LOGGING RATE NEGOTIATION: WHEN DAVID MEETS GOLIATH

By TLA Editorial

In a government press release on April 30, 2014, Premier Christy Clark said, "BC is on the right path to bring home the generational opportunity of LNG—an industry that will create 100,000 jobs and enough revenue to eliminate our debt." Rich Coleman, Minister of Natural Gas Development went on to note that "By supporting the development of this new export industry, we are creating unprecedented economic opportunities for the people of British Columbia."

The provincial government knows that the increased use of natural resources, like LNG, will strengthen the provincial economy and provide people in rural communities with jobs and infrastructure, a core objective in promoting the use of our natural resources globally.

But while LNG may turn out to be a resource that benefits communities, the same cannot be said for the forest industry where consolidation of harvesting rights and forest policy changes have allowed some to benefit while others pay a price.

We all know the background now. A global economic recession led to contractors accepting lower rates in order to survive, rates that have not rebounded with markets. As discussed by a group of veteran loggers at the Interior Logging Association (ILA) convention this past spring, "Everyone took a hit, but some say the hardest hit were BC's logging contractors."[1]

On the other side of the coin, market improvements and growing demand for forest products has led to significant profits for the major licensees.

Western Forest Products reported 2013 EBITDA (adjusted) of $129 million. Q1 of 2014 saw adjusted EBITDA of $32.8 million.[2] With lumber shipments of 218 million board feet (estimated to require 780,000 cubic metres of logs) and log shipments of 581,000 cubic metres, a total of 1,361,000 cubic metres of logs were processed to generate the average adjusted EBITDA, or an estimated $24 per cubic metre of log processed and sold. The trend continued into Q2 with a reported adjusted EBITDA of $40.9 million[3].

Interfor saw similar results, although their operations are not restricted to BC. Their 2014 Q1 adjusted EBITDA was $39.2 million on lumber sales of 439 million board feet[4] , estimated to require 1.6 million cubic metres of logs, plus log sales of 398,000 cubic metres. This equates to an adjusted EBITDA of an estimated $19 per cubic metre of log processed and sold. Interfor's Q2 of 2014 results were even better.

Canfor too was profitable, although like Interfor their operations are not restricted to BC. For 2013 Canfor reported an operating income of $285 million for their lumber sales alone on approximately 4.7 billion board feet of lumber shipments.[5] This equates to an estimated $17 per cubic metre of log processed into lumber. Profits continued into 2014 with 2014 Q2 EBITDA of $141 million.

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For coastal contactors, however, the story is much different. Research done in late 2013 showed more than 25 logging contractors had to seek insolvency protection and/or were forced into bankruptcy in the last few years and more than 10 companies faced rate mediation or arbitration as a result of an inability to negotiate improved rates for work with their employers. Both trends have continued into 2014.

Ironically, this record of struggling contractors, primarily as a result of unsustainable rates comes at a time when the *BC Forest Sector Labour Market & Training Needs Analysis*, completed in October 2013, projects 4,700 job openings between now and 2022 in the coastal forest industry alone. Logging contractors employ a significant number of people in the industry and if they cannot afford to hire and train the needed people, it puts the entire strategy to attract workers and the industry as a whole at risk.

So what is really going on here? A recent discussion with a group of coastal contractors reveals some interesting perspectives. Many believe that the core of the issue rests with the 2003 coastal restructure which allowed consolidation of the licensees that has created an unequal playing field when it comes to contract rate negotiation. There are simply fewer companies with which to do business and those who control the resource are successfully keeping rates artificially low.

Contractors were weakened through the recession and are being forced to continue to accept rates that cannot sustainably support their businesses. At the same time, there are increased costs for fuel, steeper ground that requires more expensive logging techniques, repair or replacement of "tired iron" and increased costs to ensure safe operations, recruitment and training, none of which are typically acknowledged in rate discussions.

A case in point is the unfortunate circumstances of Malaspina Enterprises, an otherwise hard working coastal contractor that was forced to seek insolvency protection and make a proposal to its creditors to keep from going bankrupt in the spring of 2014.

In the Notice of Proposal to Creditors for Malaspina Enterprises[6] (the Notice), it was stated by the trustee that: "The company began experiencing financial difficulty in 2008 with the decline of the forest industry in British Columbia. During that time, logging contractor rates plummeted as contractors struggled to obtain work and started to underbid jobs. Low bidding, high labour and operating costs have led to declining gross margins and negative cash flow. Although the company continued operating, they remained unprofitable for the last 4 years."

The Notice went on to detail the 49 unsecured debtors that were owed $2.5 million accrued by Malaspina, many of which were local community businesses that tried to support Malaspina as it struggled with low rates. A community-based traffic control firm, a wire rope firm, other logging contractors, equipment suppliers, fuel suppliers, tug boat service providers, truckers, an auto repair shop, a crane company, they all had to pay a price when Malaspina sought insolvency protection as the eventual settlement proposal agreed to by the debtors did not provide sufficient funds to cover all debts completely. Some were paid as little as $0.12 per dollar of debt owed to them.

