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29 April 2010

Hon John Key
Prime Minister
Parliament Buildings
WELLINGTON

Open Letter to the Prime Minister

As you know, the ACT Party considers the next phase of the emissions trading scheme, due to come into effect on 1 July 2010, should be suspended.

The main reason for our position has been that:

- We agreed with your previously declared position that "...while we must play our part in the fight against climate change, we shouldn't be the world leader, because that will come at the expense of our economy ... I see no sense in New Zealand exporting emissions - and jobs - to another part of the world" (Source: John Key campaign blog, October 23, 2008). The reasoning behind your statement was correct: it makes no sense to burden industries and households with extra costs at a time when they are facing other cost increases such as rises in electricity prices and a possible increase in GST. You correctly observed that this would lead to us "exporting jobs" to other countries.
- Although the impact of the scheme has been modified, it would still be significant. The Reserve Bank estimates it would add 0.4 percent to the CPI, which would risk increasing wage pressures and the pressure on monetary policy at a time when the export sector and the economy remain weak. The crucial source of new jobs and productivity gains is investment, and investment decisions are made on the basis of the outlook over many years ahead, so even the modified ETS will have significantly negative impacts on our economy, particularly if other countries, our major trading partners in particular, do not proceed.
- The countries that are the major sources of global emissions are not involved. We now know that the Rudd Government has decided not to proceed. Australia has postponed its planned ETS until at least 2013 for reasons which include the lack of action elsewhere in the world. It may have been tolerable, if inadvisable, to proceed with our scheme if an Australian scheme was in prospect shortly after this year's election but this is no longer the case. To proceed when Australia has stopped, is an extraordinarily rash and foolish decision, which will cost jobs and lower the incomes of New Zealanders.

- We are aware that interests in the electricity sector and others involved with carbon trading want the scheme to go ahead, but they have a very strong vested interest – it is not a national benefit consideration. It is the Government's role to take a national interest perspective.

The Minister for Climate Change has put forward an argument for proceeding with the ETS that is based on respect for the property rights of foresters who have planted trees in the expectation of benefiting from carbon credits.

This is a remarkably weak, and indeed a very misleading argument.

No party is more committed to respect for property rights than the ACT Party, which is why we have long objected to the treatment of pre-1990 forests. Under the ETS, owners of such forests are retrospectively penalised if they convert them to other land uses.

In the case of post-1990 forests, the first point to make is that if the ETS is suspended, forest owners would remain perfectly free to sell credits to any parties interested in buying them, eg parties subject to the European Union ETS.

The second point to note is that new plantings in recent years have fallen substantially. Most of the increased planting occurred in the 1990-2000 period. Few foresters could credibly claim their plans have been disrupted if the ETS were suspended. The Government would be able to argue that such claims are legitimate only from 2008 when the ETS legislation was passed. Even if the government were to accept that foresters had legitimate expectations of the creation of carbon credits via an ETS from some earlier date (say 31 October 2002, being the date of policy announcements used by the Government to justify differential regulation of forest land owners) the total number of hectares planted since that time is not large. And given the uncertainty of any future government policy, the potential for a future ETS could only have played a small part in any such investment decision.

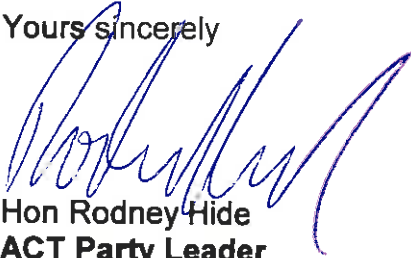
In principle, the proper course of action if property rights are significantly altered is to consider compensation. The ACT Party accepts the Government should do so if the scheme is suspended and affected foresters can justify a claim of losses arising. However, the following additional points are relevant:

- (i) Many will not do so. A temporary suspension would have limited consequences for forests planted on a 30 year plus rotation.
- (ii) If forest owners claimed and accepted compensation for the loss of sales of carbon from 2002-2009 they would also lose the opportunity value of being able to convert their land to other uses should that become attractive in the future. Moreover, they would have to gamble on the compensation (of \$25/tonne) being more attractive to them than the possibility of a much higher price (say, \$100/tonne) down the track if the ETS is later implemented and world carbon prices rise.
- (iii) I suspect that much of the limited amount of recent new planting was not motivated by the prospective ETS but by government afforestation programmes. Logically, only the marginal amount due to the ETS should be recognised in compensation claims for such forest.
- (iv) Foresters will benefit from reduced input costs for electricity and fuel if the ETS is suspended. This element is particularly important for integrated forestry and wood processing firms. This benefit should also be offset against compensation claims.

In short, the ACT Party would expect some criticism from foresters arising from suspension of the ETS and considers that claims for compensation should be considered in good faith. However, for the reasons given above we think the Crown would not be in an exposed negotiating position and that any legitimate claims would be modest. Our guess is that they would be unlikely to exceed \$10-20 million. This would be a small price to pay relative to the compensation agreed with Maori landowners last year to support the ETS and relative to the large costs to firms and households that would be avoided for the period of the scheme's suspension.

I hope you will consider this approach favourably and look forward to hearing from you.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Rodney Hide', written over the typed name.

Hon Rodney Hide
ACT Party Leader