

Cabinet Submission – Request for Decision

Minister: Honourable Steve Thompson

Ministry: Forests, Lands and Natural Resource Operations

Date: 07/04/2012

Ministry Document #

Title: A Timber Supply for the Babine Forest Products Mill

Issue:

Hampton Affiliates Ltd. requires government assurance of an adequate, secure timber supply before it will invest in rebuilding the Babine Forest Products sawmill.

Request:

1. Cabinet endorsement of proposed actions to increase timber supply in several timber supply areas (TSA's);
2. Cabinet endorsement of a timber supply proposal to Hampton Affiliates Ltd.; and
3. Cabinet direction between 2 options to create certainty and security of supply for a new Babine Forest Products mill.

Implications and Considerations:

- Some actions add risk with regard to old growth timber conservation and will be controversial with the public, ENGO's, and perhaps some First Nations;
- Potential actions in visually sensitive areas will concern the tourism industry;
- Some enabling legislation will be required no later than Fall 2012;
- New investment of \$13.6 million/year required commencing in fiscal 2013/14;
- Some options and actions may have application in the Cariboo region, also facing timber supply shortages due to the pine beetle epidemic.

Background / Context:

Without mitigating actions, the timber supply in the Lakes TSA (Burns Lake) is projected to decline from the current level of 2.0 million m³/year to 0.5 million m³/year by approximately 2017. The lower level of timber supply is not adequate to justify a Hampton Affiliates investment in the range of \$80-100 million to rebuild the Babine



Forest Products mill. Hampton Affiliates has requested the province to commit at the end of April 2012 that 864,000 m³/year of secure timber supply will be made available to the company for a 15 year period after a new mill is built in 2014, and to describe the ways in which that supply will be made secure for Hampton Affiliates. First Nations are 11% owners of the Babine Forest Products mill and expect to receive through licenses a significant part of the timber supply.

If the timber supply enabled by the proposed options and actions results in a rebuilt mill, significant revenue benefits will accrue to the province over a 15 year period through worker income taxation, corporate taxation and incremental stumpage revenues. Incremental forest product manufacture will contribute a minimum of \$150 million/year to the provincial economic base. The local economy of Lakes TSA will capture most of the direct, indirect and induced employment resulting from the new mill. Approximately 2000 hectares of damaged Crown forest will be rehabilitated annually while generating raw material supply for, and employment in, the bioenergy industry. Implementation of the options and actions raises the level of risk to conservation of old growth timber and biodiversity. The part of the tourism industry dependent on maintaining certain highly visible landscapes free of extensive timber harvesting may be negatively impacted.

If the options and actions are not implemented, the timber supply will decline to 0.5 million m³/year during the period approximately 2015-2017 and nearly all of the diminished direct, indirect and induced employment based on that supply will move west to the Houston area and east to the Vanderhoof/Fraser Lake area with major adverse economic outcomes for the Burns Lake area.

Options:

Increasing Timber Supply

It is in the interest of all parties to maintain the current 2.0 million m³/year timber supply level in Lakes TSA for as long as possible, estimated to be until 2015-17 when the dead pine timber currently supporting the supply can no longer be used for lumber production. The actions proposed below would therefore take effect at that time, but not sooner. The following combined actions to increase timber supply in several TSA's to

make it possible to propose a larger timber supply to Hampton Affiliates are offered for Cabinet consideration:

Action 1: Maintain the short-term timber supply 200,000 m³/year above the sustainable level of 500,000 m³/year for 15 years after a new mill is built. The cost of this action is that mid-term timber supply during the period 2032-2072 would be 40,000 m³/year lower than would otherwise be the case. This action to enable a higher short-term supply would be a deviation from Chief Forester policy and practice in timber supply management. There is some risk that the independent Chief Forester of the day may not agree with this action, or of a legal challenge if he/she does. These risks may be partially mitigated by the issuance by the minister of a specific expression of government's social and economic objectives for the Lakes TSA.

