# Council Policy

# Emissions Trading Scheme

**Relevant Legislation**

Local Government Act 2002
Climate Response Act 2002 and amendments

**Introduction**
The Kyoto Protocol which New Zealand ratified in 2002 is a 'cap-and-trade' system where each country is allocated a number of Assigned Amount Units (AAUs) at the start of each commitment period. New Zealand's initial assigned amount was 309,564,733 AAUs being five times our emissions in 1990. If we emit more than this amount of tCO2-e, we will need to buy emission units from another country to make up the difference.

The NZ Emissions Trading Scheme helps us meet New Zealand's Kyoto target by:

- Putting a price on emitting greenhouse gases to encourage people to reduce emissions, which reduces the amount of emission units that New Zealand needs to surrender.

- Allocating New Zealand Units (NZU's) to foresters who own or plant trees, which remove CO2 emissions from the atmosphere.

The above two items form the basis of the Councils obligations under the NZETS. This Policy provides the framework for the accounting and management of these obligations. The Policy does not address mitigation of climate change or adaption to climate change directly. The Policy does not cover district inputs e.g. influence on land use change.

The New Zealand Emission Trading Scheme (NZETS) puts a cost on emissions of greenhouse gases (GHGs), often referred to as the carbon price. It does this by requiring certain entities, including the Council in respect of its forestry holdings, to report their deforestation each year then surrender to Government emission units to cover the carbon liability.

A key challenge is to manage the considerable uncertainty that surrounds climate change policy, including the future carbon price in New Zealand.

## 1. Policy Objective

1.1. To provide a framework to aid decision-making where the future cost of greenhouse gas emissions (sometimes referred to as the carbon price) is, or may be, a material consideration;

1.2. To ensure the Council meets its obligations and is fiscally prudent when managing carbon-related assets and liabilities; and

1.3. To identify opportunities to minimise liabilities and/or maximise assets created under the NZETS, where this is economically efficient and fiscally prudent.

## 2. Policy Principles

2.1. Meeting obligations – the Council will meet all its obligations required under the NZETS and related legislation and regulations.

2.2. Conservative approach – the Council will adopt a conservative approach to managing NZUs. The Council does not have a major strategic exposure to carbon pricing nor does it have core competencies in this area. Exposing a large amount of the Council's balance sheet to carbon pricing is therefore not justified. For example, the Council does not intend to become a major carbon trader nor a speculator on future prices on carbon. Nor will the Council take aggressively short or long positions on emissions units relative to its liabilities. Assumptions about future carbon prices will also be conservative.

2.3. Decision-makers will need to consider their decisions under scenarios where carbon prices become significantly higher and fall to zero. The zero carbon price scenario is particularly important, since political decisions could create such an environment with little warning. High carbon prices on the other hand are likely to be telegraphed in advance allowing time for the Council to adapt. Ideally decisions will have a rationale and net benefit (albeit a diminished benefit) regardless of future carbon pricing, including in a scenario where greenhouse gas emissions are not priced at all.

2.4. All decisions on acquiring or divesting NZUs will need to consider possible implications of the NZETS and future carbon prices.

2.5. Acquire least-cost units – in cases where the Council is required to but cannot acquire enough units locally or where local units are above market rates, the Council will acquire units at least cost.

## 3. Monitoring and Evaluating a Changing Policy and Market Environment

Financial information, in particular information on the cost of emissions units, will be monitored and evaluated.

The information and intelligence gathered will be used to inform decision-making and annual planning processes.

## 4. Framework for assessing cost and benefits of decisions

The degree of uncertainty over carbon prices challenges typical models and assumptions for making investment decisions where a future cost on carbon is a significant consideration.

This section provides standardised assumptions and other guidance when undertaking cost benefit analysis for carbon-related investment decisions.

### 4.1. *Discount rates*

Where future cash flows (either incomes or costs) depend on an on-going carbon price, the uncertainty associated with that future price should be reflected in the discount rate used.

Higher discount rates reduce the net present value of future incomes or costs. As a general rule the more uncertain a cost or benefit is, the higher that cost or benefit should be discounted.

Given the uncertainty over the future of carbon pricing, a premium will be applied to Council's normal discount rates when assessing cash flows dependent on a future price of carbon.

### 4.2. *Carbon prices assumptions*

The New Zealand Treasury publishes regular updates of the carbon price used to calculate New Zealand's position under the Kyoto Protocol as reported in the financial statements of the Government of New Zealand. Where Treasury does not publish this information, Council officers, using the best market information available, will develop carbon price estimates to be used in financial analysis.

## 5. Meeting obligations - emission returns and responsibilities

For pre-1990 deforestation activities, reporting must be carried out annually between 1 January and 31 March in the year following the year to which the emissions relate (reporting is carried out based on calendar years). Any obligations to surrender emission units must be met by 31 May in the year following the year to which the emissions return relates.

To ensure the Council meets its obligations, specific legal requirements will be identified. Some key tasks to be assigned include:

- Completing accurate deforestation returns.
- Notifying relevant Government agencies when specified activities or transactions occur as required under any relevant legislation.
- Keeping records.
- Surrendering emission units.

## 6. Pre-1990 Forest Deforestation

Under the NZETS deforestation of pre-1990 exotic forests creates liabilities. The Council does not anticipate any significant deforestation activities involving any of its forests that can not be covered by current NZU reserves. Where pre-1990 exotic forests are harvested, it is expected that the affected areas will either be replanted or regenerated into a different forest type, such as an indigenous forest. In either case no emission liabilities are created under the NZETS.

Should deforestation of pre-1990 exotic forests be proposed, the deforestation costs created by such proposals will be considered by the Council as either:

- A new initiative under the Annual Plan process; or
- Included in the costs of a project to which the proposed deforestation relates.

For example, if an infrastructure project required deforestation of an area of pre 1990 exotic forest, the costs of any deforestation liabilities will be included in the costs of the project.

**7. Revenue from Sales and Cost Recovery**

Revenues generated from any sale of emission units will be treated as revenue received by the Council and will be ring-fenced for use with the associated LTP activity that is linked to the forest that generated the NZU entitlement.

**8. Purchasing and Trading Strategies for Emission Units**

The Council will also have the opportunity to sell units from its relevant forestry activities.

The Council will seek expert advice as required, on the acquisition and sale of emission units, including addressing the following key issues:

- ensuring that any acquired emission units meet the requirements of the NZETS,
- managing the Council's overall net position with respect to emission unit assets and liabilities,
- minimising costs to Council while ensuring appropriate risk management,
- taking into account taxation issues, as appropriate.

The Council may also consider options to acquire emission units by way of investing in post-1989 forest activities in addition to land under its direct control. Consideration of such options will require careful evaluation for risk and value for money.

The Council will give priority to purchasing emission units from local sources but not at a price that is materially above the market rates for units.

**9. Review of Policy**

There should be a detailed review of this policy in 2015 once the outcome on the Government decision over the retention of the $25 price cap for NZUs is known.

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