

THE CANADIAN FOREST SECTOR:

PAST, PRESENT, FUTURE 



INTERIM REPORT OF THE STANDING SENATE COMMITTEE ON AGRICULTURE AND FORESTRY

THE HONOURABLE PERCY MOCKLER, CHAIR
THE HONOURABLE JOYCE FAIRBAIRN, P.C., DEPUTY CHAIR

DECEMBER 2009

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Public Archives of Canada, taken from: http://www.ameriquefrancaise.org/fr/article-54/Pin_blanco_d'Am%C3%A9rique:_exploitation_des_peuplements_.html

EnviroZine, Environment Canada's On-line Newsmagazine,
http://www.ec.gc.ca/EnviroZine/english/issues/45/feature2_e.cfm

Centre d'expertise sur la construction commerciale en bois (Cecobois),
http://www.cecobois.com/repertoire/index.php?option=com_rea&view=fiches&id=224&Itemid=94

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MEMBERSHIP

STANDING SENATE COMMITTEE ON AGRICULTURE AND FORESTRY

The Honourable Percy Mockler, Chair
The Honourable Joyce Fairbairn, P.C., Deputy Chair

The Honourable Senators:

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Nicole Eaton
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Michel Rivard

* Marjory LeBreton, P.C. (or Gérald Comeau)
* James Cowan (or Claudette Tardif)

Other Senators who have participated from time to time in this study:

The Honourable Senators: Brazeau, Callbeck, Campbell, Carignan, Carstairs, P.C., Cordy, Duffy, Housakos, Hubley, Johnson, Meighen, Munson, Stewart Olsen and Tkachuk,

* *Ex Officio* members

ORDER OF REFERENCE

Extract from the *Journals of the Senate*, Tuesday, March 31, 2009:

The Honourable Senator Mockler moved, seconded by the Honourable Senator Fortin-Duplessis:

That the Standing Senate Committee on Agriculture and Forestry be authorized to examine and report on the current state and future of Canada's forest sector. In particular, the Committee shall be authorized to:

- (a) Examine the causes and origins of the current forestry crisis;
- (b) Examine the federal role in the forest sector in Canada;
- (c) Develop a vision for the long-term positioning and competitiveness of the forest industry in Canada;
- (d) Recommend specific measures to be put forward by the federal government to lay the foundations of that vision.

That the Committee submit its final report to the Senate no later than June 17, 2010.

The question being put on the motion, it was adopted.

THE CANADIAN FOREST SECTOR

Past, Present, Future

FORWARD

In the spring of 2009, the Standing Senate Committee on Agriculture and Forestry began a detailed study of the Canadian forest sector. This interim report is based on the committee's public hearings held in April, May and June of 2009. The committee heard from representatives of various levels of government, the primary and secondary processing industries, private woodlot owners, the academic community and rural associations. This interim report has two purposes: first, to make recommendations to the federal government for immediate action on specific issues, and second, to identify the themes to be addressed by the Senate committee as it continues this study in the fall of 2009 and the spring of 2010.

INTRODUCTION

The forest plays key ecological, social and economic roles in Canada. Its ecological role encompasses mainly its ability to filter and purify water, to filter air by absorbing carbon and to provide a habitat for wildlife. In its social role, the forest offers both recreational opportunities (e.g., outdoor activities, hunting), fulfills the spiritual and subsistence needs of the First Nations, and also represents a form of land use that contributes to the vitality of rural communities. The forest's economic role can be described in general terms as resource development for economic profit. The forestry crises that have plagued Canada for many years have various causes, but similar effects: factories close, jobs are lost and rural communities become more vulnerable. Therefore, the current crisis is most closely linked to the economic role of the forest, and it is this aspect that has caught the media's attention. However, the forest's economic role cannot be examined in isolation because the forest's three main roles are constantly interacting.

This interim report examines the causes and effects of the forestry crises in the context of the forest's social, economic and ecological roles. The report's objectives are to make recommendations to the federal government for immediate action on specific issues, and second, to propose the themes on which the rest of the study will focus. To that end, Chapter I provides a brief overview of the roles and historical importance of Canada's forests. Chapter II examines the leading causes of the forest system crises, and Chapter III presents the historical roles and responsibilities of the federal government. Lastly, Chapter IV formulates recommendations and specifies areas that the Senate committee may explore as it continues its work.

