NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

Natural Resources Defence Council * Defenders of Wildlife * Alberta Wilderness Association

Northwest Ecosystem Alliance * West Coast Environmental Law Association

August 8, 2003

Comments

on

U.S. Department of Commerce Softwood Lumber Policy Bulletin

(C 122 839) (June 24, 2003)

The Department of Commerce (DOC) issued a policy bulletin entitled *"Proposed Policies Regarding the Conduct of Changed Circumstance Reviews of the Countervailing Duty Order on Softwood Lumber from Canada*" (C 122 839) on June 24, 2003 in the Federal Register for comment (Federal Register, Vol. 68, No. 121, page 37456). We are pleased to have the opportunity to provide comments on the policy reforms we believe are necessary to address the distortions in the current Canadian stumpage system that subsidize Canadian timber companies. We believe that these comments will prove relevant for the further development of the softwood lumber policy bulletin.

The final policy bulletin is meant to set standards for market-based timber sales system that charges adequate remuneration and against which Canadian provinces can be measured in a changed circumstances review. If the standards were met, DOC would then determine that the provincial system does not provide a countervailable subsidy and would revoke the countervailing duty order with respect to lumber produced in that province.

There are several weaknesses in the policy bulletin that will prevent it from achieving its goals:

- The policy bulletin misses key policies and practices that inhibit market response, and proposes elimination of policies that are part of the solution, not part of the problem.

- The policy bulletin does not sufficiently stress the need for a substantial majority of wood to flow through markets. For example, it could be read as incorrectly implying that a single regional market in a province would provide enough of a market-based structure to allow an adequate stumpage level to be determined.

- The policy bulletin neglects to provide adequate safeguards against a province changing other laws (such as environmental laws) in order to offset the higher stumpage rate and minimize the burden on forestry companies.

In addition to the comments submitted here, we support the comments submitted by the BC Coalition for Sustainable Forest Solutions and the Indigenous Network on Economies and Trade.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.A

POLICIES AND PRACTICES THAT INHIBIT MARKET RESPONSE

Summary of Comment: The policy bulletin should require that artificially low minimum stumpage rates be raised.

Comment:

The policy bulletin should, but does not, address the issue of minimum stumpage as it exists in provinces such as British Columbia. In British Columbia, minimum stumpage is currently only25¢/m^3. Raising the minimum stumpage rate will end the most highly subsidized logging. British Columbia's extremely low minimum stumpage rate assumes that there is no other value to a tree but their value as timber – an assumption that is not economically valid. Forests also support tourism and non-timber forest products industries and provide important environmental services such as landslide prevention.

Minimum stumpage (and minimum bids for timber sales) must be set at least high enough to cover government costs of planning, administration, reforestation and restoration, road maintenance and the opportunity costs foregone by not retaining the resource to provide environmental services. For example, BC charges a minimum stumpage rate of 25¢/m^3, which applies to all stands for which the CVMP calculation results in an amount less than 25¢. It has been shown that for the period Q1 1998 to Q2 2000, approximately 30% of all the wood logged in the interior of BC went for the minimum stumpage (which works out to about US $10 per truckload of logs), while in the Kalum forest district 90% of the stumpage paid was at the minimum rate[1].

At 25¢/m^3, it is highly unlikely that government is covering the cost of running the Forest Service or covering the full value of standing trees, including their contribution of environmental services and amenities, quality of life and non-timber forest-dependent economic activities. By selling wood at below costs and value, the government is artificially expanding the supply to include

[1] Mitch Anderson and John Werring, *Stumpage Sellout: How forest company abuse of the stumpage system is costing BC taxpayers millions* (Vancouver: Sierra Legal Defence Fund, 2001).

economically marginal timber. Ultimately, this drives down the market value of logs overall by selling a disproportionate amount of extremely cheap timber. Thus, it is absolutely critical that minimum stumpage is raised.

SECTION I.A.2

MINIMUM CUT REQUIREMENTS

Summary of Comment: The policy bulletin should state that minimum cut requirements should be removed, provided that this tenure enhancement to companies is offset through adequate tenure-take back. Maximum cut control must be retained, and exemptions to over-harvesting penalties eliminated.

Comment:

Minimum cut control would have to be removed to allow for license holders to make the determination of what timber is economically viable on a per species basis, but should only be removed (along with appurtenancy) as part of a larger tenure renegotiation that resulted in a significant portion of tenure being returned to the Crown for redistribution, as discussed below.

We note that requirements for companies to log all of the areas approved for logging in their cutting permits are not addressed in the policy bulletin. For example, BC' s *Forest (Revitalization) Amendment Act (No. 2), 2003*, S.B.C. 2003, c. 31 creates new waste assessment requirements. This Act makes changes to sections 13 and 35 of the *Forest Act* that will now require their tenure holders to pay to government "waste assessments for merchantable Crown timber, whether standing or felled, that could have been cut and removed under the tree farm license or timber license [or forest license], but, at the licensee's discretion, is not cut and removed."

Thus, although minimum cut control is eliminated, unless a licensee's cutting permit provides for retention of standing and downed timber (e.g., for ecological or cultural reasons), licensees will continue to be penalized for not logging everything on the areas set out in their approved cutting permits. While we do not disagree that some regulation of waste is appropriate, it should be focused on: a) creating incentives for companies to leave timber standing when costs or market price don't warrant moving it to market; and b) allowing cut trees to remain on site only if there are fulfilling a legitimate ecological purpose (i.e., to provide coarse woody debris in ecologically

appropriate amounts, size and class). The BC approach still continues to force logging and shipping of timber when market conditions do not warrant it.

- **Other Cut Control Concerns**

In recently passed legislation in BC, there are also significant and far-reaching exceptions to maximum cut control requirements. Regional managers can exempt any licensee from any cut control requirements if timber is considered "at risk because of wind, fire, insect or disease" (new *Forest Act* section 75.9). Given the current beetle situation this could make cut control meaningless in many areas of the province right now. Furthermore, if the Minister reduces a company's AAC for the following reasons, the Minister can reduce or exempt that company from penalties for over-harvesting (exceeding maximum cut control) (*Forest Act* section 75.92):

- through the timber supply review (*Forest Act* section s. 8);
- for failure to meet requirements to do plans studies, analysis, (new *Forest Act* section s.9);
- through the former section 56, five percent take-back on tenure transfer/change in control;
- temporary (s. 61) or proportionate reduction (*Forest Act* section s. 63); or
- because of the creation of a designated area (*Forest Act* section s. 173).

Discretionary exemptions from maximum cut control provide a market advantage to certain licencees, allowing them to log more than their authorized cut levels without penalty, while others, who do not receive discretionary exemptions would face penalties.

SECTION 1.A.4

MINIMUM PROCESSING REQUIREMENTS

Summary of Comment: The policy bulletin should allow raw log export restrictions (i.e., restrictions which require timber to be processed in BC) to be retained.

Comment

While acknowledging that raw log export restrictions constrain market forces, retaining such restrictions is essential at this stage in Canada's reforms. If other far-reaching reforms, of the nature set out in this submission, were adopted, the relative importance of this market constraint is limited. Furthermore, over time the development of a thriving and diverse value-added manufacturing sector in BC contributes to the objective of ensuring log markets with many buyers, as well as many sellers. Removing the raw log export restrictions at this point in time, would present a barrier to building this kind of market.

