

Observations of a DysFunctional ETS

A FORESTRY PERSPECTIVE



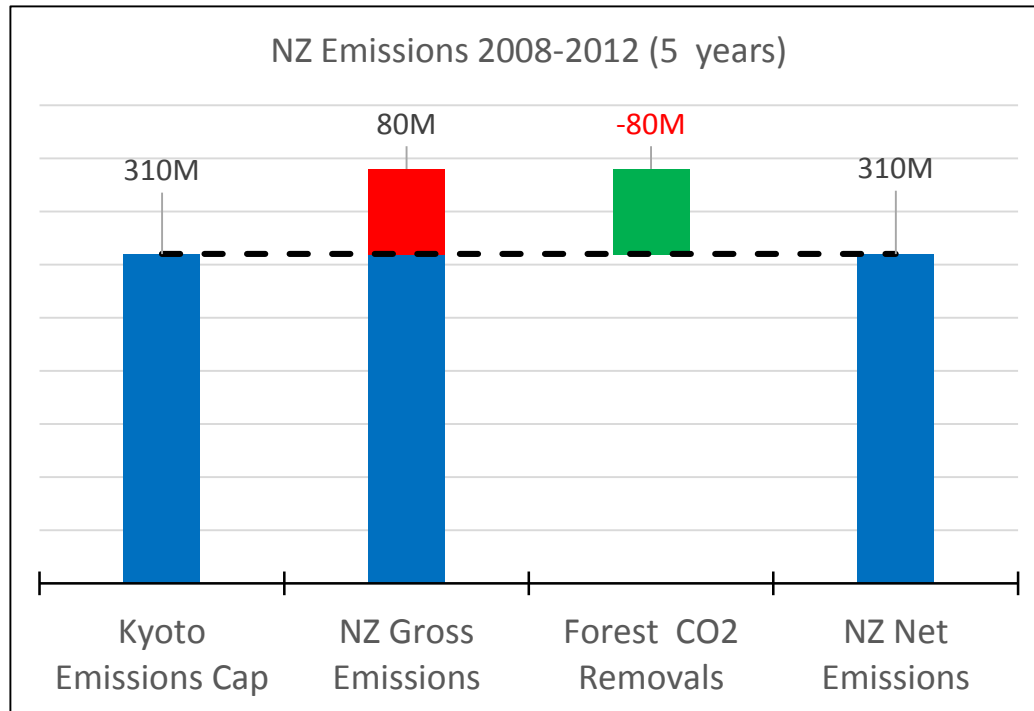
www.permanentforests.com



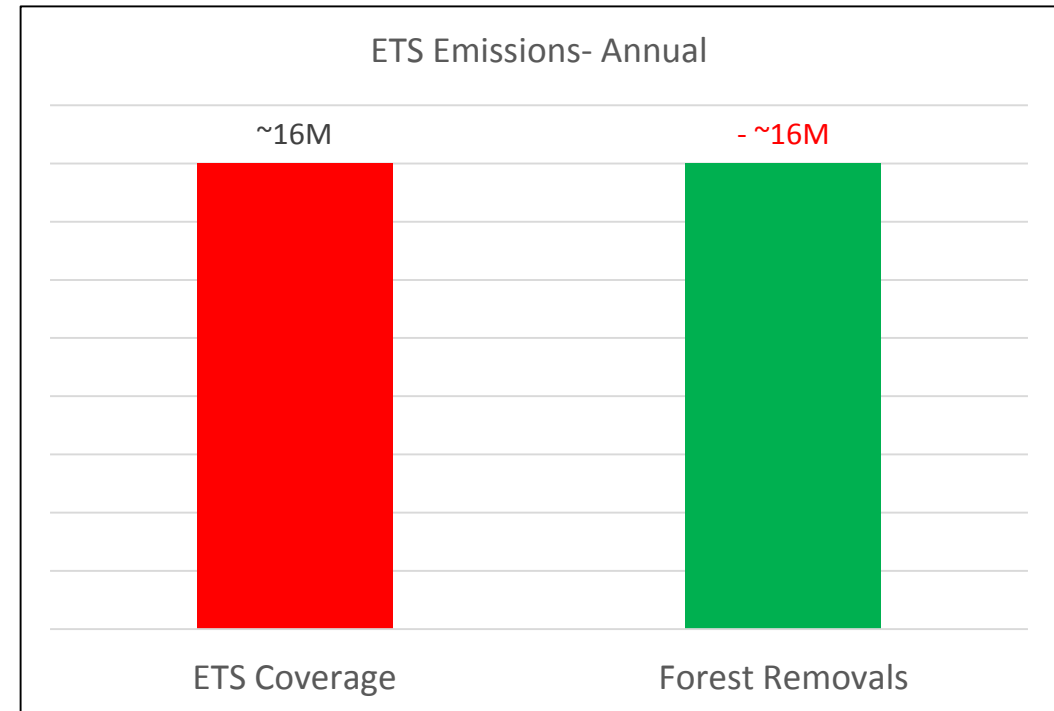
www.carbonforestservices.co.nz

The Big Picture- Framing the Context

WHY DO WE HAVE AN ETS?
TO REDUCE EMISSIONS? BUT AT LEAST COST

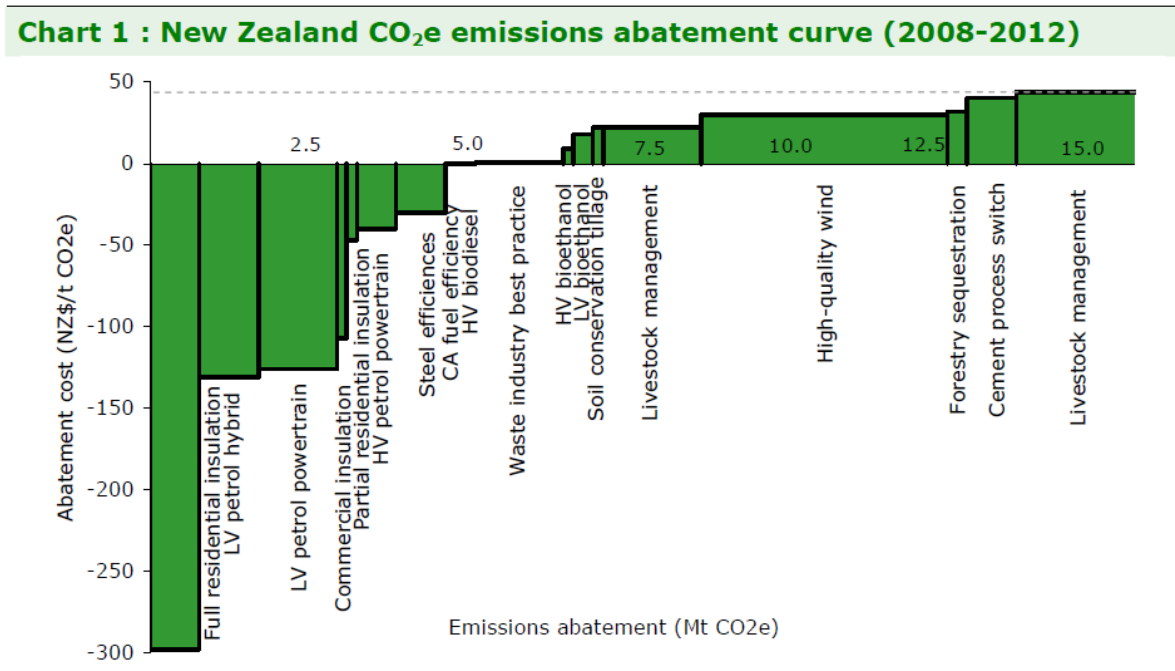


HOW TO REDUCE EMISSIONS?
NZ FORESTS CAST IN LEADING ROLE



Should Forestry be the Star Role?

- Offsetting versus Reducing Emissions
- Other low cost options which are marginalised?
- Forestry is good because it buys time
- Offset Intractable Agricultural Emissions
- Forestry also provides other co-benefits
- All options incl. forestry have part to play



Notes: The dotted grey line represents the current EUETS CO₂e price of €21/t CO₂e (NZ\$41/t CO₂e); light-vehicle (LV), heavy-vehicle (HV), civil aviation (CV).