CHAPTER I: THE CANADIAN FOREST: A HISTORICAL OVERVIEW AND SYSTEMIC APPROACH

1. A Brief Overview of the Significance of Forests in Canadian History

Forests are intrinsically linked with Canada's history. Long before the arrival of European settlers, the forest played a fundamental role in the lives of the First Nations peoples: it was a source of sustenance, supplying them with primary materials and meeting some of their basic needs, such as food, lodging and clothing. For example, the First Nations used the paper birch tree to build their famous canoes. The bark of the paper birch—also called a canoe birch—was placed over a frame built of *Thuja occidentalis* wood that had been shaped with steam. The birch bark was sewn together using spruce, pine or larch roots and was waterproofed with pitch from conifers (spruce, pine). The First Nations also used bark from the paper birch for building shelters (wigwams), weaving baskets and as writing materials. They also used many trees for medicinal purposes. For example, the leaves and bark of the *Thuja occidentalis*—commonly but incorrectly known as “cedar”—were used for infusions and ointments to treat coughs, swelling and burns. Jacques Cartier was probably referring to the *Thuja occidentalis* when he mentioned the “annedda” in his travel journals as the tree that saved his men from death by scurvy.¹

They showed us how to grind the bark and the leaves and to boil the whole in water. Of this one should drink every two days, and place the dregs on the legs where they were swollen and affected. According to them this tree cured every kind of disease. They call it in their language Annedda.

The Captain at once ordered a drink to be prepared for the sick men but none of them would taste it. At length one or two thought they would risk a trial. As soon as they had drunk it, they felt better which must clearly be ascribed to miraculous causes; for after drinking it two or three times, they recovered health and strength and were cured of all the diseases they had ever had. [...] Then there was such a press for the medicine that in less than eight days a whole tree as large and as tall as any I ever saw was used up [...]

Not surprisingly, the *Thuja occidentalis* is also known as the arborvitae, or “tree of life.” Spruce gum, used to make the famous spruce beer, eventually became a preferred source of essential vitamins and minerals for French settlers. The shagbark hickory and the yellow birch were highly valued for cabinetry in New France. During the same period, maple was used for heating homes and, of course, for making maple syrup. The hemlock was used to build barns and railroad ties, and

¹ *The Voyages of Jacques Cartier*, University of Toronto Press, 1993, p. 80

for a long time it was the preferred source for tannic acid used to process leather. The eastern white pine is closely linked to the development of the logging industry. In the 19th century, white pine was the British Navy's wood of choice for shipbuilding. In 1806, the first timber rafts were sent down the Gatineau River. The jack pine is the pine with the largest geographical distribution in Canada. Its habitat extends from Nova Scotia to the Northwest Territories. Today, the species is highly valued as it is used in a number of commercial applications (softwood lumber, pulp and paper). For a long time, however, it had the unenviable reputation among settlers of "poisoning the land" given that it is often associated with poor soil conditions. The jack pine is a close relative of the lodgepole pine from British Columbia, whose population is currently being ravaged by the mountain pine beetle. These two species of pine often produce hybrids where they co-exist. The jack pine and lodgepole pine were called "cypress" by early French Canadian explorers and Métis. This explains the origin of the name "Cypress Hills" in Southern Alberta and Saskatchewan.

Ash was the preferred wood for hockey sticks, a Canadian sports symbol par excellence if ever there was one. The Manitoba maple was used for shade trees and windbreakers in the Prairies and is used today for revegetation and stabilizing riverbanks. Spruce and fir are associated with the development of the pulp and paper industry, and of course, the fir is also the Christmas tree of choice. The construction industry uses large quantities of spruce, fir and pine. Long considered an undesirable species, the poplar has become widely used over the last 25 years for commercial purposes including plywood, and pulp and paper. The trembling aspen, a variety of poplar, is a preferred tree of the beaver both as a food source and as building materials for their dams and lodges.