SECTION I.A.5

LONG-TERM, NON-TRANSFERABLE TENURE

Summary of the comment: Eliminating long-term tenure is not the answer and should not be a requirement of this policy bulletin. Instead government take-back and redistribution of tenure should contribute to the establishment of a transparent and fully functioning market. Allowing subdivision or consolidation of tenures, and removing public oversight of tenure transfers will create greater, not lesser distortion. Issues with long-term tenures cannot be adequately addressed as a factor affecting reference prices. In addition, the policy bulletin should require that any subdivision, consolidation or transfer of tenures include transparency and public participation requirements.

Comment:

The bulletin could be read as proposing the elimination of long-term, non-transferable tenure. When large companies hold the vast majority of rights to timber under long-term replaceable tenures, their security of supply inhibits responsiveness to market changes. However, in our submission, the fundamental problem is not in the nature of the tenures, but in how much of any given company's processing capacity is secured under such a tenure form, and how concentrated control over timber rights is overall.

Alternatively, the bulletin proposes that issues created by security of supply through long-term tenures can be addressed as a factor affecting the use of reference points in independently functioning markets as a basis for setting stumpage rates on the administered portion of a province's harvest. With the latter approach there remains a risk of manipulation by the provinces and the softwood industry, particularly with regard to cost estimates for responsibilities undertaken under long-term tenures and it is in no way sufficient on its own to address issues related to distortions that occur when a small group of licensees hold vast tenures. Actual take-back and redistribution of tenures is essential.

Nor is the creation of a market in long-term tenures the answer to achieve market-based pricing. Concentration in control of such tenures allows a small number of timber companies to exert

political and economic pressure to extract subsidies. However, a market in long-term tenures would only result in greater consolidation of the industry and reduced competition; recent experience in BC, for example, is strongly towards tenure consolidation, not disaggregation. As well, it would not provide any useful information for the calculation of stumpage on logs.

We propose an alternative approach involving: a) taking back a significant majority of existing tenure rights, without compensation to tenure holders, b) redistributing of these rights through timber sales, *and* long-term tenures that require the licensee to sell all, or a substantial majority of the timber on a log market after harvesting. The rationale for this approach is set out below.

With regard to transferability, it is inaccurate to imply that tenures in Canadian provinces such as BC are non-transferable. Tenures frequently change hands through either share purchase or asset purchase arrangements, subject to certain basic legal requirements (Ministerial consent to transfer, ability to insert conditions and 5% tenure take-back in BC). These requirements are important existing mechanisms designed to address the distortions created in order to provide security of supply to a handful of big companies. For this reason, any suggestion that a market in long-term tenures is part of the solution must be eliminated from the policy bulletin. Likewise, enhancements to tenure value such as eliminating consent to transfer/change in control and the 5% take-back on transfer or change in control in BC present a financial benefit to BC softwood producers, which will be realized in the form of windfall profits in future tenure sales.

BC and other Canadian provinces are starting from a situation where cutting rights are almost fully allocated. To lock in this situation by commodifying long-term tenure would be a huge windfall benefit to the small group of companies who currently control tenures.

Furthermore, later in the bulletin it is suggested that provinces should make their tenures "freely divisible and transferable." Allowing tenure holders to subdivide and sell tenure that they paid virtually nothing to the government for in the first place is an unacceptable financial benefit to softwood lumber companies that should be rejected. It is only through the government taking back a majority of tenure and redistributing it, combined with a requirement that new tenure holders are required to sell logs on an open, competitive log market or competitive timber sale, that a market based result will be achieved.

In fact, the presence of references to transfer and divisibility of long term tenures appear to reflect an acceptance by DOC of Canadian sleight of hand, whereby tenure changes that will either maintain, or even enhance, the concentration of control over BC's wood supply by a few large companies have been presented as market-based reforms. In particular, sales of long-term tenures (the price of which reflects the existing tenure subsidy) are not an appropriate basis for establishing timber value.

- **The policy bulletin should encourage government take back of at least 50% of major licenses' area or volume (depending on the type of tenure) in order to diversify control over the forestland base and to supply log markets.**

The most direct way of breaking down the control of major licensees[1] over the B.C. forest regime is to reduce the amount of forest land (for area-based tenures) or allocated cut (for volume-based tenures) they control by at least 50 percent. From a legal perspective, this can be easily accomplished through legislative amendments to the existing forestry legislation or through new legislation.

The existing legal framework in British Columbia reflects certain historical public policy choices regarding the circumstances in which tenure rights could be reduced. Incorporating into legislation the authority to reduce the area or volume controlled through tenures, without payment of compensation to timber companies is already common practice in B.C., just not to the extent necessary to accomplish a more diverse market. For example, the B.C. Forest Act already provides for reductions in allowable annual cut through the timber supply review process,[2] for proportionate reductions to all licensees in a timber supply area,[3] and when a licensee fails to live up to various environmental, utilization, and processing requirements.[4]

---

[1] *See*, Forest Act, R.S.B.C. 1996, c. 157, s. 1, "major licence." The vast majority of major licenses are Tree Farm Licences (TFL) and Forest Licences (FL), and over 80 percent of the volume cut on Crown lands is held through TFLs and FLs. Ministry of Forests, *Annual Report 1998/99* (Victoria: Ministry of Forests, 2001), Table C-7.
[2] B.C. Forest Act, Section 8(1) (1996).
[3] B.C. Forest Act, Section 63 (1996).
[4] B.C. Forest Act, Sections 69-71 (1996).

There is no definitive study indicating the degree to which control must be diversified – and thus first removed from the few major licensees, in order to create competition and functioning markets. The 1991 Forest Resources Commission in B.C. recommended a minimum 50 percent as a basis for establishing markets.[5] In what we see as only its opening bid, Weyerhaeuser has previously indicated publicly its willingness to give up 25 percent of the volume of its coastal tenures.[6]

- **The policy bulletin should explicitly disallow compensation for government take-back of tenure to log public lands.**

Since virtually no consideration was paid when most major licenses were granted,[7] awarding compensation for freeing up a portion of the wood supply would simply amount to further subsidization of the industry. Although some major license holders may have paid consideration to a previous holder of the license, there is no outstanding obligation from the public for such a transaction. The consideration paid when tenures change hands between companies largely reflects the current subsidy arising from the B.C. stumpage system– the elimination of which should not be compensable.[8] Such compensation, particularly if based on the "current market value" of tenure, is tantamount to a present value payout of expected future subsidies on that tenure, so in fact undermines the impact of establishing markets and other measures designed to "eliminate" subsidies.

Government take back of volume or area need not be compensated under Canadian law. As a general rule, Canadian law provides considerable flexibility to the government in reallocating control over public resources. Provided it does so explicitly through legislation, the Province has the authority to reallocate public forest resources without compensation.[9] Compensation generally

---

[5] A.L. Peel, *The Future of Our Forests*, Victoria: Forest Resources Commission, 1991, pages 40-41. *See*, http://www.for.gov.bc.ca/hfd/pubs/Docs/Mr/Rc001.htm

[6] Weyerhaeuser, *Coastal Competitive Reform: A Proposal for Market-based Stumpage and Tenure Diversification for Coastal BC* (October 2001).

[7] Tenures were granted in exchange for obligations such as operating mills (appurtenancy) to employ workers.

[8] T. Green and Matthaus, L. *Cutting Subsidies or Subsidizing Cutting?* BC Coalition for Sustainable Forestry Solutions, July 2001.