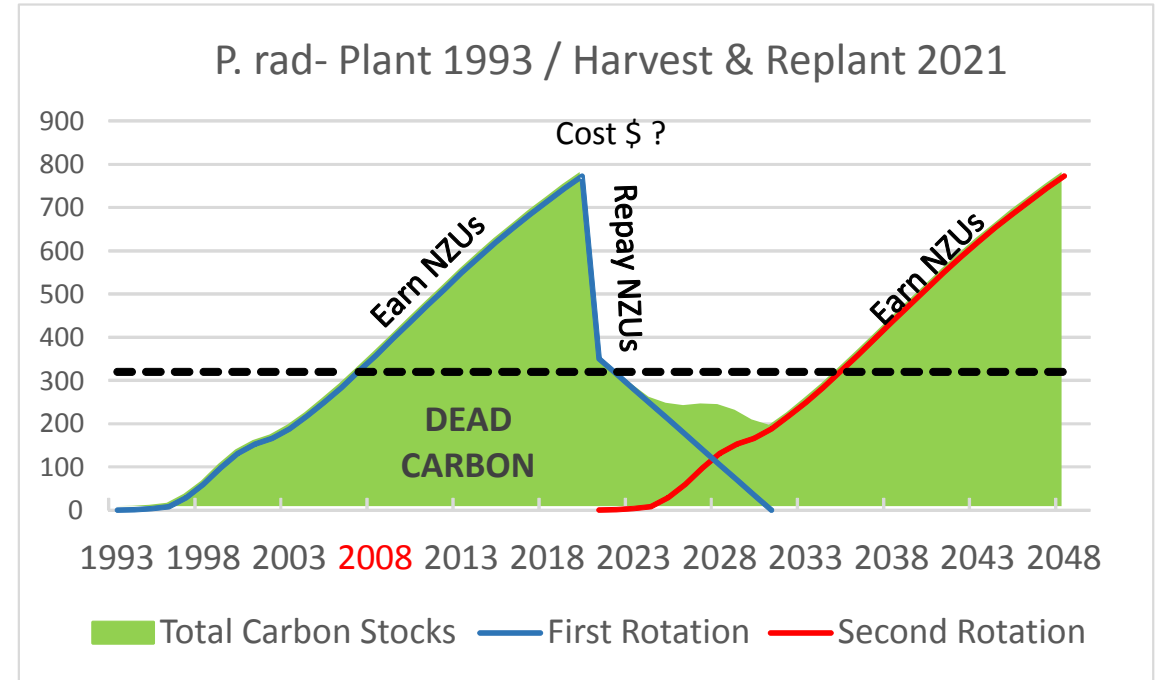
Source: *Our carbon economy* (ABN AMRO December 2007)

Post-89 ETS Forest Estate: Dead Carbon & Harvest Liability

NO SAFE CARBON UPON HARVEST

- ~25% carbon = Safe Carbon
- Most P89 forest planted in 1990s
- P89 Forests Earn NZUs from 2008 onwards
- Dead Carbon from 1990- 2008= Safe Carbon
- None to v. Little NZUs = Safe Carbon
- Means? Forest Owners Play Russian roulette and exposed to fiscal risk at harvest