Action 2: Use government economic policy supports for bioenergy to increase the timber supply by up to 250,000 m³/year. Large forest areas in the Lakes TSA contain a mix of live saw timber and long-dead pine that is not economic to harvest for lumber manufacture or bioenergy. The province could apply economic policy supports to make feasible the harvest of these forests with the result that the saw timber would flow securely to a rebuilt Babine Forest Products and the dead pine timber would flow to a suitable energy-from-biomass facility in the Lakes TSA. This action would also result in the rehabilitation of approximately 2000 hectares of beetle damaged forest annually. The 2 economic policy supports to be considered are:

- a) Expand the government program of silvicultural rehabilitation (the Land Based Investment Silviculture program) by approximately \$5.6 million/year (preliminary estimate), and apply the program to the subject forests with the result that both the dead pine and live saw timber can be economically utilised; or
- b) Work with Ministry of Energy and Mines and BC Hydro on a targeted energy pricing agreement with a suitable proponent to make harvest of the dead pine economic for bioenergy and enable the saw timber to flow to Babine Forest Products as a by-product of the bioenergy enterprise.



Action 3: Relax in several TSA's land use rules to conserve old growth timber, wildlife habitats and the visual character of some landscapes to increase timber supply. The province could take action to:

- Remove or relax old growth timber and moose management rules in the Lakes TSA to increase the timber supply by up to 99,000 m³/year.
- Remove or relax rules in the Prince George TSA, and potentially Morice TSA, to substantially increase timber supply (mainly in Prince George TSA).
- Enabled by increased supply in Prince George and Morice TSA's, mutually agree with Canfor, West Fraser and L&M Lumber to transfer their timber harvests in Lakes TSA to an adjacent TSA for a 15 year period. In approximately 2017, this action could retain approximately 216,500 m³/year of timber supply within the Lakes TSA for a Babine Forest Products mill.

Actions to take more risk with regard to old growth timber conservation or wildlife habitat will be controversial with the public, ENGO's, and perhaps some First Nations.

Opposition to changes will likely be strongest in urban regions, but will not be restricted there. The tourism industry opposes more timber harvest in visually sensitive areas, and the rural public is polarised on the issue. Deep consultation will be required with First Nations. The forest industry recommends a transparent, government-led public consultation on the issues. In the Morice TSA, the province has a government-to-government agreement with the Wetsetwen First Nation in land use planning matters which commits to establishing further constraints on timber supply, adding substantial complexity and potential legal risk to actions in the Morice TSA.

Action 4: Expand the forest fertilisation program to increase timber supply. A forest fertilisation investment program in Lakes TSA of \$3.06 million/year for 7 years commencing in 2013 would increase timber supply in the 2023-2029 period by 81,000 m³/year. The resulting timber supply creates an opportunity in 2023 to issue a new tenure in a manner that provides secure supply to Babine Forest Products. In the Prince George TSA, a program of \$4.8 million/year for 22 years would increase timber supply in the 2023-2045 period by 120,000 m³/year.



Action 5: Convert some existing licenses in Lakes TSA, and possibly other TSA's, to Tree Farm Licenses.

Tree Farm Licenses grant to a single licensee the right of exclusive timber harvest within a geographic area. This exclusive right sets the conditions for a dedicated licensee to apply a number of forest management actions/investments to increase timber supply over time (10-15 years) by about 10%. If Hampton Affiliate's current forest license is converted to a tree farm license, it is possible that the company could increase its secure timber supply by approximately 23,500 m³/year over a 10-15 year period. Pursuing this action would require enabling legislation, deep First Nations consultation and legally required public hearings.

