

A.Executive Summary

This report presents the results of an Opportunities Review conducted over the July to October 2012 period. The intent of the Opportunities Review was to strengthen BC Timber Sales' (BCTS) ability to support provincial priorities, to deliver on its mandate, and to build commitment to the organization within government and among all customer segments. The recommendations aim to better locate the organization within the broader policy framework and priorities the province has for the sector, and to enhance the ability of the province to leverage the program to continue to promote investment opportunities, innovation and job creation. The information and recommendations contained in this report are intended to support BCTS' commitment to continuous improvement.

BCTS was established in 2003 to offer fibre to the market through a competitive auction system. The competitive auction system provides the basis for collecting the market price information used to drive stumpage rate determinations, and it continues to provide a credible foundation for setting stumpage rates at levels consistent with forest product markets. The importance of providing credible pricing data is underscored by the most recent arbitration ruling by the London Court of International Arbitration (LCIA) where the BCTS model served the Province in successfully countering claims from U.S. based interests that BC's forest sector is unfairly subsidized. The forest sector avoided compensatory export taxes in excess of \$300 million as a result.

With responsibility for close to 20% of the province's apportionment, a substantial operational presence in all areas of the province, and offices in 33 communities, BCTS has an impact on all facets of the forest sector and the local and regional economies that rely on the industry as a wealth generator. In terms of direct impacts, the value of services that BCTS has secured through local suppliers since 2003 is in excess of \$900 million. It has brought 95 million cubic metres of timber to the open market and generated over \$350 million in net revenues through its timber sales. More important, since the pricing mandate requires it to test markets and respond to customer needs even in depressed market conditions, it had a stabilizing influence on local businesses and regional economies during the recent downturn across the province. While many major licensees stopped doing the development work needed to bring their own timber to market and curtailed production, BCTS did not. BCTS reduced its development work and the volume of sales to adjust to weak markets, but provincially, the BCTS maintained a strong market presence. During the market downturn, BCTS achieved a stronger revenue flow through its timber sales than those produced through other forms of tenure, generating 80% of the province's stumpage revenue from just 20% of the provincial forest land base.

The forest sector and those communities that depend on it as a wealth generator are facing great change and uncertainty. In the wake of the uplifts implemented to bring Mountain Pine Beetle (MPB) affected stands to market and put the land back into production, many regions are seeing a more constrained timber supply and growing challenges in securing the fibre to meet existing needs and emerging demand by First Nations, communities and some major licensees. While the United States is still a key market for softwood exports, it has receded in importance with growing demand in other markets. Regardless, BCTS' pricing mandate now and into the future is an important consideration in any future policy discussions. There are strong advocates for very different visions of the future of forestry and the regional, provincial and international value chains that BCTS feeds into. The organization is not immune to these issues and is feeling the push and pull of different interests. Along with most companies in the forest sector, BCTS has had to adjust its business practices to address the decline in profitability associated with the forest sector downturn following the global financial crisis. With improvements in market conditions in the fall of 2012 and increased product demand, BCTS and the broader sector have seen a return to greater profitability.

Purpose of the Review and Approach

BCTS initiated a review tasked to:

- Report on benefits and assess key areas of strength, successes and challenges associated with its programs;
- Identify the factors having an impact on BCTS and associated risks and opportunities; and
- Develop options and recommendations to act on identified risks and opportunities.

This report presents the results of that review and supporting discussions with over 120 customers, partners, stakeholders and staff including a survey of all BCTS staff (conducted July-October 2012 with an approximate response rate of 70%).

The Case for Change

BCTS is recognized generally as a valuable and dependable fibre supplier to the open market that is balanced, sustains opportunities for new entrants into the forest sector, and keeps options open for the province at a time of considerable uncertainty. The risks and challenges that the organization faces are being managed well given the limited powers and authority that the organization has under its current governance structure and legal framework. The organization has generally delivered on its mandate, providing a stabilizing influence to customers with reliable product delivery in good and poor market cycles.¹

BCTS provides fibre supply solutions that can effectively serve the needs of businesses working both within international value chains and small independent businesses working within local and regional markets. The development of more competitive fibre markets increases the level of benefit from every tree cut. By promoting regional and provincial conditions that allow fibre to move to its highest and best use, BCTS can work effectively with government partners to develop new opportunities for First Nations and communities, and to sustain the conditions necessary to foster innovation, investment and job creation. Improving access to fibre on an open market for new entrants, and proactively and collaboratively working with local governments, First Nations, business and government partners, BCTS can broker fibre solutions that contribute to local, regional and provincial economies.