This brief overview of some of the ways in which trees have been used in Canadian history² illustrates the many roles the forest plays in Canada. Of course, the way that forest resources are used has changed radically over the years, but Canada's forests are still called on to fill important social, economic and ecological roles.

² Some of these historical anecdotes were taken from *Guide d'identification des arbres du Canada*, (Jean Lauriault) Musées nationaux du Canada, Broquet, 1987, 551 pages.

2. The Canadian Forest: A Systemic Approach

We should think about the big and small companies as an economic ecosystem. They depend upon each other. We need the woodlot owners; they need the big companies. [W]e need many more small, value-added companies; the niche players, the agile players, and the big, world-class heavy hitters. If they are all functioning, everyone prospers. If you take out one piece of the economic ecosystem, the whole ecosystem shakes.

Avrim Lazar, President and CEO, Forest Products Association of Canada

We see a resilient future for the forest sector in Northern Ontario if emphasis is put on restructuring so that communities have the opportunity to develop a local vision for their forests and realize social, economic and ecological benefits from the land around them.

Joseph LeBlanc, student, Northern Ontario Community Economic Development Network

Figure 1 shows the main components of the Canadian forest system. The image as a whole represents the entire forest ecosystem. The sub-systems of the forest ecosystem are closely linked. In order for the entire ecosystem and its components to prosper, there must be a balance between the sub-systems. For example, if too much emphasis were placed on the economic aspect of forest production, for example by exploiting the forest beyond its capacity to recover, the forest's ecological role would suffer. The lack of fibre due to overexploitation would ultimately have a definite impact on the vitality of rural communities, thereby affecting the forest's social role as well. The balance would be upset. The consequences of overexploiting the forest could compound each other and increase the imbalance: the loss of virgin forest space could reduce tourism in rural areas, exacerbating the economic situation. **A first principle to remember: all forest policies must seek to achieve a balance between the three main roles of the forest. Granted, Canada's forest policies over the years have probably not always met this objective, but it is estimated that this principle enjoys a large consensus among stakeholders more so today than ever.**

Given the current economic problems, figure 1 places special emphasis on the forest system's economic role. Note that only the forest's *direct* economic role is shown. The forest also has a very important *indirect* economic role, given the numerous industries that depend on forest products or that supply the forest industry. The sub-sectors of the forestry industry are in constant interaction within this economic

framework, right from the moment a tree is cut down, as different parts of the tree serve different purposes. There can be competition between the primary processors for access to the fibre. The veneer industry can be in competition with the lumber industry for access to hardwood. In the same way, spruce trees can be used directly to produce pulp or they can be used for construction timber. **A second principle to remember: alternative uses are possible for the same fibre, which can create competition for access to the resource.**

Paradoxically, there is also a significant amount of co-operation among the various sub-sectors of the forestry industry. For example, wood chips, a by-product of lumber production, can be used by pulp producers. Sawing and sanding operations produce large quantities of sawdust that can be used to make particle board. Bark is another industry by-product and can be used as an energy source within the forest sector. **A third principle to remember: the sub-sectors of the forestry industry are often complementary.**

Even if the sub-sectors of the forestry industry are often complementary, the same by-product could have multiple uses. Operations may thus compete for access to these by-products. For example, the wood chips produced by sawmills may be in demand from both oriented strand board producers, and pulp and paper companies. Similarly, sawdust can be used by pulp producers and particle board companies, and even has some usefulness outside the forestry industry, e.g., as bedding for farm animals. As a general rule, by-products of the forestry industry can also be used for energy production (e.g., wood pellets for fuel). **A fourth principle: there are many alternative uses for by-products of primary and secondary processing, which can create competition between users or lead them to integrate vertically to ensure supply (e.g., a pulp and paper mill buys a sawmill to control its supply of wood chips).**

It is extremely important to understand the relationships between the elements described in the previous section and illustrated in Figure 1 when examining the causes of and possible solutions to the forest system's current problems. These relationships mean that a decrease in demand for one type of wood product is liable to affect other sub-sectors of the forest industry. In the same way, every government assistance policy for a specific sector will likely have an effect—negative or positive—on the other sectors of the system.