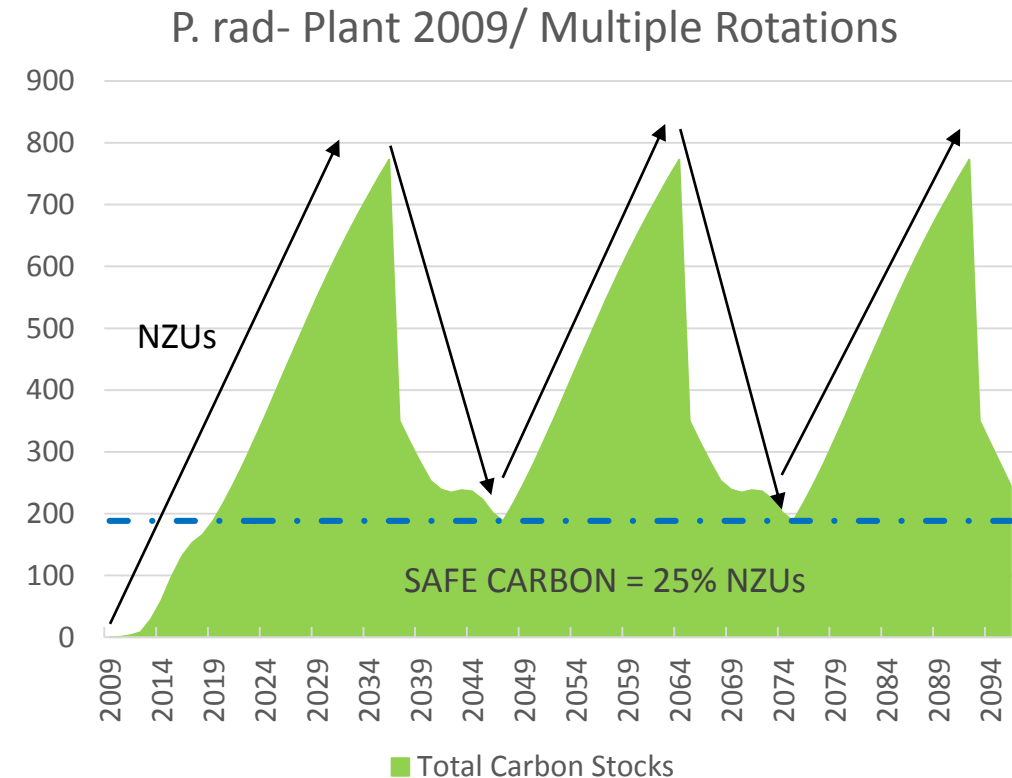
REPAY 100% NZUS UPON HARVEST



Source: P. radiata Auckland Post-1989 Tables Climate Change (Forest Sector) Regulations 2007

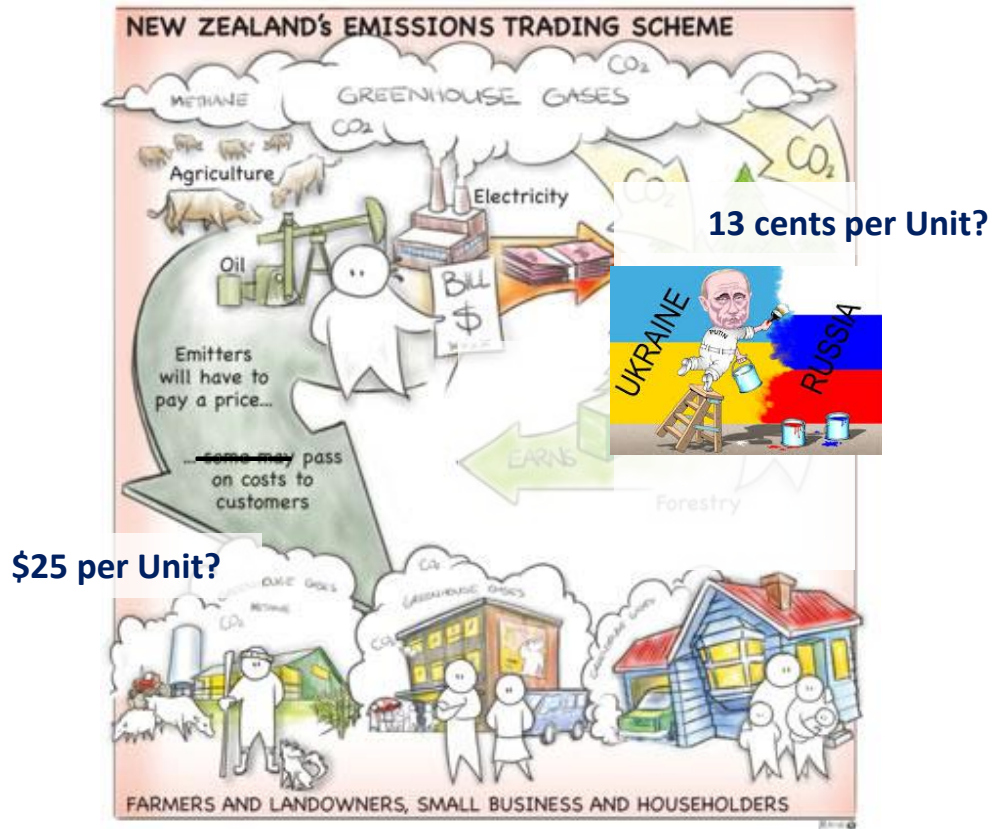
Mitigate Harvest Risk: Options

- Do Not Join ETS for Post 89 Forests
- Manage harvest profile
- Join carbon pool to aggregate forests into large estate
- Do not harvest=Permanent? Not v. suitable
- Plant new forests.... Not really happening
- Play Russian Roulette & take fiscal risk



Source: P. radiata Auckland Post-1989 Tables Climate Change (Forest Sector) Regulations 2007

What Happened to the NZ ETS: Why so Dysfunctional?