[9] In fact, this power extends to private property as well: *A.G.* v. *DeKeyser's Royal Hotel*, [1920] A.C. 508 at 542 (H.L.), cited with approval in *B.C.* v. *Tener*, [1985] 3 W.W.R 673 at 681 (S.C.C.).

is not triggered if the reallocations are implemented through statutory provisions that explicitly (in clear and unambiguous terms) state that no compensation is payable, or place limits on compensation.[10]

At present, the B.C. Forest Act contains a number of specific legal provisions that provide for reductions in allowable annual cut or deletions of area[11] from licenses without compensation. For example, compensation is not payable for actions to reduce allowable annual cut noted above.[12] Only in a few situations has the Province chosen to create a statutory right to compensation, further showing its discretion in the matter. For example, compensation is payable for reductions in AAC or tenure deletions that exceed 5 percent and are carried out for purposes other than timber production.[13]

The Forest Act is currently silent on deletions or reductions for the purpose of redistributing wood supply to new entrants for timber purposes or for the creation of functioning markets. It is therefore advisable that limitations on compensation must be addressed directly and explicitly in the legislation that provides for the necessary reduction in volume or area.

However, BC has recently moved in the opposite direction in the *Forest Revitalization Act*, S.B.C., c.17 by entrenching industry compensation entitlements, demonstrating that the policy bulletin must not remain silent on this point. Section 6 of this Act provides that each licensee is entitled to compensation "in an amount equal to the value of the harvesting rights taken by means of the reduction, which value must be determined under the regulations." It also says that in "addition" to this, the holder is entitled to "compensation from the government in an amount equal to the value, determined under the regulations, of improvements made to Crown land."

---

[10] "Where expropriation or injurious affection is authorized by statute the right to compensation must be found in the statute." *B.C.* v. *Tenor*, *ibid.* at 696; *Rockingham Sisters of Charity* v. *R*, [1922] 2 A.C. 315 at 322 (P.C).

[11] Deletions of area from licenses occur only in area-based licenses such as Timber Licences and Tree Farm Licences.

[12] B.C. Forest Act, Section 80 (1996).

[13] B.C. Forest Act, Section 60 (1996). Provides a statutory right to compensation if a deletion is made that reduces a licensees' allowable annual cut by more than 5 percent and the deletion is for purposes other than timber production (*i.e*. park creation etc.). *See*, http://www.for.gov.bc.ca/tasb/legsregs/forest/foract/part4-31.htm#60

Finally, it is essential to see a tenure take back as part of a broader renegotiation of the historical "tenure contract" associated with the entire system, rather than a unilateral impact on companies' interests. For example, tenure take back in BC is being structured as part of a package that also includes elimination of tenure requirements that limit logging companies' flexibility, such as minimum cut control and appurtenancy. These are burdensome obligations that the B.C. timber industry wishes to abolish, and which will financially benefit them by enhancing their tenure value. Thus, tenure take-back without compensation can also be seen as the quid pro quo for such tenure enhancements.

- **The policy bulletin should require government reallocation of tenure to log public lands.**

Currently, ten integrated forest products companies control more than 55 percent of the provincial annual allowable cut, while the government's Small Business Forest Enterprise Program only controls 13 percent.[14] Coupling tenure take back with reallocation of tenure to a diversity of interests will help ensure the type of diversified industry necessary for functioning markets. Diversifying the means, manner and legal status available for new entrants to control and manage forests will create a fuller spectrum of competing interests. Furthermore, breaking down control over forestland is also essential to ensure that a small group of companies cannot exert their political and economic control to extract further subsidies.

The need to diversify the types of tenure holders was expressed in 1991 by the provincial government's blue-ribbon Forest Resource Commission that stated:

> *In essence, the Commission sees a tenure system that significantly reduces the volume of timber now controlled by a relatively small number of large corporations, and transfers that freed up volume to the development of a competitive log market.*[15]

---

[14] Ministry of Forests, *Provincial Linkage AAC Report*, 2000. *See*, www.for.gov.bc.ca/ftp/Branches/Resource_Tenures_&_Engineering/external/!publish/apportionment/aptr043.pdf

[15] A.L. Peel, *The Future of Our Forests*, Victoria: Forest Resources Commission, 1991 at 40. *See*, http://www.for.gov.bc.ca/hfd/pubs/Docs/Mr/Rc001.htm

Our proposal for tenure redistribution is closely linked to the discussion of log markets (below). In our submission, reallocation of tenure through a variety of tenure forms, including new long-term tenures that require all or a specified portion of harvested timber to be sold on open regional log markets, is the preferred approach to support development of functioning markets that have many buyers and many sellers and are large enough to generate accurate price signals.

For example, the BC Coalition for Sustainable Forest Solutions has suggested that priorities for redistribution should include:

(a) long-term area-based tenures designed to accommodate First Nations;
(b) community forest agreements that require the holder to sell all or a representative portion of logs harvested through a log yard;
(c) timber sales licences of volumes less than 10,000 cubic metres to independent businesses who do not hold major licences;
(d) timber sales licences structured as harvest and haul contracts in which the Crown retains its title to the trees after harvesting; and
(e) woodlot licences that require the holder to sell all or a representative portion of logs harvested through a log yard.[16]

There are two existing tenure forms that can be used to diversify the types of companies involved in managing B.C.'s forests. Legislation enacted in 1998 established community forest agreements as a new form of forest tenure.[17] Eleven community forest pilots have been established to allow the new tenure to be tested. Woodlot licenses have existed as a form of tenure for a number of years.[18] However, because of over commitment of wood supply to major license holders, there is widespread unfulfilled demand for more woodlots and community forests.[19] Given the unfulfilled demand for these two existing tenure forms, the province could begin diversifying both the

[16] BC Coalition for Sustainable Forest Solutions, *Forest Solutions for Sustainable Communities Act*, S.B.C 2003, c.x (proposed private members bill).
[17] B.C. Forest Act, Division 7.1 (1996).
[18] B.C. Forest Act, Division 8 (1996).
[19] Over 100 communities have expressed an interest in acquiring a community forest agreement pilot. Twenty-seven communities submitted full-proposals and only eleven have been granted. Community Forest Agreement Program, Annual Report 2000-2001, *see*, http://www.for.gov.bc.ca/pab/jobs/community/. Unfulfilled demand for woodlot licenses significantly exceeds supply as numerous applications are received for every woodlot license granted. For woodlot license program, *see*, http://www.for.gov.bc.ca/RTE/woodlots/woodlot-program.htm

number and the relative proportions held in different types of tenure by immediately redistributing freed up wood supply to new entrants who have already expressed interest in community forest agreements and woodlot licenses. A British Columbia government poll indicated that 85 percent of British Columbians support more community control of forests.[20] Such broad support will enhance the future stability of reforms.

This tenure redistribution is not only compatible with competitive log markets, but is an essential component to making them work as it will result in more timber being directed into log markets. Many of the applicants for community forest agreements indicated in their applications that they would direct their timber to log markets, if more were available.

In order to make the transition during the first few years following a negotiated agreement concerning softwood lumber trade, a portion of the freed up wood supply should be made available to the highest bidder at auction through timber sales.[21] A portion of the freed up wood supply could also be made available to First Nations in order to resolve decades-old disputes over indigenous rights. Increasing timber sales for the first two years will be relatively easy as a significant number of approved cutting permits will be freed up as a result of the tenure take back outlined earlier. The planning on these approved cutblocks/cutting permits has already been completed so they will be relatively easy to convert into timber sales.

