
The Emissions Trading Scheme – time for an update

New Zealand takes its place on the global stage with its efforts to combat the effects of climate change. The Emissions Trading Scheme is at the centre of these efforts. Improvements to the Emissions Trading Scheme were announced on 31 July 2019.

Climate change is arguably one of the most pressing threats to the human planet. According to the United Nations, climate change “is the defining issue of our time and we are at a defining moment”.

The Kyoto Protocol requires its members to monitor their actual greenhouse gas emissions and precise records of trades have to be kept. It has set the framework for numerous policy, legislative and environmental initiatives. New Zealand has the unique opportunity of playing its part in reducing greenhouse gas emissions through forestry. Forestry exports are worth around \$5 billion a year and forestry directly employs approximately 20,000 people. It is a crucial part of our climate change response.

With that in mind, it is imperative that New Zealand implement a sufficient, robust and effective Emissions Trading Scheme (*ETS*). On 31 July 2019, improvements to the *ETS* regulations were announced to reach that goal. An Amendment Bill to the Climate Change Response Act 2002 will be introduced to Parliament later this year. Four changes in this Amendment Bill are worth noting:

1. the introduction of “averaging accounting” for foresters;
2. the reduction of free allocation to major industrial emitters;
3. the cancellation and replacement of units from the first commitment period of the Kyoto Protocol; and
4. the introduction of a “stand down period”.

Averaging Accounting

The original carbon stock accounting provides that foresters must surrender their ETS units at deforestation (even if forestry is planted elsewhere). Now, averaging accounting provides that a forest owner will not surrender its emissions units provided the deforested land is replanted (regardless of its location). Given new forestry can be planted in a different location, farm land can be converted to other uses. Foresters are given more flexibility. Under the new regime, the ETS units accumulate as the forest grows up to a determined average level of long term carbon storage.

Previous accounting measures required foresters to repay their emissions units in the event of a natural disaster. The latest changes to the ETS remove the obligation to repay provided replanting is done within 4 years.

Averaging accounting will be optional for forests registered under the ETS from 2019 and will be mandatory for forests registered from 2021 onwards. It will not apply to forests registered in the ETS prior to 2019.

Industrial Allocation

There are currently 26 industrial activities within New Zealand that are eligible to receive free industrial allocation. This allocation reduces their expenses under the ETS which provides an incentive for businesses not to go offshore. These activities are estimated to be responsible for up to 14 percent of New Zealand's greenhouse gas emissions. From 2021, changes to the ETS will phase down the industrial allocation. During the time period of 2021-2030, industrial allocation will be reduced at 1 percent per year. The reduction will then increase to 2 percent from 2030-2041 and increase again to 3 percent from 2041-2050.

Industrial businesses will be encouraged to invest in clean energy alternatives that reduce emissions. The Government has said it will review rates from 2031.

Cancellation and Replacement of Units

There are currently privately held units issued from the Kyoto Protocol's first commitment period (2008-2012). The ETS now require these units to be cancelled and replaced with an equivalent number of New Zealand units. Currently, a host country and the country buying the units could both claim a credit for the emission reductions. Cancelling these units avoids double-counting. The units will be cancelled on 30 November 2020.

Stand Down Period

Previously, forests planted after 1989 outside of the ETS (and some inside the ETS) could deforest and not be liable under the ETS. If replanted, these forests would earn more units under the ETS and would therefore achieve a windfall. This should be avoided since there is technically no increased benefit as the number of trees planted has not changed.

Changes to the ETS now create a "stand down period". If the described land is deforested, the land cannot be replanted (and joined to the ETS) for a period of

time.

Commentary

The above recent changes to the ETS are aimed at more effectively capturing the purpose of the ETS. The introduction of the stand down period and removal of industrial allocations create a more universally comprehensive scheme. However, major industrial emitters will continue to point to the wider economic and fiscal implications of their becoming fully subject to the scheme (and lack of any net environmental benefit in a global context). The issues here are indeed vexed.

The new averaging accounting regime favours foresters. It improves the ETS's flexibility and creates a more appealing system. Forestry land can be replanted in different locations and foresters are also more adequately protected from natural disasters. Encouragement to plant forestry must be met with a realistic scheme that recognises farming and forestry are not static or predictable. Rotating land use enables farmers and foresters to productively work their land without ETS liabilities arising. There are currently concerns over productive farm land being turned into forestry permanently. It is arguable that workable farm land could be lost, reducing New Zealand's agricultural industry. The ability to convert forestry land back to farm or cropping land (with forestry planted elsewhere) helps address these concerns.

Having an effective ETS helps New Zealand to more accurately monitor and work towards reducing its greenhouse gas emissions. These new changes take us one step further to reaching that goal.
