

New Zealand Emissions Trading Scheme (NZ ETS) – Further update on Climate Change (Forestry) Regulations 2022

With several important changes to the NZ ETS due to come into effect on 1 January 2023, the Government has sought to provide further clarification as to how these changes might operate in practice.

As previously highlighted by Anderson Lloyd in our article [Carbon Forests](#), the Climate Change (Forestry) Regulations 2022 (**Regulations**) are set to replace the current Climate Change (Forestry Sector) Regulations 2008 from 1 January 2023. The Regulations have now been approved and bring about changes including:

- the introduction of a new activity in the NZ ETS for permanent forests known as "permanent post-1989 forests";
- a new carbon accounting approach, called 'averaging accounting';
- a new exemption from carbon liabilities for forests partly or fully cleared because of a temporary adverse event; and
- general technical improvements to make the NZ ETS easier to participate in and manage.

This update will provide further information about all of the above changes and how they may function in practice.

We have already covered the topics of 'averaging accounting' and permanent forests in the article mentioned above. To briefly summarise:

- Permanent post-1989 forests are a new category of forest set to be introduced into the NZ ETS. They are post-1989 forests that may not be clear-felled

for at least 50 years after they are registered in the NZ ETS.

- Averaging accounting is the new carbon accounting method to be used in the NZ ETS from 1 January 2023. This method allows forests to earn New Zealand Units (**NZUs**) by taking the average of the long-term amount of carbon that a particular forest is expected to store over multiple rotations.

From 1 January 2023 all forests newly registered in the NZ ETS will be required to utilise either averaging accounting or enter into the new permanent post-1989 forest category.

Permanent post-1989 forests

Entering into the new category

The approved Regulations include additional details as to how the category will operate, as summarised below:

- If a forest owner moves land directly from a Permanent Forest Sink Initiative (**PFSI**) covenant to the permanent forestry category, the initial 50-year registration period does not start from zero.¹ Instead, the 50-year period (in which the forest may not be clear-felled) will commence from the date the initial forest sink covenant was first registered.
- If a forest owner with PFSI land chooses to move their land into the post-1989 forest category (which will result in the forest being subject to averaging accounting) they are still able to move the land into permanent forestry at a later date. As long as the forest has never been clear-felled, the 50-year registration period will count from when the initial PFSI covenant was first registered.
- Given how averaging accounting functions (discussed in greater detail below), a forest owner entering their land into the post-1989 forest

¹ The PFSI will close from 1 January 2024. For more information on the PFSI see our [previous article](#) on Carbon Forests.

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category from the PFSI may already have earned more NZUs for their forest than it would be entitled to at its average age. In such circumstances, a forest owner will have to surrender NZUs to the government.

- Small areas of permanent forest may be removed from the NZ ETS before the 50-year period ends. This can only be done however with approval from the Minister for Climate Change. The Minister must be satisfied certain conditions are met to allow for the removal and a forest owner will need to pay NZUs to the government for the removed area.

Clear-felling permanent forests

Guidance as to what to do after a forest is clear-felled has also been provided by the government following the approval of the Regulations. If a forest owner clear-fells a permanent forest they:

- must pay NZUs for the emissions from the area that was clear-felled; and
- may face a penalty based on the value of the clear-felled forest.

If a person has notified the Environmental Protection Authority (**EPA**) of clear-felling and a final forestry emissions return has been submitted that includes clear-felled land, the EPA must apply to the court for a pecuniary penalty against the person that has clear-felled permanent forestry.

This additional penalty is payable based upon the determined \$ / tonne figure for the forest type that was within the clear-felled area in that particular region as set out in the Regulations. These values range from \$5 / tonne for Exotic hardwoods anywhere in New Zealand to \$15 / tonne for Douglas fir and indigenous forest anywhere in New Zealand.

These NZU penalties may not apply however if it can be shown to the EPA that a "defence" applies, including where:

- the clearing or deforestation was beyond the forest owner's control;
- the forest owner could not reasonably foresee the clear-felling; and
- the forest owner could not have reasonably taken steps to prevent the clearing or deforestation.

On-going considerations

An important and on-going consideration that the government is debating currently is the matter of fast-growing exotic forests and their potential exclusion from the permanent post-1989 category. At the time of writing, Cabinet has made a decision (which is not yet publicly known) on this matter and has agreed to redesign the NZ ETS permanent forest category. In the interim, the existing NZ ETS permanent forest category will open to all forests (including exotic forests) on 1 January 2023 while the category is redesigned.

Averaging accounting and first rotation forests

There are certain situations where the new carbon accounting method of averaging accounting may not automatically apply. If a forest is registered in the NZ ETS between 1 January 2019 and 31 December 2022, the owner has a choice between moving to 'averaging accounting' or continuing with the 'stock change' method. If a forest owner elects to move to averaging accounting, the owner will need to complete a special emissions return.

