ETS and collect NZUs for each tonne of CO₂ sequestered. Upon harvesting the participating owner of the forest is then required to account for the deemed CO₂ emissions.

There have been a number of wording changes in relation to those sections of the Bill dealing with post-1989 forest land. In the main these changes are, relatively speaking, issues of detail and/or clarification rather than significant policy changes.

Pre-1990 Forest to Post-1989 Forest Land

New detailed drafting ensures that a pre-1990 forest landowner holding 50 hectares or less who obtains exempt land status and carries out deforestation but, then at a later time, wishes to enter that land into the ETS system as post-1989 forest land can do so subject to surrendering deemed emissions resulting from the earlier deforestation. In other words, the land will be treated as if it had not been declared to be exempt land in the first place.

Grantor Liability Post Forestry Right

Clarification and certainty has been provided around the transfer of an ETS registration in relation to post-1989 forest land. For example, where the participant is the holder of a registered forestry right, but not the owner of the underlying land, and that forestry right expires or is terminated. At the point of expiry or termination, the landowner becomes the participant in respect of that post-1989 forest land. The former participant (ie forestry right holder) is still liable to submit an emissions return and surrender an appropriate number of NZUs.

We see this as an area where owners of the underlying forest land who are considering proposals from, say, an existing or prospective forestry right holder to enter the subject land into the ETS will need to have a clear understanding as to their respective rights and obligations and the processes and procedures to be followed upon expiry of the forestry right.

Traceability of NZUs

The Bill has also been amended to ensure that it does not prevent giving participants sufficient documentation about the ownership and source of NZUs. This documentation would enable third-party certifiers to link NZUs or AAU's to specific forests. In a global carbon market where buyers are demanding transparency and traceability of emission

units, this may well assist forest owners to market their NZUs to maximum effect.

National Party Minority View

Given that 2008 is an election year where Labour is trailing National in the polls and there is no guarantee that this Bill will be passed before the election, we comment briefly on the National Party's minority view on the Bill. The National Party considers the forestry provisions of the Bill to be "seriously deficient" and considers that there is an urgent need for a fresh process of engagement with the forestry sector to develop a more sound and practical approach to greenhouse gas emissions and plantation forestry.

Specific concerns include:

- the "artificial" distinction between pre-1990 and post-1989 forest land and the resulting inequities of treatment
- arbitrary definitions from the Kyoto Protocol which do not reflect reality, including the "fallacy" that carbon is released on harvest, ignoring carbon stored in timber products
- arbitrary provisions which give perverse incentives, including, for example, an incentive to replant pre-1990 forest land then clear fell the replanted crop at age 8 to minimise any deforestation liability
- deferring the entry of liquid fuels into the ETS to 2011 significantly reduces the market for NZUs that forest owners may wish to sell.

Other Government Measures Complementary to the ETS

In addition to the ETS mechanism the Government is keen to encourage long-term afforestation using other afforestation initiatives such as the Afforestation Grant Scheme (AGS) and the Permanent Forest Sinks Initiative (PFSI).

Under the AGS would be participants tender for afforestation grants and carry out afforestation post-1989 forest land. In return AGS participants acknowledge that they are unable to enter that land into the ETS and collect NZUs.

The AGS participant can sell the timber. The Government gets the sequestration benefits and is liable for emissions under the Kyoto Protocol. A particular feature of the scheme is the reservation of part of the funding for species with low carbon sequestration rates. This is to reflect the public interest in planting indigenous species.

Tenders for the first round closed on 30 June 2008. At the date of writing the Government had yet to announce the results of that tender round.

The PFSI is a scheme under which the Government grants emission units in return for the planting of "permanent" forest. There has been some media comment about the relatively low rate of take-up under the PFSI. This may be due to potential participants wanting to see how the ETS develops. However, the Ministry of Agriculture and Forestry has received several PFSI applications, including one from SFM New Zealand Pty Ltd (a Simpson Grierson client), and at the time of writing we understand some applications are very close to being finalised.

Conclusion

The Bill has received mixed reviews from different parts of the forestry sector. There have been generally positive reactions to such changes as increased free allocation to certain owners of pre-1990 forests (at least from those receiving the increased allocation), the prospect of offsetting deforestation liability by planting bare land, and to the post-1989 forest regime generally. However, many in the forestry sector remain unhappy with certain fundamental aspects of the regime for reasons such as those outlined in the National Party minority view. There is still no date set for a second reading debate on the Bill and progress of the Bill beyond a second reading remains uncertain.