Sources of material for Figure 1:

Economic role diagram: based on the presentation by the New Brunswick Federation of Woodlot Owners before the Senate committee

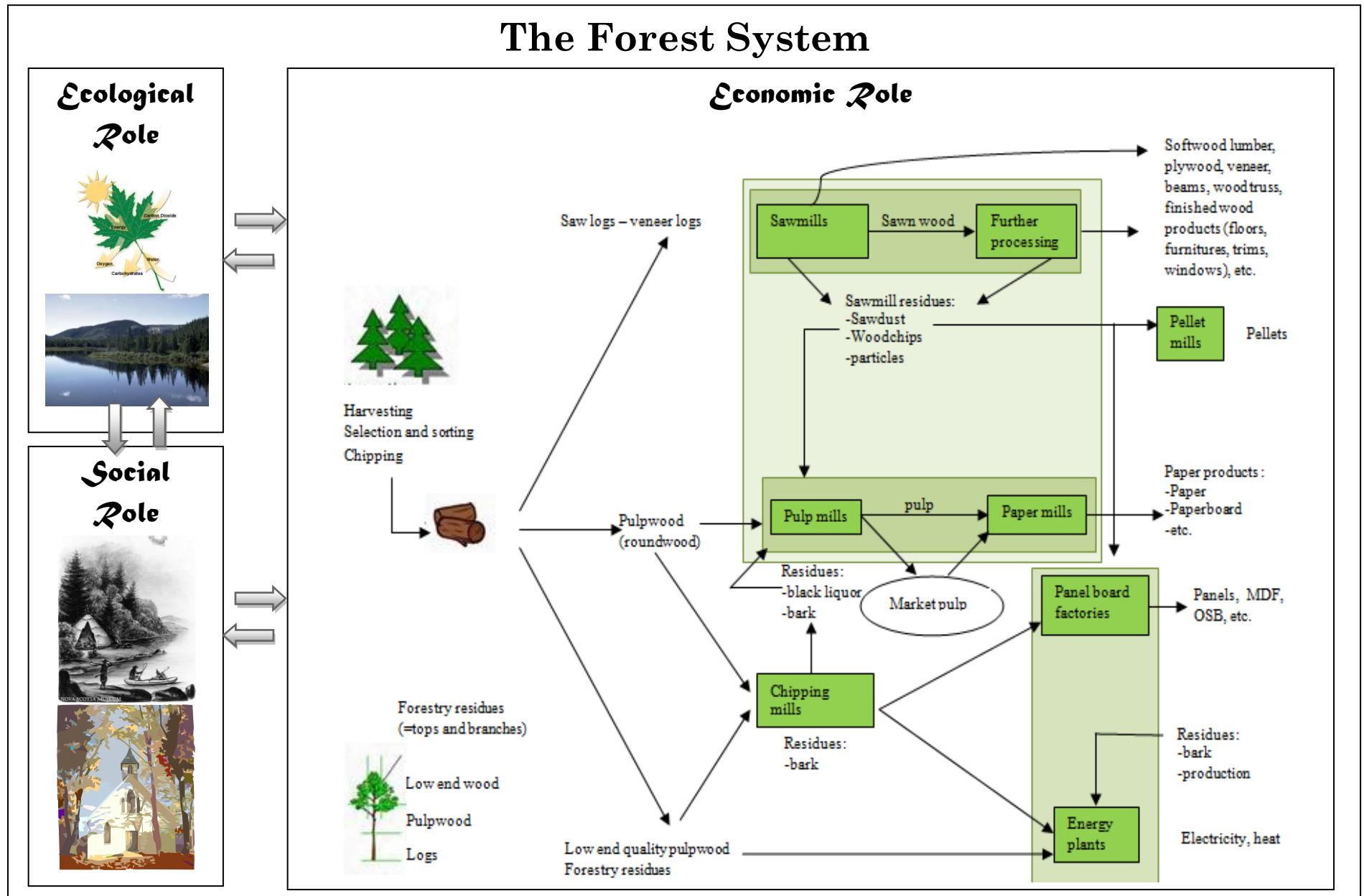
Images: Images Nova Scotia, “Indian Canoe and Wigwam” Watercolour, Anonymous, Collection of the Nova Scotia Museum of cultural History,
<http://museum.gov.ns.ca/imagesns/html/21732.html>)