In order to ensure the establishment of an open, competitive market, all wood harvested under timber sale licenses during the initial few years could be required to be directed to a regional log market. Within two years following a negotiated agreement, the provincial government will have had the opportunity to establish new legal tenure types to continue to diversify control of the land base. These new tenure types should allow for devolving decision-making control over the forested land base to community management authorities and First Nations.[22]

---

[20] Environics, August 2000. *See*, http://www.environicsinternational.com/
[21] B.C. Forest Act, Section 20 (1996).
[22] The Community Ecosystem Trust proposal of the University of Victoria's Eco-Research Chair of Environmental Law & Policy is one example of a potential framework for Community Management Authorities. *See,* Michael M'Gonigle *et al*., *The Community Ecosystem Trust: A New Model for Developing Sustainability,* University of Victoria, 2001. See also the submission of the BC Coalition for Sustainable Forest Solutions on the softwood lumber policy bulletin (August 8, 2003).

- **The policy bulletin should require transparency and public participation in any subdivision, consolidation or transfer of tenure.**

Any new regulations governing subdivision, consolidation or disposition of tenures should include transparency and public participation requirements. As provinces restructure their tenure systems, there may be an inclination to remove public accountability of tenure transfer transactions. This is undesirable from both a public policy and economic perspective, as availability of full information is key if markets are to be truly open and transparent, and generate accurate price signals.

For example, in British Columbia, the ordinary practice concerning public land tenure transfers had been for public hearings to be held and for a report about the proposed disposition to be made public. However, under the new BC Forest Revitalization Amendment Act provisions dealing with disposition and licensee change in control there is not even a requirement to give notice of proposed tenure disposition to the public or First Nations. This is also the case with consolidation or subdivision of tenures.[23]

The lack of a requirement for notice and for consultation for subdivision, consolidation and transfer of public land tenures is a violation of First Nations and public rights. Tenure subdivision, consolidation and transfer involves vast areas of public lands, many of which are subject to unextinguished Aboriginal title. Lack of transparency in tenure disposition also affects the functioning of markets as some potentially willing buyers will be unaware of opportunities available.

[23] BC Bill 29 –2003, Forest (Revitalization) Amendment Act (passed May 29, 2003, section 10 in force April 1, 2006; Section 12(b) in force July 1, 2003, rest will come into force by regulation).

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.A.6
OFFSETTING PROVINCIAL ACTIONS

Summary of Comment: The policy bulletin should clarify what is meant in this section by "other requirements or conditions on the sale of provincial timber that would inhibit or undercut the operation of the policy reforms" discussed in section I.A, to include clear benchmarks for cost appraisals that encompass forest management based on ecological sustainability and a prohibition of regulatory relief through roll backs of environmental protections through new legislation or lack of enforcement of existing laws.

Comment:

The policy bulletin states that the DOC will also examine any evidence that suggests that a province maintains or introduces other requirements or conditions on the sale of provincial timber that would inhibit or undercut the operation of the policy reforms. It gives as an example that DOC will want to ensure that a province's decisions with respect to the annual allowable cut authorized on provincial lands is consistent with sound forest management and the full rotational economics of the forest, rather than a means of increasing supply and thereby artificially lowering the amount charged on provincial stumpage. This does not go far enough to ensure that annual allowable cut is based on principles of ecological sustainability and to ensure that practices such as weakening of environmental protections are not substituted as another type of subsidy to softwood lumber companies.

- **The policy bulletin should articulate clear benchmarks for cost appraisals that encompass forest management based on ecological sustainability.**

When the British Columbia *Forest Practices Code* was introduced in 1995 it contained mechanisms for habitat and species-specific biodiversity protections. These have never been fully implemented, and have been constrained by arbitrary timber supply impact caps on their implementation. At a minimum, environmental standards, and thus industry costs, should be benchmarked at a level that reflects full, scientifically defensible implementation of the Code framework as initially enacted.

Forest management in most of Canada is driven primarily by volume goals, rather than by a combination of economic and ecological considerations. For example, the government in British Columbia, the largest lumber producer and exporting province in Canada, has mandated logging levels that are above sustainable levels, even by its own estimates.[1] Under some calculations, 30 to 40 percent of the current AAC could be considered sustainable, while the remainder depletes natural capital.[2]

Trade distortions cannot be eliminated without ecological sustainability providing the underpinnings for provincial planning and logging levels. Canada should ensure that both coarse filter (habitat) and fine filter (species specific) protections are in place for biodiversity. Both landscape level planning, and species specific measures must be scientifically based and unencumbered by unsustainable timber targets, timber supply impact caps, and undue influence by timber companies.

Ecologically sustainable landscape level planning tends to exert downward pressure on logging levels, maintain conditions needed to ensure ecological integrity, help ensure that a wide range of species' needs are met, and encourage efficiency and effectiveness in operational planning. This raises the value of forest products and increases competitiveness between U.S. and Canadian lumber producers.

Ecologically sustainable landscape level biodiversity planning should also be complemented through an internationally directed "focal" species approach and an aquatic conservation strategy. These measures should be coupled with protection of representative ecosystems and the monitoring for the effectiveness of management in achieving the goals of the viability of focal species across the landscape and the perpetuation ecological sustainability, as well as ecologically based stand level requirements. The Canada/United States border area would benefit from this type of approach. It has been used in the United States for over two decades, and is accepted by every major international forest protection protocol or management guidelines.[3]

---

[1] British Columbia Ministry of Forests, Timber Supply Review Backgrounder, updated as of August 2002. *See,* http://www.for.gov.bc.ca/tsb/back/tsr/tsrbkg.htm.
[2] T. Green, *Cutting for the Economy's Sake: Setting Timber Harvest Levels that are Good for B.C.'s Economy*, Working Paper prepared for Sierra Club of BC, April 2000 at 79.
[3] *See, e.g.,* 16 U.S.C. § 1604(g)(3)(B); 36 C.F.R. § 219.19; 36 C.F.R. §§ 219.26; 219.27(a)(5),(g) (provisions of National Forest Management Act and implementing regulations requiring maintenance of diversity and viability of species, partly through focus on "management indicator species," on U.S. federal forests).

- **The policy bulletin should include safeguards against regulatory relief such as roll-backs in environmental obligations, or failure to enforce environmental laws that artificially alter industry cost structures, thus "passing back" subsidies to Canadian companies**

Roll-backs in environmental obligations can be seen as one way to reduce costs for logging companies. Without adequate safeguards against such roll backs, a softwood lumber trade agreement that eliminates other subsidies could pave the way for provincial governments to offer logging companies other compensations, such as reduced environmental obligations. This is just as much a subsidy as below-market stumpage fees.

In fact, such roll-backs are already being implemented in at least British Columbia. British Columbia is currently in the process of completely overhauling its legal framework for forest practices in such a way as to reduce environmental protections, particularly measures to prevent environmental damage before harm is done. [4] While regulations under the Forest and Range Practices Act are still under development, there is every indication that environmental standards will be substantially reduced in the new framework.[5] As British Columbia implements its forest practices changes to provide environmental relief to the forestry industry, this will substantially offset any economic reforms the government might promise in the context of the softwood lumber trade discussions.[6]

The B.C. government itself has made the Forest Practices Code a core softwood lumber issue. For example, a 1997 B.C. Ministry of Forests study estimated that the Code 'cost' the B.C. industry C$12.22 per cubic meter, or C$733 million per year extra, over forest management obligations prior to 1992 and used this to justify low stumpage fees.[7]

---

[4] For amendments to B.C. Forest Practices Code and the new Forest and Range Practices Act seem http://www.for.gov.bc.ca/code/.