Where action can be taken now: A range of actions are proposed that are intended to deliver tangible results in the short-term, and which focus mostly on processes and products currently delivered by BCTS. While the actions will be familiar to most within the organization and many business areas are already embracing them, their cumulative impact signals a significant shift in how the organization operates and engages the world around it. In particular, the recommendations promote:

- The development of stronger customer focus and greater responsiveness to customer needs;
- Actions to develop stronger support for BCTS across all key relationships, including First Nations, communities, licensees and fibre processors, market loggers and brokers, suppliers who provide services to the organization, and key government partners such as the Ministry of Forests, Lands and Natural Resource Operations (FLNRO) and the Ministry of Aboriginal Relations and Reconciliation (MARR);
- Work with key partners to leverage BCTS to deliver fibre supply solutions that effectively support provincial priorities while limiting risks to the apportionment and ability to meet pricing, revenue and fibre supply targets;

¹ BCTS has successfully delivered on the majority of its mandate, save and except a few business areas which accumulated an undercut (i.e., they did not meet targets with respect to the volume of fibre offered to the market). At the time the report was completed BCTS was taking measures to address this issue.

- The development of a better work environment and more rewarding careers within the organization.

The longer-term: In the longer-term, the recommendations lead to more fundamental change within BCTS. The recommendations build towards change in the government structure and legal framework to enhance the ability of the organization to act as a full service, professional forest land manager and position it more strongly to succeed. In particular the recommendations are designed to:

- Increase the capacity to develop and support a financial plan that promotes profitability in the short and long-term and bring stability to how the organization operates;
- Enable the purchasing and trading of volume and securing operating areas through greater use of area-based tenure to provide the province with a sustainable and more diverse portfolio of forest lands managed by BCTS (in trust for the people of British Columbia) that provide opportunity to investors and innovators – First Nations, communities and private sector businesses alike; and
- Create an organization with the ability to provide the range of benefits, competitive wages and work environment that attracts and retains the talent needed to spur innovation and drive BCTS forward.

Key Themes and Future Challenges

Relationships with First Nations and Communities: Many of the challenges facing BCTS relate to broader decision-making processes that must consider a range of competing interests at the regional or local level. There is a general perception that the organization has not worked hard enough to develop effective relationships and to broker regional fibre supply solutions that respond to the needs of communities and First Nations and the benefits that BCTS can bring to First Nations and local government are not sufficiently understood. At the same time, there is a strong perception held by some within and external to BCTS that it risks diluting its mandate by investing in partnerships and that more effort is needed to communicate to decision makers the costs associated with drawing on the apportionment to provide replaceable tenures to communities and First Nations. Regardless, opportunities exist to secure fibre through mutually beneficial business arrangements with some First Nation entities.

Security over the Apportionment, Operating Areas and Timber Supply Constraints: Competing demands and pressures for tenure are resulting in the reallocation of parts of BCTS' apportionment to replaceable licenses to meet First Nations, community or other needs. Unless carefully implemented, reallocation could pose a risk to the pricing mandate. This may represent a financial risk for BCTS as well since they must continue to develop a standing timber inventory (STI) at considerable cost.

Competitiveness of Fibre Markets: All customer groups note the need for BCTS to continue to reach out to customers, work harder to identify their fibre needs, and commit to meeting those needs through the ongoing development and refinement of the products and processes used to bring fibre to market. At present, the range of products and the manner in which they are delivered constrain the ability of some customer segments to access fibre. Customers identified concerns with the Category 2 (Cat 2) program. Opinions were mixed with an even split between those who saw no benefit, and those advocating for it. Advocates saw the need to strengthen the program to more effectively meet the needs of independent mills. Some called for a range of different products (i.e. licence types) such as non-replaceable forest licences (NRFL) types of arrangements, and flexibility within the products such as highly modified Cat 2 requirements to respond to the needs of specific proponents or First Nations. Others advocated for greater BCTS involvement in the development of regional log merchandizing centres in order to meet the demands of independent mills (without replaceable tenure) who rely on a steady supply of fibre and have no interest in the harvesting side of the equation. Beyond this, in the interests of continuous improvement, a range of opportunities to streamline or improve the bidding process, bid packages, TSL contract requirements, and the structure of specific types of sales to improve their marketability were offered.