If all of the foregoing options are implemented, timber supply in Lakes TSA between approximately 2017-2032 could result as shown below:

Base Timber Supply Without Actions to Mitigate Supply		500,000 m ³ /yr
Action 1: Maintain an Elevated Harvest Level for 15 Years		200,000 m ³ /yr
Action 2: Economic Policy Supports for Bioenergy		250,000 m ³ /yr
Action 3: Relax Land Use Rules in Lakes TSA		96,000 m ³ /yr
	Total for period 2017-2022	1,046,000 m ³ /yr
Action 4: Fertilisation Program in Lakes TSA	Impact during 2023-2029	81,000 m ³ /yr
Action 5: Hampton Affiliates Tree Farm Licence	Impact during 2023-2032	23,500 m ³ /yr
	Total for period 2023-2029	1,162,500 m ³ /yr
	Total for period 2030-2032	1,072,900 m ³ /yr

Creating a Share of Supply for Babine Forest Products:

From the total supply described above, the needs of 4 long-term license holders (Hampton Affiliates, West Fraser Timber, Canfor, L&M Lumber), the government BC Timber Sales Program, existing commitments to First Nations for new licences and small scale timber salvagers must be met. The following actions are proposed for Cabinet consideration to form the basis of a timber volume proposal to Hampton Affiliates at the end of April 2012:

Action 1: Express government intent to pursue all of the actions described above to increase timber supply, including a commitment to seek necessary funding from Treasury Board

Action 2: To provide certainty of supply from Hampton's long-term license, express an intent to recommend to the minister that the proportion of future supply allocated to such licenses remain the same as at present (43% of total supply)

Action 3: For the portion of total supply not allocated to other licensees, offer a commitment to negotiate with a single entity representing the Six First Nations in the Lakes TSA one or more Forest Tenure Opportunity Agreements and timber harvesting licenses that will include terms and conditions requiring that the associated timber supply will be made securely available to a new Babine Forest Products.

Action 4: Commit to good faith negotiations with West Fraser Timber, Canfor and L&M Lumber to transfer their timber harvests out of the Lakes TSA for a 15 year period commencing approximately 2017. Commit to negotiate with a single representative of the Six First Nations entity the same agreements as described in Action 3 above to license and supply an equivalent volume from Lakes TSA to a new Babine Forest Products mill.

Action 5: Make a commitment that, when incremental timber supply is available from the forest fertilisation program (2023) that a new tenure will be issued in the same manner as described in Action 3 above.

The above actions result in a 15 year supply for a new mill as described below:

Action	Hampton Supply Effect
Maintain a 43% supply allocation to long-term licenses	234,575 m ³ /year
New supply through First Nations partnerships	382,950 m ³ /year
Supply resulting from license transfers out of Lakes TSA	218,532 m ³ /year
Total Hampton Supply From Approx. 2017 to 2022	836,057 m³/year
Supply resulting from fertilisation and Tree Farm License	104,500 m ³ /year
Total Hampton Supply From Approx. 2023 to 2029	940,557 m³/year
Loss of supply when fertilisation program impact expires	-81,000 m ³ /year
Total Hampton Supply From 2030 to 2032	859,557 m³/year

Increasing Certainty and Security of Supply for Hampton Affiliates:

The volume proposal described above is less than the 864,000 m³/year request of Hampton Affiliates for most of the 15 year period. The likelihood that Hampton Affiliates will accept the timber supply proposal outlined above will be influenced by the degree of certainty associated with the supply. Two options are offered for Cabinet consideration to establish the degree of certainty and security of supply for a new mill:



Option 1: Rely on Existing Policy and Legislated Approaches:

Under this option the province would:

1. Issue to the independent Chief Forester a new expression of the government's social and economic objectives for the area and rely on him and his successors to implement the timber supply actions previously discussed over a 15 year period commencing in approximately 2017.
2. Rely on a series of ministers to maintain the share of the annual allowable cut allocated to licenses such as Hampton's over the same period.
3. Use current Forest Act provisions to issue direct award licenses to First Nations pursuant to new Forest Tenure Opportunity Agreements with contractual conditions that the timber volume be supplied to Hampton Affiliates.