[5] Sierra Legal Defense Fund, *Who's minding our forests? Deregulation of the forest industry in British Columbia*, May 2002. *See*, www.sierralegal.org. For more information concerning the process of revising the B.C. Forest Practices Code *see*, http://www.resultsbasedcode.ca/

[6] To understand the magnitude of those cost structures, in addition to the stumpage break, in 1998, B.C. also passed 550 rollbacks to the Code, saying that this would result in a savings to the B.C. industry of an estimated $C300 million per year. There is still hundreds of millions of dollars more at stake.

[7] KPMG, Perrin, Thorau & Associates Ltd., and H.A. Simons & Associates Ltd., *Financial State of the Forest Industry and Delivered Wood Cost Drivers*, April 1997. *See*, www.for.gov.bc.ca/het/costs/fin-10.htm

Discussions about forest management in British Columbia figured into the last Softwood Lumber Agreement,[8] and in 1998, B.C. justified its unilateral stumpage rate reduction based on the costs of implementing the environmental provisions in the then-relatively new Forest Practices Code. That was an explicit acknowledgement that timber pricing and forest management are inextricably bound together in this dispute. Public forest management regulations compose a large part of the cost structure of the B.C. forest industry in a province where such regulations govern 80 percent of the forest landbase. The revision of the Code is a *de facto* re-working of those cost structures.

Any softwood lumber trade resolution will need to ensure that gains made in reforming economic subsidies are not offset by new subsidies to the forestry industry through weaker environmental protection. Any changes to the Forest Practices Code in British Columbia, for example, should maintain or strengthen and implement the substantive environmental standards of the existing forestry laws. Environmental protection regulations should contain standards that are measurable, verifiable, and therefore enforceable.

Lack of enforcement of environmental laws also confers a benefit on timber companies and artificially reduces industry cost structures. Canada has typically refused to enforce its federal Fisheries Act against timber companies or to require provinces to implement and enforce the Act. For example, a 1997 study of logging practices around streams found that 83 percent of B.C. streams surveyed were clearcut to the banks. The same study found that only 12 percent of the streams surveyed had been logged under prescriptions containing explicit prohibitions on the damaging practice of dragging logs through them on the way to logging trucks.[9] These practices are permitted under the B.C. Forest Practices Code, even though they are prohibited under the federal Fisheries Act.[10]

---

[8] A side-letter, which was incorporated as part of the 1996 U.S./Canada Softwood Lumber Agreement, effectively prohibited the provinces from modifying their timber management and pricing systems in a manner that would reduce the average cost of timber or its harvesting to the industry.

[9] Sierra Legal Defense Fund, *Stream Protection Under the Code: The Destruction Continues,* February 1997.

[10] Canadian federal Fisheries Act, Section 35(1) ("no person shall carry on any work or undertaking that results in harmful alteration, disruption or destruction of fish habitat"). Section 36(3) ("no person shall deposit or permit the deposit of a deleterious substance of any type in water frequented by fish…")

There is evidence that Fisheries and Oceans Canada staff realized that compliance with the B.C. Forest Practices Code was not sufficient for compliance with the Canadian federal Fisheries Act, as the following statements from agency staff illustrate:

> "*…MacMillan Bloedel's assertion that adherence to the Forest Practices Code will fulfill their commitment to maintain fish, fish habitat, and riparian attributes is not the Department of Fisheries and Oceans' position, particularly with regard to small streams."*[11]
>
> *"If you look at the small streams that are harvested under the Forest Practices Code, they are no longer ecosystems."*[12]

The Canadian government must by law remedy this situation, although so far it has failed in its responsibility. Sections 35(1) and 36(4) of the Fisheries Act respectively prohibit work or undertakings that result in the harmful alteration, disruption or destruction of fish habitat, and the deposit of deleterious substances in water frequented by fish. Section 43 authorizes the Canadian federal government to pass regulations to carry out the purposes and provisions of the Act. Sections 35 and 36 also contain specific regulation making powers. For example, under Section 36 of the Fisheries Act, the Canadian government has regulated pulp mill effluent emissions (as clean water is one element of fish habitat).[13] The Canadian government has the similar powers under Section 35. Thus, subject to limitations that arise from the jurisprudence in this area,[14] the Canadian federal government has the authority to develop and implement regulations setting specific standards for conservation and protection of fish, which should include protection of fish habitat through streamside buffers.

Second, Section 40 of the Fisheries Act authorizes Fisheries and Oceans Canada to pursue prosecution after-the-fact of those who harmfully damage fish habitat. It has the ability to assess

---

[11] Dovetail Consulting, *"An Evaluation of DFO Involvement in Land and Resource Management Planning in British Columbia,"* prepared for the Habitat and Enhancement Branch, Fisheries and Oceans Canada, March 5, 1999 at 56.
[12] *Id.* at 59.
[13] Pulp and Paper Effluent Regulations, SOR/92-269.
[14] E.g. controls on logging and other works or undertakings must be linked to actual deleterious affects on fish. *Fowler v. The Queen*, [1980] 2 S.C.R. 213; *Northwest Falling Contractors Ltd. v. The Queen*, [1980] 2 S.C.R. 292.

penalties ranging from summary convictions with C$300,000 fines and up to six months imprisonment, to indictable convictions with fines up to C$1 million and three years imprisonment.

Third, under Section 37 of the Fisheries Act, Fisheries and Oceans Canada may require information from the proponent of a project, such as logging, to allow the agency to determine if the activity will result in a harmful alteration, disruption, or destruction of fish habitat, or if the activity will result in the deposit of a deleterious substance. If the information obtained indicates that a violation of the *Fisheries Act* is likely to occur, the agency may require modifications to the activity or restrict its operation.

Citing reduced appropriations, inflation, increased workload, and declining per capita enforcement expenditure, a recent analysis concluded, "wildlife populations and biological diversity are endangered by chronic underfunding and marginalizing of wildlife and conservation-oriented enforcement programs in British Columbia…" [15] The report notes that inadequate enforcement capabilities are further "aggravated by escalating and uncoordinated land use activities" including timber operations. Fish and wildlife enforcement in British Columbia was further diluted in 1995, when conservation officers were tasked with the additional enforcement of provisions of the Forest Practices Code. As of 2002, it is estimated that this new responsibility diverted between 10 and 20 percent of conservation officer time and resources that previously were available for other enforcement. The author concludes that "B.C. has now crossed the threshold at which protection of fish and wildlife populations and their habitat by enforcement services has effectively and materially been abandoned." Any combination of relaxed regulatory requirements and inadequate enforcement of remaining regulations would constitute an additional subsidy to the Canadian timber industry.