And there are other similar stories across the coast. Kip Brown Trucking's low rate driven insolvency ($1.45 million in unsecured debts to 45 creditors) was compounded as noted by the trustee since: "In 2010 fuel prices soared and contracts the company previously bid on were non-negotiable for increasing fuel costs."[7] Clayoquot Forest Management Ltd. in their Notice of Proposal to Creditors owed close to $1.6 million to 51 creditors and Cold Stone Logging Ltd. in their proposal listed 93 creditors who were owed $1.5 million.

One might suggest that the continued use of contractors in this poor financial situation, effectively transferred wealth from the contractors and small community businesses that tried to support the contractors to the major companies that used their services, now that we have seen the outcome of the various insolvency proposals.

As previously stated by Dwight Yochim, a past TLA Executive Director, "People knew these companies were in trouble. They knew the rates were unsustainable. …If logging companies knew, the licensees must have known."[8]

That said, many community-based businesses provided credit as they endeavoured to operate with low rates, only to get burned in the end.

To make matters worse, the licensees continue to try to impose these types of rates on the remaining contract logging industry by suggesting that they are the prevailing market rate. One has to ask if rates that assume the need for ongoing losses that are inevitably borne by local community businesses via insolvency, really reflects BC's logging "market."

We all operate within the current legislative and regulatory framework that unfortunately and inevitably lead to contractor insolvency; however, should we as a community be supportive of those rates that reflect "the market" and all contractors should support them? If so, then it means that we must also accept that the contractors, and by extension the small community businesses who are inevitably damaged when they are caught in an insolvency proposal, should be burdened with funding licensee operations.

So what has this continued trend resulted in other than the profitable use of a public resource by the licensees?

Utilization of public natural resources to create "economic opportunities for the people of British Columbia," as stated by Rich Coleman, should not be limited to those who achieve control of the resource.

The difficulty in operating their business with unsustainable rates has forced many contractors to downsize or to turn down new opportunities that they would otherwise try to secure. Many simply cannot afford to invest in new equipment or to pay the costs to train new recruits to work and operate equipment safely within the current rate environment. The last thing any contractor wants is an injury or fatality. This trend does not bode well when the need to attract 4,700 new recruits to this industry looms on the horizon.

Even the United Steelworkers recognized the significant impacts this issue can have on their members when they recently ratified their agreement with Western Forest Products (WFP). "The agreement offers members protection when working with contractors. The company (WFP) agreed to implement holdback provisions if any of their contractors become delinquent in health and welfare or pension payments."[9] They have seen it happen already and are obviously concerned it will happen again.

Utilization of public natural resources to create "economic opportunities for the people of British Columbia," as stated by Rich Coleman, should not be limited to those who achieve control of the resource. It is a reasonable premise to suggest that there should be balance in the economic benefits that flow from provincial natural resource use and that the regulatory and operating environment that frames business operations should reflect this.

In 2005, the TLA predicted that the changes brought about by the *Forest Revitalization Act* would bring hardship to contractors and communities as a whole, but agreed to them having been told by government that if things don't work out, changes would be made. Ten years later, our prediction is all too evident and change is needed once again.

As the TLA approaches its 75th anniversary of advocating for loggers' issues (it will come as no surprise that rate issues were the catalyst for TLA's creation in 1943), we can be sure that our members will adapt and survive in an effort to protect the personal investments they have in their companies. This trend has already started as was noted by ILA panel members, where some are diversifying to other resource sectors, some are downsizing and many are simply going to retire. If there is no profit in contract logging, TLA members will also adapt and move along.

Without change to rates, the framework within which they are negotiated in the logging sector or the insolvency process that allows continued operation of insolvent companies after their debts have been absorbed by community businesses, it is now predicted that there will not be enough loggers to deliver logs, a trend already being acknowledged in the BC Interior by some licensees and for the same reasons. As the super-cycle approaches, the entire forest industry may be at risk because of rates.

We would hate to be correct in our prediction…again!

The TLA has long been an advocate for loggers and community-based business. All community-based businesses that support the logging sector should, however, be cautious when you are asked to extend credit to a logging contractor. Ask if they have been insolvent in the past (an indicator of the impact of low rates) and confirm for yourself the likelihood of you being paid. The evidence to the contrary is mounting as low rates force more contractors to struggle.

Should this continue, then LNG better pay off as the forest industry and the BC communities that rely on it may need the economic support.

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[1] Truck LoggerBC, Summer 2014, "Loggers Not Out of the Woods Yet"
[2] Western Forest Products Inc. 2014 First Quarter Report
[3] Western Forest Products Press Release July 31, 2014
[4] Interfor Press Release May 6, 2014
[5] Canfor 2013 Annual Report
[6] District: British Columbia, Division No: 03-Vancouver, Court No: B140488, Estate No: 11-1848863: April 25, 2014
[7] Creditors Package Proposal April 20, 2014 – www.bowragroup.com
[8] Truck LoggerBC, Summer 2014, "Like Ripples in a Pond"
[9] Alberni Valley Times, August 5, 2014.