



26 October 2007

MEDIA BACKGROUNDER

NZFOA response to the Government's proposed Emission Trading Scheme Announced September 2007

Overview

1. The NZFOA welcomes the government's decision to allocate carbon credits and liabilities to those owners of Kyoto forests who want to participate in carbon trading (Kyoto forests are those planted from 1 January 1990).
2. We also welcome options intended to encourage new forest plantings. It is gratifying to see recognition of the range of environmental and economic services provided by forests and wood products.
3. In total the Government has responded positively – in whole or in part – to three of the six Kyoto policy points requested by the forest industry. In other respects the latest policy proposals fall well short of what is required.

Because they do not provide equitable treatment across competing land uses, or across past and future forest investors, the forest industry considers that these proposals will not achieve their stated objectives.

Specifically they are inequitable, over-complicated, inconsistent, insufficiently comprehensive, and do not signal the path to a reduced carbon emission economy clearly, or rapidly, enough.

4. They are also overly focussed on the regulation of forestry and under-focussed on the key emitting sectors. Agricultural intensification and fossil fuel use result in increased atmospheric Greenhouse Gas (GHG) emissions. Despite this, carbon emitters or polluters, including the transport and energy sectors, will be shielded from most of the cost of their impact.
5. Agriculture is effectively being quarantined from Kyoto obligations at the expense of forestry. Given a finite land base, and the fact that some investors are influenced by relative profitability in their land-use decisions, this will be highly distortionary and is likely to work against government climate change objectives.
6. The NZFOA supports the polluter-pays principle on which New Zealand's environmental legislation is based. If appropriate market-based Kyoto policies were applied across the economy, there would be no need to introduce policies to stop land-use change from forestry to farming.

7. The government's earlier policy proposals have had an extremely negative impact on confidence and investment in the forest sector, and have contributed to deforestation decisions. We anticipate that under the new proposals there will continue to be negative sentiment in the industry and that this will influence planting & replanting decisions.

Pre-Kyoto forests

8. The government's policy regarding pre-Kyoto forests mirrors the wording of the Kyoto Protocol.

The protocol was designed to protect indigenous forests and is irrational in its treatment of plantation forests. For this reason, the forest industry asked the government to develop Kyoto policies which had the best long-term outcomes for New Zealand, even if they didn't exactly mirror the Kyoto rules.

9. The government has ignored this advice, even though trees planted pre-Kyoto (before midnight on 31 December 1989) remove CO₂ from the atmosphere in the same way as Kyoto-eligible trees (those planted since).

Some of that CO₂ is removed long-term (wood used in building structures) and some of it temporarily (tree prunings left to decompose and mill waste burnt as fuel). But regardless of what happens to the products from a forest, the emissions following the harvest of New Zealand's non-Kyoto forest should not be treated in the same way as the burning of fossil fuels which inevitably add to atmospheric CO₂. At worst, a forest planted into pasture, harvested and replaced with pasture, over say 35 years, will be carbon neutral.

10. Under the Kyoto protocol, pre-Kyoto forests are treated like fossil fuels. If they are harvested and not replanted, a liability is created for New Zealand. The government has chosen to pass most of this on to forest owners. The only concessions are:

- o No liability on blocks of 2 ha and potentially up to 50 ha
- o In the past, the government has indicated that it will accept liability for deforestation equal to "historic rates" – defined as 21 million tonnes. This is known as the "Deforestation cap". Assuming 800 tonnes CO₂/ha, this equates to 26,250 hectares over the 5 years of commitment period 1.

Given 1.2 hectares of Kyoto forests and a 26,250 hectare government cap (spread over 5 years), the concession is minimal, if it indeed it is included in the final policy.

11. Forest owners wishing to deforest will have to buy NZ Emission Units (NZUs) on the open market.

The cost of doing so will be substantial – a likely minimum of \$12,000 a hectare (\$15/tonne NZU x 800 tonnes/ha). In addition, the IRD has proposed that this liability should be a capital transaction – more than \$17,000 in forest revenue net of costs at a tax rate of 33 cents in the dollar.

This cost will give forest owners the incentive to adopt practices which are economically rational, but otherwise perverse.

Expect to see:

- o Widespread deforestation continuing until 31 December. Deforestation following the 2005 announcement of the government's intention to impose a Kyoto deforestation tax has already led to markets being over-loaded with logs and a fall in log prices.
- o In forestry blocks with underlying land titles of 50 ha or less, deforestation of a patchwork of these titles post-2007.

In most situations, however, the cost of buying NZUs for deforestation will mean many blocks in Kyoto forests will be effectively locked into forestry forever.