Natural Resources Canada (<http://scf.rncan.gc.ca/index/education3/?lang=en>)

Canada’s Economic Action Plan (<http://www.plandaction.gc.ca/eng/media.asp?id=1809>)

Schematic: Parliamentary Information and Research Service, Library of Parliament

Figure 1 – The Canadian Forest System



CHAPTER II: CAUSES AND EFFECTS OF THE CRISES IN THE FOREST SYSTEM

My first comment would be that we should be discussing crises within the forest sector and not just a crisis. There are a number of crises for which explanations differ.

Jean-Pierre Dansereau, Director General, Fédération des producteurs de bois du Québec

(...) most of the hardships that the Canadian forest industry and woodlot owners throughout Canada are currently facing are largely created by outside influences which are almost entirely out of our control.

Andrew Clark, President, New Brunswick Federation of Woodlot Owners

Let us be truthful about this: this is market-driven. There are no markets for our lumber; there are no markets for Mr. Cameron's remanufactured products; there are no markets for the pulp and paper products.

R.M. (Rick) Jeffery, President and CEO, Coast Forest Products Association

The commodity industry in Canada in the lumber and pulp and paper aspects of the forest industry will diminish relative to other elements of the forest sector in the future. The competition will be able to outdo us in price for a good length of time. I am not sure at what point this levelling of pricing will happen, but we face some distinct disadvantages in the world markets when it comes to commodities.

Harry Bombay, Executive Director, National Aboriginal Forestry Association

The current problems in the forest system can be explained largely by the decreased demand for products made of Canadian wood, although the reasons for the reduction in demand vary from one product to another. The strong Canadian dollar, limited access to credit, and timber supply are among the factors that have exacerbated the problems caused by shrinking markets. One challenge related to market loss is to understand why the industry's very structure made it so susceptible to the decrease

in demand for primary products. The next sections will examine these three aspects and look at the consequences of the crises in the forest system.

1. The causes of the Forest System Crises

a) Structural Decline in Demand for Newsprint

Take the newsprint sector, which is a traditional market. Despite the high quality of paper manufactured in Quebec, which is based on the quality of black spruce fibre, the market for this product is shrinking. It is going down by about 8 per cent per year.

Yves Lachapelle, Forestry Director and Special Adviser, Strategic Issues, Quebec Forest Industry Council

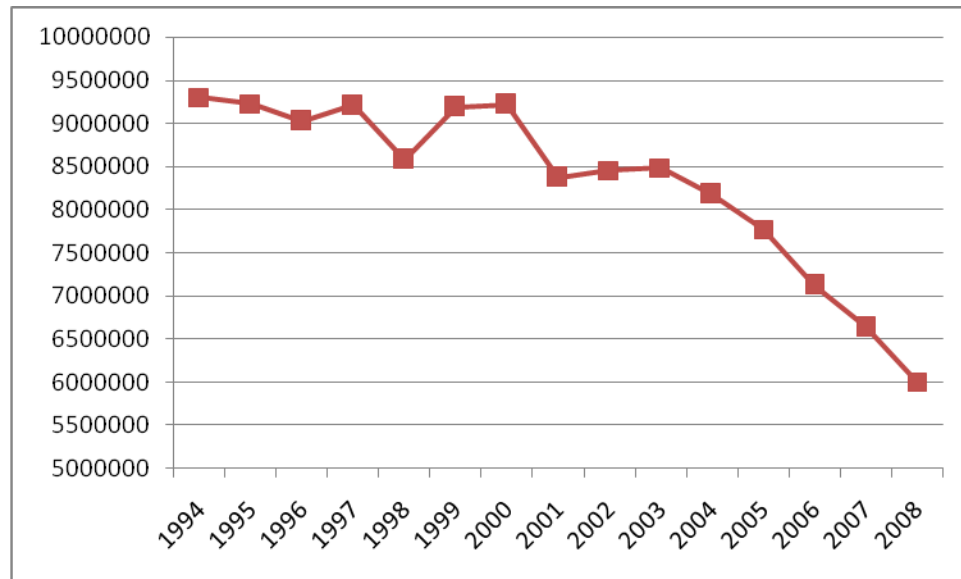
[...] people are switching from classified advertisements to Craigslist — and they will not come back.