Responsiveness to Customer Needs: BCTS serves a diverse customer base with sometimes very different needs and expectations. A diversity of fibre supply strategies exist in today's forest economy and BCTS is part of the mosaic of forest land managers that supply the market. There is a perception among some of the larger fibre processors that, as BCTS continues its mandate to mirror the market and behaviour of major licensees, improvements could be made relative to the timeliness of delivering the apportionment to the market. This is more prevalent on the Coast, the Cariboo-Chilcotin, and portions of the Prince George Timber Supply Area. The view among many independent fibre processors is that the Cat 2 program remains essential to securing fibre supplies and that BCTS could be using it more effectively to meet the needs of some customer segments. Customers value the access they have to BCTS and the level of communication that exists. However, a pervasive theme running through the consultations is that BCTS has not made clear commitments to its customer segments, and that it should communicate more effectively to understand and respond to them.

BCTS Staff – Human Resources: At the staff level, there is a general perception that BCTS is less effective than it could be and that its relevance to decision makers is weakening. Staff are reporting a loss of engagement and slipping morale within BCTS. The flat organizational structure, while viewed as efficient, limits career opportunities. With wage rates that aren't viewed as competitive with the private sector and some parts of government, staff see a growing problem in attracting and retaining staff. At the same time, there is general support for the organization, its strong operational focus and clear mandate. Staff are concerned about the future of the organization and its ability to attract, inspire and retain skilled and experienced people, yet they are also enthusiastic, proud and loyal.

Suppliers: BCTS depends on a range of suppliers to bring its fibre to market in a timely fashion and to meet post-harvest obligations. Engineers, foresters, road developers, multi-phase and silviculture contractors, and other consultants support the work of every business area. Staff identified challenges in accessing suppliers and these shortages are leading to delays in bringing some sales to market. In some areas, BCTS staff have begun to undertake work traditionally done by contractors to make up for the short-fall. Suppliers and staff identified a range of factors that have contributed to the shortages: more attractive terms provided by major licensees where the work can be done more efficiently and higher rates and per diems can be realized (likely to further draw down on the pool of suppliers as the market picks up); the procurement policies of BCTS which they feel over-emphasize lower price (leading to challenges for both staff and suppliers who sometimes find it hard to secure the best people at the best price); and the structure and complexity of contracts including the practice of bundling up work (e.g. multi-phase) which has effectively created a challenging barrier to entry for many smaller companies that could otherwise be drawn upon.

Administrative and Organizational Structures: The operational realities facing many business areas have changed significantly since the launch of BCTS in 2003. Timber supply constraints, treaty negotiations, forest health, and changing market demands have fundamentally altered the current or projected workload within some business areas. While customers, partners and stakeholders generally did not see a need to alter the administrative and organizational structure (focus was on output, not on the process to deliver the output), considerable concern was expressed at the management and staff level in some business areas that the current structure was leading to inefficiencies, and declining staff morale. On the other hand, some business areas expressed support and satisfaction with the current structure. As well, with the formation of FLNRO there is concern, albeit limited, over the extent to which the business areas align sufficiently with the administrative boundaries of the broader ministry and the extent to which this is inhibiting communication and effective issues management. This is particularly true in the Prince George TSA where two business areas co-exist but are measured as one through AAC partition requirements.

Governance Model and Legal Framework: The last several years have challenged the organization and the strengths and vulnerabilities associated with the current governance model and legal structure have come into focus. While opinions are mixed, many staff believe the ministry structure is a significant constraint to developing an effective strategy for attracting and retaining skills and experienced staff. In addition, many have noted that the current financial model has made it difficult to make investments into the STI and manage the organization under weak market conditions. The mixed success in engaging First Nations and doing what is needed to secure operating areas have also been attributed in part to limitations associated with the current legal framework. In spite of these challenges, the

organization has in many respects been successful as a net revenue generator over the long-term, as a fibre supplier, and providing the basis for meeting the province's obligations under the terms of the Softwood Lumber Agreement.

Recommendations

The recommendations are summarized below in Table 1 and organized around eight key themes that emerged through the review. For each recommendation, a range of potential implementation options have been proposed to strengthen the performance of BCTS in the short-term. Longer-term actions have also been proposed. These require a higher level of investment, often require legislative or regulatory changes, entail a shift in the mandate of the organization, and increase its legal authority. Collectively, the recommendations and implementation options are designed to take the organization from a focus on:

- Delivering the apportionment to the market to responding to customer needs;
- Pushing back against competing claims on the apportionment to brokering better solutions that enhance the province's capacity to achieve long term strategic interests;
- Short-term and responsive planning to longer-term planning supported by robust information;
- Struggling within the constraints of the current organization to changing the rules;
- Managing BCTS risks to sharing risk with registrants;
- Staff doing the best with what they've got to a fully empowered and engaged team that is well supported, delivers results, and is rewarded appropriately; and
- Pursuing program objectives through individual business areas to collaborating across the organization to provide corporate solutions that effectively, efficiently and consistently respond to customer needs.