As earning NZUs under averaging accounting is based upon which rotation (or harvest cycle) a forest is on, understanding the general workings of the process is critical.

Under averaging accounting, a first rotation forest will earn NZUs until it reaches the average age for that forest type (and is subsequently considered to be long-term carbon stock).

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First-rotation forests are forests that have not been harvested before. Any forest on land that has been left unstocked (where land contained forest on 1 January 2021 or was harvested before 1 January 2021 and is then such land is deforested) for a period of at least 15 years before replanting will also be considered a first rotation forest.

Participants cannot earn NZUs in the NZ ETS after the forest reaches its relevant average age. This means that participants will not earn NZUs in respect of:

- registered first rotation forests that are past the relevant average age; or
- registered second or later rotation forests.

Under the Regulations, the average age of each of the five main forest types has been specified:

- Radiata pine: 16 years;
- Douglas-fir: 26 years;
- Exotic softwoods: 22 years;
- Exotic hardwoods: 12 years; and
- Native (indigenous) forest: 23 years.

The Regulations also prescribe the methodology for calculating NZUs under averaging accounting. There will be three measures of carbon stock for land in the carbon accounting area using an averaging accounting approach, as follows:

- the determined carbon stock (DCS);
- the nominal average carbon stock (NACS); and
- the typical average carbon stock (TACS).

This methodology will be more straightforward than what is contained currently in the Climate Change Response Act 2002 (**CCRA**), for instance the updated process for NACS will only recognise three age bands for each particular type of forest and assign only three

corresponding levels of settled long term average carbon stock.

Temporary Adverse Events Exemption

Under the Temporary Adverse Events Exemption (effective from 1 January 2023), where a forest is affected by an event such as fire, windthrow or disease rather than having to surrender NZUs to cover any emissions stemming from the event, participants with post-1989 forests can effectively 'pause' their participation in the scheme by making an application under section 193A of the CCRA.

The Regulations define "adverse events" as including:

- natural events such as windthrow, snow, flood, landslide or slip, drought, infection by disease, damage by pests (such as insects or animals), and naturally caused fire; and
- accidental events such as accidental fires (including a controlled burn that becomes uncontrolled), application of herbicide (including herbicide blown from other land), and browsing by animals.

Forests will be considered "affected land" under the CCRA if:

- the land is a carbon accounting area;
- the land is affected by an adverse event pursuant any associated regulations;
- the relevant adverse event results in each hectare of land ceasing to have tree crown coverage of more than 30%;
- the adverse event persists for at least the minimum period of time prescribed under the Regulations; and
- the carbon stock loss is equal to or greater than the minimum prescribed amount under the associated regulations.

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An application will not be accepted unless the EPA is satisfied that the participant is likely to achieve re-establishment of the relevant forest and carbon recovery in accordance with the CCRA within the prescribed time frames.

During the re-establishment period, the forest will not earn any more NZUs until it achieves the same level of carbon stock as it was prior to the occurrence of the temporary adverse event. The exemption extends to any clearing required as a result of the event.

If a temporary adverse event occurs to a first rotation forest, then the land, on re-establishment, is to be treated as continuing to have a first rotation forest.

Offsetting

This update to the NZ ETS will essentially allow some participants with post-1989 forests under averaging accounting the ability to offset their deforestation liability by planting forests elsewhere in the country.

Where a participant in the NZ ETS converts a post-1989 forest to another use, that participant will not have to surrender NZUs they have earned in relation to the post-1989 forest provided the participant can plant and actively establish an offsetting forest in another location that has the same carbon storage.

This update will also aim to improve the offsetting process for pre-1990 forests. The update seeks to benefit those owners who hold large areas of pre-1990 forest land that could be suited to another land use but would suffer significant deforestation / harvesting liabilities as a result of such a change. The improvements contained in the update are intended to provide more flexibility around how to achieve an offset forest, the ability to adjust an offsetting application after it has been approved and limit enforcement action to the specific areas of forest land that are not offset (as opposed to liability for all deforestation from the original application / revocation of the entire application).

Specifically, the update shall:

- define 'usual rotation periods' to determine carbon equivalence;
- provide a time extension for offset establishment;
- allow recently planted forests to be used; and
- allow excess land from previous applications to be re-used.

Want to know more?

If you have any questions about the upcoming Climate Change (Forestry Sector) Regulations 2022, or you wish to explore forestry investment options in general or you require assistance with navigating the ETS, please contact our specialist [Carbon Trading, Emissions Trading Scheme and Climate Change team](#).