Toitū Te Whenua
Land Information
New Zealand

Interagency Meeting

Date: 24 February 2023

Topic: Costs and Savings from Carbon Emission Reductions under the ETS

Attendees: Claire le Grice (LINZ), Andrew Wells (LINZ), Emma Kelly (LINZ), Luke Hilton (LINZ), Steven Cox (MPI), Tim Denne (MFE), Heather Martindale (MFE), Scott Gulliver (MFE), Melanie Craxton (Treasury), and Lachy Stark (Treasury)

Agenda:

1. Introductions
2. Outline of proposed investment + general benefit to NZ test
3. LINZ's understanding of carbon claims in investment plan
4. Key discussion points re ETS + NZUs + NDC
    a. Is it revenue neutral; or is it a fiscal cost?
    b. Is a new forest a benefit?
    c. How do we recognise the deficit between our NDC (Nationally Determined Contribution) and international targets?
5. Next steps + close meeting

Key points of discussion:

- The aim of the meeting is to discuss the carbon claims, ETS and NDC in general terms rather than to specifically respond to our two current applications. LINZ is trying to assess whether the afforestation can be considered a benefit as claimed in the wider context of the ETS and NDC.
- LINZ needs to be able to articulate in our assessment report whether the afforestation activity is beneficial. The current applications emphasise the economic, environmental, and significant government policy benefits resulting from the afforestation activity. LINZ needs to determine if these claims are credible.
- LINZ is drafting a consultation letter to the applicants of the current applications to outline our understanding of the claims to give them an opportunity to comment. The wording in relation to the carbon claims will need to be reviewed to ensure it is factually correct.
- The outcome of this discussion and thinking will be useful for future applications, however we expect the claims in future applications will be made in different ways, so a broad understanding of the ETS and NDC will assist.
- **Carbon emissions may be neutral as a result of afforestation registered in the ETS**: Forestry registered in the ETS is allocated carbon units (**NZUs**) in accordance with its entitlement under the scheme. These NZUs are not capped, and are additional to the limit the government sets. This means that carbon emissions are technically neutral as a result of afforestation because these additional NZUs may be on sold to emitters allowing them to reduce emissions less than they would otherwise. If or when that on sale actually occurs is not certain.
- **Forestry additionality**: The current price of NZUs incentivises afforestation. The group were clear that ~~P~~p*inus radiata* afforestation in particular is readily occurring in New Zealand. It is likely that this is constrained by practical factors, such as nursery capacity and labour shortages, rather than constrained by lack of capital available in New Zealand. We cannot be

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certain that, but for this forest, the government would have to purchase additional offshore mitigation to meet its NDC.

- ETS units issued to foresters generate an expense ~~are a liability on~~ to the Crown's accounts when they are issued. The stockpile of outstanding units, including those that have been issued to foresters, is an ongoing liability for the Crown. There is no direct cash impact of the stockpile on the Crown and it is not counted as net core debt. Revenue is generated when participants in the ETS surrender NZUs back to the Crown.
    - Revenue, expenditure and the outstanding value of the stockpile are all sensitive to the secondary market price for NZUs. ~~The Crown's economic position is technically neutral as a result, although in reality it's accepted that NZUs may be issued at a different market value than when they are surrendered depending on the length of time in between those two events.~~
- There is a private economic benefit to registered Post-1989 foresters under the ETS.
- **The NDC is not considered a liability on the Crown's accounts:** It is not certain that the government will meet the projected shortfall of its NDC through the purchase of offshore mitigation. There are a number of factors which cause this uncertainty, including:
    - The government is not legally bound to meet its NDC as there is technically no legislative requirement to do so. It's acknowledged however that there is the potential for significant international, policy, climate, and political consequences if the NDC is not met. It is expected that there will be a genuine attempt to meet the NDC but this is not legally required.
    - The Government has the ability to modify or change the obligation before it crystallises – it is within the discretion of the Government to adjust the timing and nature of the costs that will be incurred to meet targets by selecting from a range of policy options available to reduce emissions.
    - There may be technological advances which will contribute to meeting the NDC without purchasing offshore mitigation.
    - There may be a reduction in domestic emissions as a result of various incentives.
- The actual cost of meeting the NDC through the purchase of offshore mitigation is uncertain as the prices for carbon units fluctuate due to a number of factors.
- Treasury provided advice to MOF on the NDC liability in 2021. Treasury has prepared a Climate, Economic, and Fiscal Assessment Report (**CEFA**) on the NDC which is expected to be released in late March.
- **Farming emissions additionality:** The farming emissions related to the subject land will reduce however it is not certain (or even likely) that this will result in a reduction of overall domestic emissions. The sheep and beef grazing will more than likely be moved to another piece of land and continue elsewhere. The sheep and beef do not simply disappear once they are removed from the subject land. This is particularly applicable for a 'winter grazing' block.
- The uncertainty around the actual reduction in emissions as a result of the removal of grazing and afforestation affects the credibility of the economic benefit claim, the environmental benefit claim, and the significant government policy claim.

Action points:

1. LINZ will circulate meeting notes for review;

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Commented [MC[2]: This is due to their ability to on-sell units they have earned, which they earn as they sequester.

Commented [MC[3]: To be technical here:

while the Paris Agreement is a legally binding international treaty, the legally binding elements of the treaty require the Parties to prepare, communicate and report progress against successive NDCs that they intend to achieve (Article 4). **There is no legal requirement to set an NDC at a particular level, to calculate what each Party ought to contribute to the global effort, or to enforce the achievement of the Parties' targets**. (source: Tsy advice 2021).

Commented [MC[4R3]: Because there is a lack of a clearly identified party to whom obligations are owed, it is also considered that a constructive liability also does not exist (in addition to there not being a present obligation, as noted in the comment above).

Commented [MC[5]: It would be more accurate to say that **how much offshore mitigation** might be required to achieve New Zealand's NDCs and **what it might cost** remains highly uncertain.

2. Treasury will provide LINZ with any information which has been proactively released in relation to Treasury's advice on NDC liability (Lachy will be LINZ's main point of contact);
3. LINZ will circulate the carbon claims content of our consultation letter for review.