

Report to:	Council Public Excluded
Date:	31 August 2022
Subject:	Marlborough Regional Forestry Delegation
Prepared by:	Sheryl Poulsen - Finance Manager
Input sought from:	M Fletcher - Chief Financial Officer, Marlborough District Council
Authorised by:	Murray Dickson - Senior Manager Corporate Services

1. SUMMARY

The Council owns 11.5% of the Marlborough Regional Forestry joint operation (MRF), with the Marlborough District Council (MDC) owning the 88.5% balance share.

MRF has no delegation to purchase forestry blocks as they come to market – this decision rests with the Councils themselves as per legislation. Typically, these blocks have relatively short closing dates that do not align with the meeting cycles of both Councils.

This report seeks the Council's approval to establish a delegation for MRF to enter into conditional agreements for the purchase of additional forestry blocks prior to Council confirming any purchase. (This delegation for conditional agreements will still require the Council Chief Executive to execute the conditional agreements).

This report mirrors a similar report being presented to MDC. We are proposing to have an MRF representative available to speak to the report if required.

This report was also presented to the Finance Audit & Risk Committee on 30 August for endorsement to Council.

This report is in public excluded as it contains sensitive commercial information, which would be valuable to prospective sellers and competing purchasers.

Attachment:

- i. MRF – Investment Guidelines

2. RECOMMENDATION

It is recommended that the Council:

- a) Notes the endorsement (if any) from the Finance Audit & Risk Committee;
- b) Receives this report; and
- c) Agrees to establishing a delegation for Marlborough Regional Forestry (MRF) to authorise Council's Chief Executive to enter into conditional agreements for the purchase of additional forestry blocks prior to Council confirming any purchase, subject to:
 - i. the criteria contained in paragraph 8 regarding size and locality being met and sound justification being provided for any proposed purchase being outside the first three categories in the order of preference also contained in paragraph 8;
 - ii. the purchase price being within 5% of valuation; and
 - iii. any purchase being funded by the realisation of assets held by MRF.
- d) Delegates the Chief Executive Officer to determine the release of this public excluded report.

3. BACKGROUND

Currently MRF has no delegated authority to purchase additional forestry blocks as they come to market, because it is subject to clause 32(1) of Schedule 7 of the Local Government Act 2002, which states:

*“a local authority may delegate to a committee or other subordinate decision-making body ... any of its responsibilities, duties or, powers **except** -
(c) the power to borrow money, or **purchase or dispose of assets** other than in accordance with the Long Term Plan (LTP).*

While the LTP does mention MRF, it does not contain any reference to purchasing additional forestry blocks.

Also worth noting is Clause 32(2) of Schedule 7 which states that:

*“**Nothing in this clause restricts the power of a local authority to delegate** to a committee or other subordinate decision-making body ... the **power to do anything precedent** to the exercise by the Local Authority of any power specified in sub clause (1).”*

“Anything precedent” described in this clause includes evaluating the potential land investment, making an offer, and authorising the Council’s Chief Executive to enter into a Sale and Purchase Agreement but with a condition that the purchase must be subject to Council approval before it takes effect. This is similar to other conditions commonly found in property Sale and Purchase Agreements such as, subject to the purchaser obtaining, (for example):

- finance;
- a valuation;
- a LIM report; and/or
- a building inspection report.

Typically, if these clauses are included in Sale and Purchase Agreements they must be met to the satisfaction of the purchaser. Prospective sellers should therefore have no issues accepting such a condition.

No requirement to contribute to purchase cost

MRF would sell the required number of ETS units (carbon credits) for settlement, so there would be no call for cash from either of the two district councils to complete the proposed land purchase.

At 30 June 2022, MRF holds just under 180,000 NZEU (carbon credits) which have no surrender liability provided all cleared land is replanted. The market value of each unit is currently \$85. It is proposed to sell units to fund the purchase, which will also be subject to final approval by Council.

Requirement for independent valuation

Every land purchase made by Council should be supported by a valuation, and the same applies to MRF. However, as with any sale and purchase agreement, the final amount will be determined by negotiation, so a 5% margin has been incorporated into the recommendation.