Pros: No new legislation would be required except to enable conversion of forest licenses to Tree Farm Licenses.

Cons:

1. There is some risk of legal challenge to a statutory decision of the Chief Forester to maintain short term supply levels above the otherwise sustainable level.
2. Timber supply decisions of the Chief Forester must not be fettered. There is no guarantee that, over a 15 year period a series of Chief Foresters, perhaps with changing objectives of the government of the day, would fully recognise the timber supply actions previously described.
3. There is no guarantee that a series of ministers would hold the timber supply allocation to the long-term licenses such as Hampton's stable for a 15 year period.
4. Chiefs and councils, potentially with varied agendas, will change repeatedly over 15 years causing concern that contractual supply agreements will break down during the period. Government remedies (license suspension, cancellation and appeals) are time-consuming. Mill operations would be disrupted as they occur.



Option 2: Create Extraordinary Legislation to Add Certainty to Timber Supply Outcomes Over Time.

Under this option government would enact legislation to enable a set of specific actions to add certainty to the supply of timber to a new Babine Forest Products mill over a 15 year period. Such a piece of legislation could:

1. Suspend current *Forest Act* provisions for the Chief Forester to set the annual allowable cut, and the minister to make license apportionment decisions, in the Lakes TSA. Vest these functions with the Lieutenant Governor in Council;
2. Such legislation could prescribe timber supply arrangements between First Nations and Hampton, moving that matter out of the contractual realm;
3. Empower government with a legislated, rapid remedy in the event of a relationship breakdown between First Nations and Hampton Affiliates to ensure mill supplies are not interrupted;
4. Consideration could be given to new government powers to direct award one or more licenses to an entity other than a First Nations entity, such as to a partnership between First Nations, a non-aboriginal community entity and Hampton Affiliates.

Pros:

1. The inherent uncertainty that comes with the independent exercise of discretion by the Chief Forester and minister is avoided;
2. There would be much more certainty that disputes between First Nations and Hampton Affiliates could be quickly addressed in the interests of continuity of mill operations;
3. Concerns in the non-aboriginal community that First Nations have an extraordinary level of control over the local economy may be alleviated;
4. Placing some legislated controls on First Nations-held tenures in Lakes TSA may help manage high expectations for large timber volumes by First Nations in other parts of the province.



Cons:

1. Some stakeholders will likely assert that the forest stewardship oversight of the Chief Forester has been improperly set aside in favour of economic interests;
2. First Nations will object that government is exercising too much control over their commercial interests in timber;
3. A future government could repeal the legislation.

Fiscal Impacts:

Preliminary estimates of fiscal impacts for the first 3 years of 2 investment initiatives within the Land Based Investment Silviculture program, increasing timber supply through forest rehabilitation and forest fertilisation, are outlined below. These programs are proposed to run beyond the current fiscal plan as outlined earlier in this submission.

Fiscal Year	Program	FTE's	Operating (\$ millions)	Capital	Total for Year (\$millions)
2013/14	Fertilisation	?	8.0	0	13.8
	Rehabilitation	?	5.6	0	
2014/15	Fertilisation	?	8.0	0	13.8
	Rehabilitation	?	5.6	0	
2015/16	Fertilisation	?	8.0	0	13.8
	Rehabilitation	?	5.6	0	
Totals		?	40.8	0	40.8

Due to past budget reductions in the Land Based Investment program the expenditures outlined above cannot be accommodated re-prioritisation, reductions or cessation of other activities, necessitating an addition of funding to the program. A funding decision will be required prior to summer 2012 to enable field planning of projects to take place before fiscal 2013/14.

The effect of the investment program above is to generate 451,000 m³/year of saw timber in the Lakes and Prince George TSA's for each year of investment. The investment generates extraordinary returns to the provincial economy in terms of employment, government revenues and contribution to the provincial economic base.