Fulfilling the pricing and costing mandate is just one part of a much greater range of benefits that is delivered by BC Timber Sales. The recommendations are intended to further enhance the effectiveness of BCTS and maintain opportunities for new entrants and long-standing businesses that collectively are the building blocks of prosperity in British Columbia's emerging bio-economy. This ultimately is the foundation of BCTS and the recommendations underscore the importance of these outcomes.

Table 1: Summary of Recommendations, Expected Benefits, Supporting Actions and Timing

Theme	Recommendations and Benefits	Short-term Options Within the Mandate	Longer-term Options
<p>1. Meaningful Relationships with First Nations and Communities</p>	<p>1. Increase efforts to build awareness and understanding of the BCTS Program.</p> <p>2. More effectively leverage BCTS to create local partnerships that provide mutual benefits.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • <i>Reduced risk to apportionment</i> • <i>Increased planning capacity</i> • <i>New potential revenue streams</i> • <i>Increased support for BCTS</i> • <i>Stronger corporate solutions and support for FLRNO and provincial priorities</i> 	<p>More effectively engage First Nations, communities and local government to improve understanding and awareness of the benefits BCTS creates and can provide at the local level.</p> <p>Where there is a sound business case for doing so, develop “business to business” relationships with First Nations, local governments and existing licensees to pursue regional fibre supply opportunities.</p>	<p>Provide leadership in brokering local and regional fibre supply solutions including B2B relationships with communities, First Nations and government partners.</p> <p>With FLNRO promote tenure agreements with First Nations that make volume available through the BCTS auction system.</p> <p>Promote revenue sharing opportunities and mutually beneficial social, skills, and business capacity enhancement among First Nations.</p> <p>Pursue joint area/volume based tenures with First Nations and communities.</p>
<p>2. Stewardship and Sound Forest Management</p>	<p>3. Strengthen operating area security.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • <i>Stewardship reputation is enhanced</i> • <i>Pricing mandate is protected</i> • <i>Reduced risk to investment on the land</i> • <i>Financial and resource security</i> 	<p>Gather operating area information to verify timber supply and use baseline data to spatially identify economic fibre volumes.</p> <p>Support the Ministry (FLNRO) in its Timber Supply Review and AAC determinations to ensure that the apportionment is in line with what can be supported by operating areas.</p>	<p>Promote forest estate planning in collaboration with key customers and partners.</p> <p>Evaluate operating areas and adjust where necessary to maintain sustainability and the quality of pricing and costing information.</p> <p>Purchase volume, explore opportunities to purchase or acquire replaceable tenures (volume or area based) to support the mandate of BCTS.</p> <p>Protect BCTS operating areas through changes to existing legislation.</p>
<p>3. Responsiveness to Customer Fibre Needs</p>	<p>4. Develop fibre supply plans in the context of a market trends and customer needs and adopt a longer planning horizon.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • <i>Strategic approach to developing STI</i> • <i>Enhanced quality of customer service</i> 	<p>Develop service strategies by customer segment.</p> <p>Develop supporting performance targets and hold TSMs accountable for them.</p> <p>Develop an annual sales schedule in each business area that is governed by customer needs and provides for an even flow of fibre.</p>	<p>Develop and communicate an annual three year market outlook and five year fibre supply strategy. The strategy should consider market needs by customer segment and should include a communication plan targeting customers and partners.</p>