- No transparency means Emitters can make \$ from pollution
- Consumers & Small/Med Businesses face possible inflated carbon costs
- >95% units surrendered are foreign
- NZ\$ exported offshore & Forestry participation marginalised
- Carbon price collapse. Low carbon price means no incentive to reduce emissions
- Gross emissions in 2012 increase 25% from 1990 levels. Environment loses out

Source: www.climatechange.govt.nz/emissions-trading-scheme/about/what-it-means-for-me

Carbon Price Collapse: Not all Bad News For Post 89 Forestry

RUSSIAN ROULETTE & UKRAINIAN LAUNDRETTE

- Wipe Harvest Liability using cheap units & make profit
- At least 25% exited the ETS
- Once Exited & wiped carbon liability Re-join again & start earning NZUs
- “Re-registration Arbitrage” or laundering Russian/Ukrainian credits into NZUs
- In 2013, only about 40% exited participants re-joined
- How Come? Disillusioned with ETS..... Low Carbon Price.... Harvest dates approaching.... wait and see what happens to price and policy

Loophole closes: Too late and Not for Everyone

SURPRISE MOVE. GOVT BANS KYOTO UNITS

Problem with Ban

- Government should have acted sooner. Re-registration arbitrage allowed to grow
- No forewarning/ consultation. Forest owners caught out. Already sold NZUs/ Bought ERUs
- Ban only applies to post-1989 forest owners
- Emitters can still use cheap Kyoto units until May 2015

IMPLICATIONS FOR THE ETS & FORESTRY?

- Forest exodus out of ETS
- Latest differentiated treatment of forestry is inequitable
- NZ Carbon Market could languish until at least May 2015
- After 2015, prices may still remain low... Westpac estimate market oversupplied to 110M NZUs

Unforeseen Consequence: Is My Post-1989 ETS Forest Really Pre-1990?

- ETS re-applications subject to rejection of some areas previously registered as P89
- Why? Improved imagery from 1990/ Possible different approach to interpreting eligibility of land use

Consequences:

- Possible registered post-1989 ETS forest not eligible
- Good news- MPI cannot revisit determination of registered forest unless deception present
- But... what about forests that subsequently exit? These appear open to being re-classified
- Has this created an ongoing legacy of risk for present and future owners of registered ETS forests?
- Perhaps a better way forward would be make determinations full and final unless good reason

ETS Forestry Compliance: A Widespread Problem?

- Up to 35% of participants may have a compliance issue
- Compliance can carry significant costs & penalties
- Issue normally Mapping or Emissions Returns
- Part of Problem MPI encourages Self Service
- Online ETS Maps Out of Date
- MPI does not check forest existence in applications
- Poor mapping can lead to over & under allocation of NZUs



MPI Online Map 2009



MPI Online Map 2013



Gorse incorrectly registered as post-1989 forest and forest incorrectly excluded.

ETS Forestry Compliance: A Widespread Problem

EMISSIONS RETURNS

- Emissions returns another compliance issue
- Again MPI do minimal checks on emissions returns
- Participant is responsible (similar to Tax Regime)
- Should ETS Compliance be Same as Tax Compliance....?
- Better to improve MPI systems, implement checks and encourage use of professionals

VOLUNTARY DISCLOSURE

- MPI focus on good compliance over penalties
- >100% penalties can be waived
 - Genuine voluntary disclosure
 - Participants willingness to assist
 - Previous compliance history
 - Reliance on professional advisors
- Sort compliance out now to mitigate risk and costs

Conclusions:

- Emissions Trading Scheme or Carbon Tax?... ETS appears here to stay
- Keep the scheme domestic- limit overseas participation
- No gaming/ No arbitrage- Need Price Transparency
- Forestry need to address dead carbon issue. Need to plant new forests
- MPI process and systems need to be ironed out, including compliance
- Less DIY and more use of carbon professionals
- Most important return balance between “least cost” and “reducing emissions”.
Need a proper carbon price to have a functioning ETS

THANK YOU!

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