---

[15] Horejsi, Brian L., *Losing Ground: The decline in fish and wildlife law enforcement capability in British Columbia and Alaska*, 2002. Raincoast Conservation Society. Victoria, BC. 45 p. Full text of the report is available at: < http://www.raincoast.org/files/enforcement_FINAL.pdf > or at <http://www.raincoast.org/publications.htm#losing%20ground >

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.1

REFERENCE PRICES

Summary of Comment: The section on reference prices mentions the volume of timber traded on the market as a criteria to assess whether the reference market functions as a truly competitive market, but does not go into any detail on what this means. The policy bulletin should include a section that discusses the volume of timber traded on the market necessary to determine whether the reference market functions as a truly competitive market, including the establishment of viable regional log markets, the expansion of the auction of timber though timber sales licenses, and a prohibition on log bartering.

.

Comment:

The section on reference prices mentions the volume of timber traded on the market as a criteria to assess whether the reference market functions as a truly competitive market, but does not go into any detail on what this means. The policy bulletin should include a section that discusses the volume of timber traded on the market necessary to determine whether the reference market functions as a truly competitive market. Alternatively, or in addition, the policy bulletin should make a more definitive statement regarding how much fibre furnish a major mill must acquire through a market rather than from proprietary tenures. In the end, a substantial majority of timber volume harvested must flow through market mechanisms, including markets in logs.

While increasing the number of timber sales for small business loggers is important to help establish a fair market benchmark for public timber in Canada, it is equally if not more important to create actual markets in logs available for processing. Provinces in Canada should institute regional log markets to generate accurate timber values, ensure ease of access to wood for all wood processors (particularly in the value-added sector), and provide confidence that the full value of logs is being collected. In addition, sufficient volume should be required to flow through log markets to ensure an 'even playing field' and truly competitive bidding (e.g., at least 60 percent of timber harvested is proposed by value added manufacturers). Finally, stumpage fees should be calculated in a transparent manner, using accurate timber values from log markets and timber sales so that the full value of the wood is collected.

The objective of timber pricing reform in British Columbia would be that at least 60 percent of all volume harvested would flow through market mechanisms, including log markets. The 1991 Forest Resources Commission found that:

> *A log market with a significant piece of the action will also ensure that log prices reflect the species and grades of logs and their value in production. The log market, in assuring that prices are maximized in keeping with the true market value of the resource, will also reduce waste in the woods and ensure the most economic value is captured through manufacturing higher value-added products.*[1]

To achieve this end, the Forest Resources Commission recommended that "the amount of Allowable Annual Cut held under tenures by companies with manufacturing facilities be reduced to not more than 50% of the lesser of either their processing capacity or their present cut allocation." In turn the wood freed up would be used "to create a greater diversity of tenures," and timber made available through these new tenures, including "area-based tenures managed by communities, Native Bands and woodlot operators, etc.," would "be used as the basis to develop a competitive log market in British Columbia."[2]

- **The policy bulletin should set criteria for the establishment of viable regional log markets.**

One objective of increased volume to market mechanisms is to make certain enough timber is available to a broad range of processors to ensure that, over time, competition among processors is pushing B.C.'s processing sector further up the value-added chain. Only when value-added processors have ease of access to the volume and grades of timber they require will the full value of B.C.'s timber supply be realized. This objective would be assisted if at least 60 percent of the wood harvested in B.C. flowed through regional log markets, not just through market mechanisms in general. Ideally, each region would have one or more log markets, depending on regional logging activity, geographic concentrations of processing activity, and transportation limitations. This is necessary to fully capture the range of timber attributes across the province as well as geographic or other circumstances that can affect the value of timber.

---

[1] A.L. Peel, *The Future of Our Forests*, Victoria: Forest Resources Commission, 1991at 40-41. *See*, http://www.for.gov.bc.ca/hfd/pubs/Docs/Mr/Rc001.htm
[2] Ibid.

Log markets are important in order to increase over time the number of processors active in the market. Even if a broad range of loggers participate in a competitive, transparent market in timber sales, if those loggers can only sell their logs to a few large commodity processors – lumber or pulp companies – the value of B.C.'s log supply will remain artificially constrained by the value of those low value products.

Regional log markets provide the opportunity for a broad range of processors to access timber in a competitive market situation, thereby driving up the value of B.C.'s wood supply over time as an increasing number of value-added processors are able to outbid low value processors. This in turn would translate into higher bids for timber sales and higher stumpage to the Crown.

While B.C. has experience with log markets, such markets have not fulfilled their potential due to built-in structural impediments. The primary problem has been that they were simply too small to get past marginal pricing problems. For example, one or two major companies could take most of the volume on the log market at an artificially high price, which they could pay because they were only buying a relatively small top up to their tenured supply or demand is depressed by massive volumes of subsidized timber. Despite these shortcomings, log market experiments have been very successful in providing access to timber for many small processors and in realizing much higher values for low-grade timber purchased for value-added purposes.[3]

In order for regional log markets to work in practice, several conditions will have to be met, including:

- Sixty percent of the actual harvest in each region should be the threshold volume directed to log markets.
- Regional log markets should be arms length from industry, and from government agencies responsible for developing forestry policy and regulation.
- Government should be responsible for scaling.

---

[3] Catherine M. Mater and Scott M. Mater. *Vernon Forestry: Log Sorting for Profit. A Case Study from "The Business of Sustainable Forestry"* (Project of The Sustainable Forestry Working Group, n.d.), 15-10: "*One of the largest increases [due to sorting of logs] occurred in the sale of lower-grade logs, which included a large percentage of dry logs and logs that had died on the stump…. A typical dry sort was sold at $110 per cubic metre. After deducting the average cost of $55/m^3 for logging and sort yard and stumpage costs, these sorts provided a return of $54.75/m^3 more than if sold for traditional lower-grade uses."*

- Logs should be sorted into as many sorts as buyers demand, especially to facilitate small processors' participation.
- Capacity should exist for fulfillment of any chain of custody (tracking) requirements for certified logs.
- At least one scaler in each market should be trained in both the B.C. scaling system and the Scribner system used in the United States.
- Government should apply stiff penalties for collusion to manipulate prices by companies.

Ideally, *each region* within a Province would have one or more log markets, depending on regional logging activity, geographic concentrations of processing activity, and transportation limitations. One or two small markets, which would not be ecologically and otherwise representative of the range of conditions and forest types across the province, are not a sufficient basis for use in calculating administrative stumpage, nor is the so-called "Vancouver Log Market."

Northwest Ecosystem Alliance prepared a detailed report examining the Vancouver Log Market.[4] This market consists of all logs sold, purchased, or traded in coastal British Columbia. While the "market" has no physical log yard or trading floor, the prices for these logs are compiled and published on a monthly basis by the Government of British Columbia's Ministry of Forests.[5] The stumpage fee assessed coastal tenure holders is then based, in part, on the average market value calculated from the previous six months' Vancouver Log Market transactions.

As a B.C. legislative committee stated, "The Vancouver Log Market displays features inconsistent with a freely competitively driven market place."[6] The log market fails to function as an actual market because the tenure system allots most of the government timber on the B.C. Coast to a small number of large corporations that both harvest timber and produce lumber. Log sales in British Columbia are not independent sales, but are actually log swaps among tenure

---

[4] Northwest Ecosystems Alliance, *Log Price Comparisons in the Vancouver Log Market,* December 2001.
[5] The British Columbia Forest Act, section 136(1), requires any person "who harvests timber, who buys or sells timber or products manufactured from timber or who operates a timber processing facility" to report, *inter alia*, "the volumes and prices of timber, or of products manufactured from timber, that are bought and sold."
[6] Graham Bruce (Chairman), *Second Report of the Select Standing Committee on Forest and Lands: Forest Act Part 12 and the Vancouver Log Market*, Mar. 12, 1991, quoted in Northwest Ecosystems Alliance, *Log Price Comparisons in the Vancouver Log Market,* December 2001at 4.

holders.[7] Further, since the government timber price is based on previous log market prices, the circular relationship between timber prices and log prices in Canada depresses the reported log prices.