The process to complete a purchase

Once delegation has been granted to MRF, from both the Kaikōura and Marlborough District Council’s, the process going forward will be for MRF to:

- 1 evaluate any forest block that emerges to market against the approved criteria, then
- 2 negotiate a price to within 5% of valuation, and
- 3 ensure there are adequate NZEU to cover the purchase price, then

- 4 authorise the Chief Executives of both Councils to enter into a sale and purchase agreement subject to approval from both Councils before it takes effect, then
- 5 it is likely that an extraordinary meeting would need to be called (separately for both Kaikōura and Marlborough District Councils) to formally approve the purchase. These meetings may be required at short notice and with the public excluded.

4. FINANCIAL IMPLICATIONS AND RISKS

The purpose of the guidelines is to ensure that land purchases for forestry are prioritized to fill the current harvesting void for MRF, that would otherwise be experienced every 30 years or so. MRF has sufficient ETS units to complete the land purchase with readily available cash. Neither of the joint venture councils would need to contribute directly to the purchase cost.

Community Implications

There are no community implications from this proposal.

Risk Management

MRF is well-managed by M & R Forestland Ltd, including risk management, however normal risks associated with land purchases and forestry operations (including net returns) remain. These risks are considered minimal.

Health and Safety

There are no health and safety concerns from this proposal.

5. COMMUNITY VIEWS

Groups and Organisations

No views of groups or organisations have been sought in relation to this proposal.

Wider Community

No views have been sought from the wider community.

6. RELEVANT LEGISLATION

Policy

This is not a matter of significance in terms of the Council's Significance and Engagement Policy.

Legislation

This proposal is not contradictory to any legislation. The decision to provide for MRF to undertake initial assessment, negotiation, and offer of purchase but with only a partial delegation, to ensure compliance with Clause 32 of Schedule 7 of the Local Act (2002).

Delegations

The MRF Committee has no delegated authority to purchase or dispose of assets. Approval is required from both the Kaikōura and Marlborough District Council's for all land purchases.

7. COMMUNITY OUTCOMES SUPPORTED

The work is in support of the following community outcomes.



Future
We work with our community and our partners to create a better place for future generations



Development
We promote and support the development of our economy



Marlborough Regional Forestry – Land Purchase

The purpose of this brief is to provide a guideline for the most suitable type of property to purchase in order for Marlborough Regional Forestry (MRF) to grow their Estate.

Area

In order to achieve economies of scale, recommendations of the most suitable size of the land are as follows:

1. Minimum of 100ha beyond 10km of estate

A 100ha block will provide one years' worth of continuous harvesting and the size is large enough to ensure efficiencies with day-to-day tree crop and estate management.

2. 50ha within 10km of current estate

A 50ha block near the current estate will provide six months of continuous harvest and due to the proximity of the current estate, day to day tree crop and estate management can still be managed efficiently.

Forest Locations

To simplify the process of selecting a suitable forest block the following locations will not be considered

1. Outside the Marlborough District Council boundary

To ensure no outlier forests, land within the Marlborough District boundary should only be considered.

2. No land with the Marine Coastal Environment (the Sounds) will be considered

While M&R have experience in management of forests within the coastal environment, we also understand the ongoing difficulties of operating within the Sounds and we perceive potential conflict of interest with MDC.

Age class priorities

The MRF estate has been harvested at the optimal age, however this has left a six year harvest gap. Additional land or forest purchases will aid in smoothing the harvest to a perpetually sustainable model, the benefit of this has wider ramifications than just consistent harvesting, it will allow MRF to sustain a work force across establishment and silviculture operations, ensuring skilled labour is retained.