12. The effect of this will be to effectively reduce the value of such land to zero. This, or even a negative value, is based on the amount a forest owner could afford to pay for the land in order to achieve an economic return from a crop of radiata pines to be harvested in 30 years time. [Source: Steve Wilton, Forest Enterprises, Masterton.]
13. The question of who assumes responsibility for deforestation liabilities between land owner and forest manager is another key consideration. Liability appears to lie with the entity that controls the decision. Thus, in a situation where a land owner contractually requires land to be returned post-rotation to them in an un-forested state then they are liable. This will significantly, and adversely, affect Maori land owners who negotiated arrangements pre-Kyoto in good faith.
14. The government's judgement in respect of pre-Kyoto forests appears to be coloured by a prejudice against land owners making so-called windfall profits from the conversion of forestry to dairy farms. An economically rational response would be to encourage conversion where it is environmentally sustainable, on the condition that the forest owner replanted elsewhere on hill country which is better suited to forestry than livestock.

This process of "forest transfer" is not permitted under Kyoto's rules, but would be sensible from the point of view of the country as a whole. When forests in the Central North Island were planted in the 1920s, the land was known as "bush sick" because animals did not thrive there. Now we know that topdressing with the trace element cobalt cures this problem, making many of these areas ideal for livestock farming. It is everyone's long-term interest for land to be used for its most economically sustainable use.

15. In total, the liability for deforestation imposed on the forest industry for its pre-Kyoto forests is massive – \$14.4 billion, assuming 800 tonnes/ha, \$15/tonne CO₂ and 1.2 million hectares.

NZFOA consider it neither reasonable nor logical that land owners who have made no net contribution to carbon emissions through forestry investment

should be penalised for their actions, particularly when those who have contributed significantly to emissions are being left untouched

This liability should be carried by the Crown as the price of ratifying Kyoto and for including forestry in that ratification, against the express wishes of the forest industry.

In a worst case scenario, no more than 200,000 hectares are likely to be deforested and only 50,000 of these are likely to be harvested in commitment period 1. (MAF estimates that this is the area of land suitable for livestock conversion).

16. By removing this liability from the forest industry it would:
 - o Remove the overwhelming sense of injustice which pervades the forest industry.
 - o Inject new confidence into an industry which, with the right policy signals, has a huge potential to create value for the NZ economy and to solve – through renewed planting programmes – many of the issues associated with New Zealand’s transition to a carbon neutral economy.
 - o Result in land owners making economically rational decisions regarding the best use of their land

Agriculture

17. Forestry competes for land with other rural sectors, some of which are indirectly subsidised by being exempted from paying the true environmental cost of their emissions. This allows them to pay a higher price for land, to the disadvantage of those wanting to invest/reinvest in forests.
18. The government appears to be reluctant to control agricultural emissions out of fear that it “may constrain agricultural production”. This does not appear to be a concern with the forest sector.

Sustainable land management will be hard to achieve if the government is unwilling to do anything that conflict with farming’s ability to operate as a permitted activity. Forestry enjoys no such privilege. Since all forest activities are assessed on the basis of effects, logic and equity dictate that all land uses should be treated in the same way.

19. It is intensification of agriculture, primarily, the growing national dairy herd, that has been, and will continue to be, the major emissions problem for New Zealand. Strategically addressing the issue of dairy emissions is, to some significant degree, likely to address deforestation as this is the main driver of deforestation.
20. New Zealand will be held accountable for all agricultural emissions regardless of the practicalities of reduction. Any sheltering of agricultural emissions has to be made up from somewhere else if NZ is to meet its targets and

effectively it is the forest sector that is being asked to shelter the agricultural sector.

21. To date, research has not delivered cost-effective options for reducing methane emissions and therefore the government accepts that reduction in emissions from the agricultural sector may not be as great as from those in other sectors. However, the opportunity to offset those emissions through other means does exist – notably through offsets such as forest sinks.
22. Forest sinks from tree planting would provide flexibility for farmers and will typically result in the delivery of many of the other benefits that the government lists as being concurrent goals such as erosion control, enhanced biodiversity and improved water quality. They would also be a valuable and viable mechanism for farmers to meet the carbon emission obligations.
23. The NZFOA urges that work should begin immediately on a tradable emissions permit scheme that involves the agricultural sector, that it should not be restricted to just nitrous oxide and that less than full grand-parenting of emissions is appropriate.
24. It is acknowledged that the technical issues surrounding the development and implementation of a trading scheme are not insignificant. Challenges also exist in implementing such a scheme for the forest sector. The scheme may need to evolve, and be modified, over time but, again, such challenges are not a sufficient justification for rejecting a trading permit approach.
25. Conversely, seeking to control such emissions by putting constraints on, and only on, ex-forest land is not a sophisticated response. Equitable and consistent policy would target any land management option that resulted in a higher level of greenhouse gas emissions than the existing use. This would include, for example, conversion of sheep and beef to dairy, horticulture to agriculture, bare land or scrub to agriculture, and intensification of existing agriculture within the same farming type.
26. There is a huge potential to integrate plantation forestry into the NZ landscape. Up to 1 million hectares of steep and erosion-prone farmland would arguably be better off in forests. This would make land use more sustainable overall and greatly simplify the management of many farms where the steeper areas are hard to graze efficiently and are often prone to weed infestation. Europe is a good model for this – with 9 million forest owners averaging 13 ha each. [Source: Michael Cambridge].

[ends]