In addition, the log market ensures a steady supply of low-cost wood fiber to the major lumber producers. As the B.C. industry trade association stated, "The cyclical nature of the forest industry results in many operators seeking mutually supportive and stable business relationships. . . . Pricing may become of equal consideration to the practices of long term guarantees and security of supply."[8] Thus, even so-called independent loggers (who, in any event, harvest only a tiny percentage of the timber) are forced by the lack of a functioning log market to sell their logs to the lumber producers at depressed prices.

It is unsurprising, then, that the study found log prices on the Vancouver Log Market are significantly depressed in comparison to delivered log prices for similar grades and species of logs on the Washington and Oregon coasts, especially for Western Red Cedar.

- **The policy bulletin should require expansion of auction of timber though timber sales licences.**

Timber auctions are a relatively easy way to get more timber into a competitive market system quickly. A pool of timber, whether consolidated in government (through a tenure take back) or selected from licensees' plans, is already available, as licensees generally already have obtained approvals for a minimum of two years of cutting. As a result, most of the required planning has already been done.

British Columbia already directs approximately 13 percent of its timber supply through the Small Business Forest Enterprise Program – a government administered program that prepares and sells some of its cutblocks through timber auctions. There are many small business harvesters and contractors that would be ready to step into such a system as most major licensees are already required to contract out a large portion (up to 60 percent on the coast) of their cut to contractors.

---

[7] Pearse, Peter H., *Ready for Change: Crisis and Opportunity in the Coast Forest History,* A Report to the Minister of Forests on British Columbia's Coastal Forest Industry, Vancouver, November 2001 at 24.
[8] Council of Forest Industries, *Response to the Select Standing Committee on Forest and Lands First Report on the Vancouver Log Market and the Forest Act - Part 12*, Aug. 1990, at 13.

Timber sale auctions are a transparent way of valuing timber "on the stump." The prices will be a valuable benchmark for a market-based stumpage formula for administered prices.

In order for a viable market in timber sales to emerge in practice, several conditions should be met, including:

- Ten percent of the bid price should be deposited upon award of a sale and forfeited for non-performance to reduce speculative bidding.
- Terms of timber sales should be two years with the possibility of extension by one year for market reasons.
- Timber Sales Licences could require winning bidders to direct the wood to regional log markets (allowing them to reflect competitive assessments of logging costs).
- Bidding for conservation purposes should be allowed on timber sales.
- Timber sales must be small in size, and otherwise pro-competitive (e.g., with measures to offset advantages larger players could use to lockout new entrants).

- **The policy bulletin should prohibit log bartering.**

Major licensees currently barter significant portions of their tenured timber amongst themselves to acquire the appropriate log profile for their mills. This type of a barter process retains control of logs within a small circle of tenured licensees, without opening up the process to the full range of potential buyers. It shields the companies from having their logs subjected to true market valuation. This type of bartering hampers the establishment of true market values for timber in B.C. Instead, B.C. should ensure that all wood not processed by licensees is required to be sold through competitive, transparent regional log markets.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.1.a
NUMBER OF PARTICIPANTS IN THE REFERENCE MARKET

Summary of Comment: The policy bulletin should require large reference markets and expand its current focus on the *number* of participants in the reference market. Focus should instead be placed on proportion of timber supply, proportion of mill requirements met through transparent market transactions and independence of players (as well as number of participants), with specified thresholds where appropriate.

Comment:

The policy bulletin focuses on the *number* of participants in a market. Proportion of timber supply flowing through the market is perhaps an equally, if not more, important measure than absolute number of participants. It would be possible to have many small bidders, increasing the number of participants, but without the market demand of the large players the market will continue to underestimate value. This is particularly true if most of the market participants are themselves under-capitalized, and unable to exert the same scale of market pressure as the major processors.

Greater consideration should be given the possibility of using proportion of fiber furnish to large mills acquired in transparent markets as a characteristic or measurable indicator to monitor, preferably with a threshold specified in the policy bulletin. It is not by mistake that the Forest Policy Commission of 1991 made this one of the options in their recommendation for building a more transparent market for logs in B.C.

Independence of bidders in the timber auction should also be considered. At an extreme, a situation where most of the "bidders" in a market were tied to major tenure-holders in some manner would not likely lead to truly competitive market functioning.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.1.b
QUALITY OF INFORMATION

Summary of Comment: The policy bulletin should clearly state that in addition to transparency, high quality information depends on independent gathering and maintenance of the information, as well as public accessibility of the information. As well, it should prohibit the barter and swap of logs in non-monetary, non-arms-length transactions; these should take place in open and transparent markets.

Comment:

The policy bulletin correctly states that full and transparent information availability is a critical criteria. However, additional guidance is necessary. The policy bulletin should make it clear that such information must be gathered and maintained in an independent manner from the companies, and must be publicly available as an additional check on transparency. Transparent, independently gathered, and publicly available information is necessary for a market-based pricing system.

This section should also raise the problem of log barter and swap. There are regions in Canada (e.g., coastal British Columbia) where a significant proportion of timber changes hands through barter, with mutually agreed upon "prices" being set by the two parties involved in the exchange, not in an open and transparent manner. The extent and nature of these swaps carry much information on the relative value of species and grades, which isn't readily transferable or transparent as a barter or swap transaction. These trades must instead be monetized and take place in an open and transparent market arena, such as a regional log market where trades are monitored and prices used to verify data gathered through standing timber auctions.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.1.c
DIRECTION OF CAUSAL LINK

Summary of Comment: The policy bulletin should be cognizant of the potential for a forest sector to organize itself into two separate "markets": one that participates in the official timber auction process that sets stumpage prices, and one that operates among the major players away from the market function, in order to insulate the official market from the demand effect of large processors who have an interest in keeping stumpage prices low. Only a market where a majority of timber is passing through will reduce the ability of the sector to organize itself along these lines.

Comment:

If the major processors can meet most of their fiber requirements on their own tenures, they could effectively "reverse" the causal link by avoiding the market, relying largely instead on barter/trade among themselves to meet specific mill requirements (e.g., grade or species specifications). This potential for reversal will be increased by changes that make tenures more easily transferable among those major players. For example, with recent policy changes in B.C., 80% of the timber supply currently held by a few major processors will be left in their hands, and tenure transfers are now much easier, less transparent, less open to public scrutiny. In such a situation, it will be relatively easy for the few largest players to tailor their tenure holdings to their mill requirements (and meet minor adjustments in fiber furnish through swaps), especially when combined with the removal of appurtenancy requirements that allow the companies to shut down mills with ease.

As an alternative, the policy bulletin should consider guidelines that result in a significant tenure take-back (i.e., 50% or more) and targets for acquisition of fiber in markets.

SECTION I.B.1.d

BARRIERS TO ENTRY OR EXIT IN THE MARKET

Summary of Comment: Raw log export restrictions should not be part of the prohibited "barriers to entry or exit in the market." As well, a market in *tenure* should not be an objective of the policy bulletin; fully functioning markets in *logs* is the objective, which can be achieved separate of tenure.