Theme	Recommendations and Benefits	Short-term Options Within the Mandate	Longer-term Options
4. Competitiveness of Fibre Markets	<p>5. Develop timber sale licences to be more responsive to each customer segment.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • Broader bidder pool • Better customer service • Stronger bidder management of risks which should result in more informed bidder behaviour 	<p>Maintain continuous improvement process to ensure the quality, consistency and accessibility of information supporting bid packages and administrative standards.</p> <p>Seek options to improve bidder access to the tendering process.</p> <p>Develop specific product offerings to better engage all customer segments and broaden the pool of potential bidders.</p> <p>Market niche components within stands and smaller sales to target needs of smaller fibre processors including cut timber and promoting log merchandizing if a sound business case exists.</p>	<p>Support industry in reviewing ministry policy where changes are necessary to reflect evolving operating conditions.</p> <p>Explore opportunities to market volumes through direct awards or through B2B relationships to support government objectives and regional priorities.</p> <p>Develop policies and guidelines defining the role and approach BCTS will take to respond to the needs of smaller independent fibre processors (including independent primary breakdown facilities without major quota including options to promote pilot log merchandizing centres and harvest and haul contracts in areas where demand exists.</p>
5. Engaged, Skilled and Experienced Staff	<p>6. Develop a Recruitment, Retention and Succession Strategy.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • Increased staff morale and engagement • More effective use of staff skills/talents • Increased staff continuity 	<p>Develop and Implement succession plans.</p> <p>Promote mentoring and development programs to enhance career advancement within BCTS and explore opportunities to better utilize the skills and expertise within the organization.</p> <p>Affirm government commitment to BCTS.</p>	<p>Review job descriptions, salaries and benefits, and align with those of competing employers.</p> <p>Improve the ability to more effectively utilize the core skills of existing employees.</p> <p>-</p>
6. Cost-effective Supplier Relationships	<p>7. Increase the pool of qualified suppliers serving BCTS.</p> <p><i>Benefits:</i></p> <ul style="list-style-type: none"> • Assurance that work will get done • Higher quality suppliers • Greater flexibility and efficiency in project delivery 	<p>Broaden the supplier pool, improve its quality and increase value for money.</p> <ul style="list-style-type: none"> • Remove unnecessary barriers to entry and draw more effectively on smaller firms. • Seek alternatives to least cost and other procurement tactics. • Use internal staff when the business case warrants it. 	<p>Consider direct awards to enhance First Nation and community relationships.</p> <p>Review project requirements and standards for closer alignment with industry practices.</p> <p>Develop shared functions to serve regions and to deliver services internally to augment supplier capacity.</p>
7. Administrative and	<p>8. Align organizational structure and functions with changing timber supply conditions and customer locations, and promote</p>	<p>Promote sharing of staff and resources between business areas.</p>	<p>Periodically review business area timber supplies and structure to maintain or strengthen the ability</p>

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Organizational Structure	<p>collaboration between business areas.</p> <p><u>Benefits:</u></p> <ul style="list-style-type: none"> • <i>More effective management of internal costs; more efficient organization; better service</i> 	<p>Promote communication and collaboration between business areas and consistency in processes, practices and products to optimize efficiency and consistency in customer service.</p> <p>Undertake a timber supply review of each business area and realign boundaries or amalgamate business areas where necessary to maintain business functionality.</p>	<p>to manage risks and achieve performance targets.</p> <p>Where it makes business sense, continue to share resources (staff capacity and technology) between business areas.</p>
	<p>9. Promote collaboration with FLNRO to achieve mutual objectives and protect the integrity of the mandate.</p> <p><u>Benefits:</u></p> <ul style="list-style-type: none"> • <i>More effective B2B partnerships</i> • <i>Effective collaboration within FLNRO</i> 	<p>Strengthen communication and collaboration between Timber Sales Managers and District Managers to support issues management.</p> <p>Strengthen relationship between BCTS and Timber Pricing Branch staff (including professional reliance) relative to timber pricing and appraisal submission requirements.</p>	<p>In collaboration with FLNRO, promote the ongoing development of BC’s forest policy framework and clarify respective roles between BCTS and other partners.</p> <p>Expand BC Timber Sales role to assist FLNRO service delivery.</p>
8. Governance Model and Legal Framework	<p>10. Increase the capacity and ability of BC Timber Sales to fulfill its mandate by increasing the control and flexibility it has to make decisions and implement them.</p> <p><u>Benefits:</u></p> <ul style="list-style-type: none"> • <i>More effective B2B partnerships</i> • <i>More effective recruitment and retention</i> • <i>More flexibility in financial management</i> 	<p>Amend the Special Account to enable business to business relationships and development of solutions that are outside of the core business.</p> <p>Identify legislative or other amendments to the special account that are required to provide for revenue sharing and account management outside the current parameters.</p>	<p>Assess the business case for adopting a new governance model and legal framework that considers the need for:</p> <ul style="list-style-type: none"> • A financial model that enhances efficiency and cost effectiveness over the economic cycle. • Sufficient control over HR decisions to sufficiently recruit, reward, develop and retain staff. • Stronger B2B relationships with First Nations and local governments.