



Australian Government

Department of Climate Change

EMISSIONS TRADING STAKEHOLDER CONSULTATION

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AGENDA PAPER: COVERAGE OF FORESTRY

This paper does not necessarily represent the views of the Australian Government or any Government Minister. It is a working paper prepared by the Emissions Trading Division of the Department of Climate Change. The views contained in this paper are preliminary only and are subject to change. The aim is to promote discussion and submissions at not sought at this time.

1. Introduction

Forestry and agriculture have often been considered together in the context of emissions trading because of the interchangeability and interactions between these two broad land use options. However, forestry involves a number of features that are different from agriculture, including having more established measurement approaches.

2. Coverage

Forestry differs from other land-based sectors because it tends to be a net carbon sink rather than a net source of emissions.

Forest carbon sequestration and emissions are relatively well understood, and reliable and cost effective methods of estimating forest carbon are readily available. Firms are currently estimating forest sequestration in order to participate in various voluntary offsets schemes and government programmes such as the Australian Government's Greenhouse Friendly™ programme and the New South Wales and Australian Capital Territory's Greenhouse Gas Reduction Scheme using direct sampling methods and via the National Carbon Accounting System.

Growing forests are likely to sequester more carbon than they emit, so including them in the scheme is likely to benefit forest owners.

This characteristic of forestry suggests that while there are many small entities (including many farm businesses) involved in this activity, the practical issues relating to coverage are different to those for agriculture.

A range of other issues have been raised. For example, there may be concern that distortions in land use will arise if some land-use activities are included in the scheme before others. A shift toward less emissions intensive activities, including farm forestry,

would reflect an efficient allocation of resources taking into account the carbon price, assuming an appropriate framework for natural resource management.

Questions for stakeholders:

- *Stakeholders are invited to comment on the range of issues relating to inclusion of forestry in the scheme.*

3. Coverage options

Decisions will be required as to the mode of coverage and the definitions of eligible forests and net sequestration. For example, coverage could be limited to only eligible sequestration from Kyoto forests or different definitions adopted. The paper, *International Accounting Rules: Implications for Scheme Design*, considers the relationship between scheme coverage and the international accounting rules.

There are two broad coverage options:

- mandatory coverage; or
- voluntary ‘opt in’.

Unlike other sectors of the economy, including agriculture, a voluntary approach is possible for forestry because forests are likely to sequester more carbon than they emit. Forest owners therefore have an incentive to voluntarily include their forests in the scheme.

Mandatory coverage

This option would bring a large number of entities into the scheme, depending on the threshold for inclusion in the scheme.

Many of these forests, particularly harvest plantations would incur compliance costs despite having few, if any, net emissions and little to gain from inclusion because increases in sequestration in their forests would be roughly equivalent to their harvest emissions. While owners of harvest plantations could potentially benefit from the scheme by increasing average sequestration over time, the magnitude of these benefits would depend on the future carbon price. If the cost of future liabilities is higher than the value of sequestration benefits obtained in the growth phase of the forest then owners of harvest plantations could, in some limited circumstances, incur a net liability¹.

¹ The net present value of carbon will be the same over time if the nominal price of carbon increases at the rate of interest. However, future carbon prices could increase more rapidly than this, in which case the future carbon price would be higher in real, net present value terms.

Voluntary 'opt in'

A voluntary approach would allow forest owners to determine for themselves whether participation in the scheme would be of benefit.

Benefits of scheme participation will be greatest where land-owners intend to maintain forest or conservation plantings as there would be no emissions from these². As noted above, the benefits for harvest plantations will depend on whether forest managers have flexibility with regards to harvesting schedules, future log prices and the future carbon prices.

Questions for stakeholders:

- *Stakeholders are invited to comment on the merits of these options.*

4. Detailed design issues

Coverage of forestry will also require decisions regarding reporting intervals, and the baseline and period over which net sequestration would be calculated. These rules will affect compliance costs and impact on the ability of forest owners to manage periodic harvest liabilities or emissions from events such as bushfires.

Inclusion of additional forests in the scheme would affect the number of units available (and hence the unit price); and so timeframes for including additional forests in the scheme, and notifying the market of these additions, would also be required.

New Zealand has decided to include eligible Kyoto forests in its emissions trading scheme from 2008 on a voluntary basis and has developed detailed rules regarding scheme participation. Aspects of their approach to coverage may be instructive.

New Zealand approach

The New Zealand scheme allows owners of eligible Kyoto forests to participate in the scheme to receive permits for the increased carbon stored in their forests during the Kyoto commitment period (2008-2012). Forest owners are also required to hold permits to cover net emissions, if any, from these forests, including as a result of harvesting, clearing or fire. As a transitional measure, New Zealand has placed limits on emissions liabilities so that these can not exceed the number of permits received for sequestration.

The scheme allows entities other than the land owner to participate in the scheme, for example lease holders or owners of forestry or carbon property rights. Scheme liabilities are recorded on the title and once land is in the scheme, exit is possible only after acquittal of any existing or potential harvest liabilities. In effect, this means that land owners have ultimate liability for forest emissions.

Forest owners have 18 months to decide whether or not they wish to participate in the scheme. If they choose not to opt in to the scheme during this period, they will be given a second opportunity to opt into the scheme at the start of the next international agreement.

² Emissions could occur if forests were subject to bushfire however these emissions would net out over time if the forests were allowed to regenerate.

Scheme participants are required to meet the costs of participating in the scheme including the costs of measuring, verifying and reporting removals/emissions. In effect, these costs create a threshold for participation in the scheme.

The design of the New Zealand scheme is focused on ensuring New Zealand meets its Kyoto target. For this reason, participating land holders have to report (and buy/receive permits) by the end of the commitment period, but can choose to report more regularly.

Questions for stakeholders:

- Stakeholders are invited to comment on the pros and cons of New Zealand's approach; and on whether there are other options or approaches that should be considered.