Economic Impact Type	Impact	\$ Value Millions
Direct Forest Employment*	221	
Provincial Gov't Personal and Corporate Income Tax Paid per Direct Forest Employee**	\$22,500/employee	4.97
Stumpage Revenues***	\$x/m3	X.X
GDP Generated per Direct Forest Employee**	\$190,000/employee	35.36
	Total	

*Central 1 Credit Union, July 2010

**Business Council of BC and Council of Forest Industries, December 2007

***Ministry of Forests, Lands and Natural Resource Operations, April 2012

The foregoing does not include the economic benefits that will accrue in the bioenergy sector or reforestation industry sector.

Policy:

Holding timber supply levels 200,000 m3/year above the analysed sustainable level for a period of time is a deviation from past timber supply policy. There is some risk of a legal challenge if such a decision is made by the Chief Forester.

Legislation:

1. Forest Act amendment to enable forest license conversion to tree farm licence.
2. Dependent on Cabinet decision, new legislation to add certainty to timber supply.

Stakeholder and Citizens:

Deep consultation will be required with First Nations related to issues of relaxing land management rules to increase timber supply. The province has a government-to-government agreement to work with the Wet'suwet'en First Nation in land use planning matters in the Morice TSA. Public consultation will be required regarding changes to Land Use Act and Government Action Regulation orders that will be necessary to give effect to changed land management rules.

Hypothetical Apportionment Scenarios – Lakes TSA

Tenure Type		AAC 1,049		
		AAC 2.0	Scenario 1: Maintain Current RFL Apportionment Pattern (43% of 1,049 million)	Scenario 2: Change RFL Apportionment Pattern (to 43% of 0.50 million m3 reference forecast)
Replaceable FL	Apportionment	868,604 (43% of 2.0)	*451,107 (Down 48%)	**215,000 (43% of 0.5)
	Committed	868,604	451,107	215,000
	Balance	0	0	0
NRFL	Apportionment	1,467,057	***362,950	***599,057
	Committed	458,301	362,950	599,057
	Balance	+1,008,756	0	0
BCTS	Apportionment	714,873	199,943 (BCTS base - 48%)	199,943 (BCTS base - 48%)
	Committed	714,873	199,943	199,943
	Balance	0	0	0
FS Reserve	Apportionment	35,000	35,000	35,000
	Committed	0	0	0
	Balance	+35,000	+35,000	+35,000
Totals	Apportionment	3,085,534	1,049,000	1,049,000
	Committed	2,041,778	1,014,000	1,014,000
	Balance	1,043,756	35,000	35,000

Volume in WFM/Canfor/L&M licenses transferred to other TSA's (analogous to undercut vol). Could be tenured through FTOA-based NRFL to be secure supply for Hampton for 15 years.

- *Hampton share would be 234,575 m3/year in secure replaceable forest license
- **Hampton share would be 111,800 m3/year in secure replaceable forest license
- ***This apportionment could support NRFL in the low volume stands and remainder in conventional sawing stands. Could be tenured through FTOA-based NRFL to be secure supply for Hampton while satisfying the '300,000 m3/year promise' to First Nations.

Secure Supply For Hampton:

1. If Canfor/WFM/L&M licenses are not transferred out of the Lakes TSA, Hampton's secure supply under these scenarios would total either 597,525 (Scenario 1) or 710,257 (Scenario 2) m3/year for the period approximately 2017-2032. If the other licenses are transferred out, the secure volume for Hampton rises to 814,057 m3/year under both scenarios;
2. When the fertilised stands become harvestable in 2023, a new opportunity license for 81,000 m3/year for 7 years could be awarded in a manner to be secure supply for Hampton for the period 2023-2029;
3. If Hampton is awarded a Tree Farm License, any additional timber supply they are able to generate on the license would be secure supply. A metre-for-metre conversion of their mid-term replaceable forest license volume would give them a TFL with AAC of 234,575. A 10% increase in timber supply on such a TFL would add 23,457 m3/year to their secure timber supply.