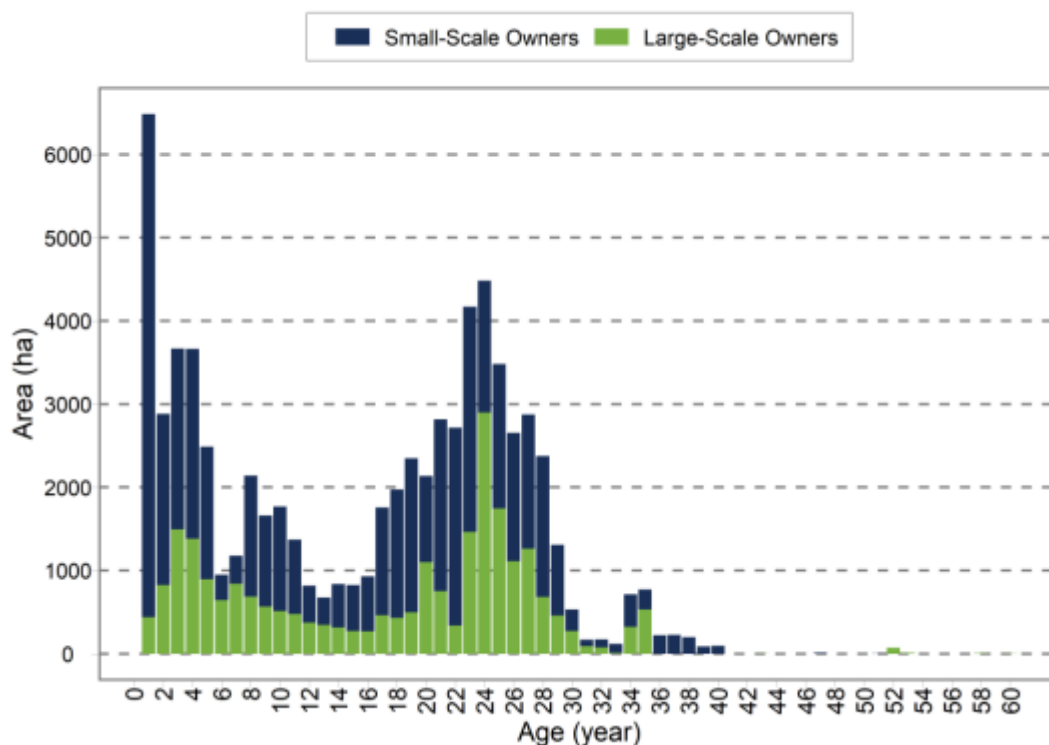
Typically, trees that are one-two years old can be valued at the cost of establishment, with this increasing each year. Generally, forests or land with scale that has been entering the market over the last few years has been bare, unplanted or with one – two-year-old trees.

The graph (2021) below shows the age class distribution for forests in Marlborough, M&R are familiar with the structure of forests that are due for harvest. The small-scale owners are either made up of

partnerships or held by individuals and are around 100 -200 ha, or they are larger forest areas that have been subdivided into smaller lots and held by individuals, generally around 20 - 40ha.

M&R's experience is that at the end of partnerships or depending on the age of the individual post-harvest, these are the types of properties which will be offered to the market for sale. As such M&R anticipate younger age classes or cutover coming to the market.

Marlborough Modelled Age-class Distribution for All Species



As a guide M&R recommends the purchase of;

1. Forests aged 1-2 years old

There is no premium attributed to the value of the tree crop, it is second rotation and therefore roads and skids have been built. Recently established forests do pose some risk which is why a premium is not built into the valuation, typically forests established by reputable Forest Management companies have records of quality control, weed control and survival assessments. These can be assessed in the due diligence phase. Other forests may require physical assessments to determine the quality and level of stocking.

2. Cutover land

This is land that has been harvested and is ready to be replanted. The value of the property is in the land, it has roads and skids, but establishing the forest will need to be completed by MRF.

3. Bare land

This is farmland that is suitable for establishing in a forest. Typically, these are low fertility, poor grazing sites. These will be the first rotation and do not have forest infrastructure in place, depending on the farm tracks some engineering may be needed to assist with establishment.



4. Forests age 3-6.

The value for trees starts to increase over time and these forests begin to command a premium for the tree crop. At this age the crop is easily seen and any establishment issues should have been resolved or identified.

5. Age classes 7-15

These forests will either be pre or post thinned stands and command a premium for the crop, depending on the age class and the tending they have received, they may require immediate cash flow for silviculture operations.

6. Age 15 plus

It is less common to see older forests for sale within the region, while these are worth considering, they require due diligence as to their value, particularly those nearing harvest as there is typically competition from log traders in this market.

Carbon

Land valuations consider if a property is eligible for carbon and the land is priced accordingly. Typically, if cutover land is eligible, it will already be entered into the ETS scheme. However, not all bare land meets the criteria and therefore due diligence to determine if it is eligible should be undertaken.

New rules are coming into effect and will apply to all post-89 forests registered from 1 Jan 2023. Forest owners will no longer need to surrender NZUs when they harvest; instead, they receive NZUs up to an average harvest age which for *Pinus radiata* is 16-year-old. The condition is that forests need to be harvested close to target age and replanted. The benefit of this is a reduction in cost and complexity of the ETS for forest owners.