Comment:

The policy guidance section concerning barriers to entry or exit in the market concerns, in part, Canadian raw log export restrictions. However, provided other reform components are in place, and given the political difficulties associated with removing raw log export restrictions, we do not believe that this should be part of the policy guidance.

As well, the inclusion of a market in long-term tenure should not be considered relevant to issues of log market transparency and function. A fully functioning and transparent market in logs or standing timber combined with a transparent method of stumpage calculation would provide an adequate buffer between decisions that affect allocation of long-term tenure (a public asset in much of Canada) and the price of raw material to the processing sector.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.1.e

SAFEGUARDS AGAINST COLLUSIVE BEHAVIOUR

Summary of Comment: In addition to "safeguards against" collusion, the policy bulletin should also speak to policy decisions that encourage collusion.

Comment:

See the situation outlined under "Direction of Causal Link." Such a situation, whereby market avoidance is the preferred behavior among major processors, is difficult to detect and prevent. The loopholes that may allow for the 'self-organization' of the industry into two very separate spheres of activity – the "market" sphere and the "non-market/tenured" sphere – must be closed. That would require setting a high threshold for proportion of the timber supply flowing through a market, and prohibiting log bartering and trade. Those who wish to avoid the market, particularly larger players, must not be allowed that option.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.2.a

TRANSPARENCY IN THE FUNCTIONING OF THE MARKET USED AS A REFERENCE POINT FOR MARKET PRICES

Summary of Comment: In focusing primarily on transparency, the policy bulletin does not go far enough in establishing the necessary criteria for a functioning reference market. The policy bulletin should include the development of a market that mediates the market transaction in a neutral, disinterested fashion and prohibits practices such as highgrading and bartering.

Comment:

We welcome the DOC's recognition of the importance public availability of information regarding market transactions and its emphasis that log swaps are problematic in establishing an adequate reference market.

However, there are some serious conceptual shortcomings in the policy bulletin that must be addressed. Most significantly, simply improving reporting of log swaps and bilateral arrangements between companies is completely insufficient to establish a reference market. True transparency requires a log market that is arms length from producers, which mediates the market transaction in a neutral, disinterested and transparent fashion. Given the history of market manipulation from softwood producers in the Canadian provinces, and the strong incentive to under-value given the potential impact of such trades on stumpage, reporting of transactions after the fact by such companies provides little guarantee of true transparency.[1] Recent discussions with officials of major licensees have indicated that prohibiting such swaps (i.e., forcing such transactions into a market) would not be problematic for them.

Transparency is also important for reporting not only prices and volumes, but also species of wood.[2] This lack of transparency makes it easier for companies to overharvest high value species. High value species are often the most highly subsidized through the loop-holes in the administrative stumpage system that allow high-grading. Mandatory establishment of the annual

[1] Mitch Anderson and John Werring, *Stumpage Sellout: How forest company abuse of the stumpage system is costing BC taxpayers millions* (Vancouver: Sierra Legal Defence Fund, 2001.
[2] For example, new reporting requirements in BC's Forest Statutes Amendment Act, 2003, S.B.C. 2003, c. 32 would require only the records be kept and reported of the volume of timber harvested, not the species.

allowable cut on a species by species basis for each management unit (TSA or TFL) would help address this problem. Stumpage should be calculated and paid on a per species basis, not a blended basis.

For example, currently in B.C., when setting a stumpage rate for cutting permits (which may incorporate more than one cutblock), a single rate is determined based on the cruised value of the permit and appraised logging costs. While the stumpage rate is based on the species and grades present, it is effectively averaged over the cutting permit, meaning that the low value (or even "negative" value) of the bulk of the volume in the permit area is used to offset the high value of the most desirable wood. This results in manipulated low overall stumpage rates.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

SECTION I.B.2.b
APPLICATION OF PRICES OBSERVED IN INDEPENDENTLY FUNCTIONING MARKETS TO STUMPAGE SET ON THE ADMINISTERED PORTION OF A PROVINCE'S HARVEST

Summary of Comment: The policy bulletin should not include surveys of private transactions as a price reference.

Comment:

The policy bulletin allows the use of surveys of private transactions to identify the prices and costs in a reference market. We urge the DOC to remove any language that allows surveys of private transactions to be used in this fashion. In British Columbia for example, softwood companies are notorious for inflating supposed costs when such information is derived from surveys and is not based on actual evidence (in fact, reducing or eliminating these distortions was one of the objectives of the BC Ministry of Forests when it developed the CVPM and its associated "waterbed" approach). Other models, such as use of "harvest and haul" contracts have a much higher likelihood of generating reliable evidence about costs. These provide logging services in a representative selection of areas that are contracted on a competitive basis. We cannot stress enough that to determine the price payable to the Crown accurately, we need transparent indications of both the market value of logs and the costs incurred to remove the logs from the forest. This extends to planning and other costs.

SECTION III

CHANGED CIRCUMSTANCES REVIEW

Summary of Comment: The policy bulletin should include clear instructions as to required data and the evidentiary burden that must be satisfied, including documentation of potential "pass-backs" to industry through weakened regulations, failure to enforce laws or financial contributions in other areas. It should include a process for public notice of changed circumstances review initiation, public access to non-proprietary information in the changed circumstances review process, and public participation in decisions concerning changed circumstances review.

Comment:

To ensure that countervailable practices have ended, the Department must examine subsidy programs, regulatory cost reductions and the failure to enforce provisions, such as environmental laws. The Department should be wary of "pass-backs" of increased revenues or otherwise increased subsidies to the industry. Documentation of regulatory and other cost reductions should include environmental laws and operating regulations such as forest practices codes.

A changed circumstances review is dependent on accurate and timely information. Participation of members of the public in Canada and in the U.S., as well as of First Nations is critical for the Department to have and assess information about the complexities of provincial forestry systems. Public notice of changed circumstances review initiation will allow members of the public and First Nations to prepare for participation. Public access to non-proprietary information in the changed circumstances review process will allow members of the public and First Nations to assess the information provided to the Department of Commerce and identify relevant, additional information. Finally, a timely process for public participation in decisions concerning changed circumstances review will ensure that the Department receives relevant information from members of the public and First Nations in such reviews.

NRDC * Defenders of Wildlife * NWEA * WCEL * AWA
COMMENT ON SOFTWOOD LUMBER POLICY BULLETIN – August 8, 2003

Submitted By

_____

Susan Casey-Lefkowitz
Natural Resources Defense Council
1200 New York Ave, N.W., Suite 400
Washington, D.C. 20005
Tel: 1-202-289-2366
Fax: 1-202-289-1060
Email: sclefkowitz@nrdc.org

Defenders of Wildlife
1130 17th St. NW
Washington DC, 20036
Tel: 202-682-9400
Fax: 202-682-1331

Northwest Ecosystem Alliance
1208 Bay #201
Bellingham WA 98225
Tel: 360-671-9950
Fax: 360-671-8429

West Coast Environmental Law Association
1001-207 West Hastings St
Vancouver, British Columbia V6B 1H7
Canada
Tel: 604-601-2509
Fax: 604-684-1312

Alberta Wilderness Association

455 12 Street NW, Box 6398, Stn. D.

Calgary Alberta T2P 2E1

Canada

Tel: 403-283-2025

Fax: 403-270-2743