Avrim Lazar, President and CEO, Forest Products Association of Canada

The demand for newsprint is in serious decline in North America, with the sharpest decrease appearing over the last few years. The main reason for this decrease is the popularity of the Internet and electronic publications. Fewer newspapers being sold mean a reduced demand for newsprint, which has created huge problems for companies and workers in the Canadian pulp and paper industry. The following graph depicts newsprint production in Canada between 1994 and 2008, clearly showing that production is in freefall. It is important to note that this decline is more structural than cyclical, that is, most of the decrease can be attributed to an irreversible trend: the increased popularity of online and electronic publications, which is certainly not just a passing phase or a cyclical phenomenon. This is not to say that the decline will continue at the same rate as it has in the last few years. Nevertheless, there is a large consensus that the newsprint market will never again reach the peak it achieved in the 1970s and 1980s in North America.



Graph 1- Newsprint Production in Canada (tonnes)



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>

There is a lot of talk about the fierce competition from Brazil for pulp³ production. This competition is not a factor in the decline of newsprint production. In fact, Brazilian newsprint production has plummeted 40% in the last decade, unlike Chinese newsprint production, which has skyrocketed in the same timeframe. This increase in Chinese newsprint is due to domestic consumption; more than 90% of Chinese newsprint was consumed domestically in 2008.⁴

b) Decreased Demand due to Competition from Developing Economies

The big competitors for hardwood pulp are Central and South America. Their cost of production is such that they can ship copy paper, or printing paper, into Canada much cheaper than we can even produce it.

Jim Farrell, Assistant Deputy Minister, Natural Resources Canada

³ Pulp is a material prepared by chemical or mechanical separation of fiber from wood. Wood pulp can be produced from softwood trees such as spruce, pine and fir, and from hardwoods trees such as eucalyptus, aspen and birch. Pulp is the raw product used in the paper making process.

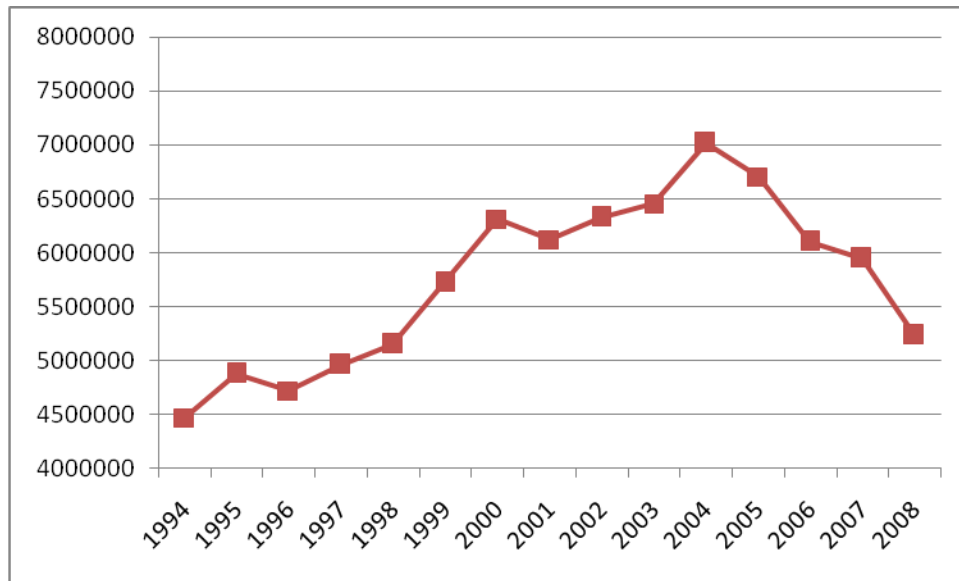
⁴ Source: http://0101.net/clime.net/1_5/2fb/148/215/China%20Newsprint.pdf

The demand for pulp has not experienced the same decline that newsprint did. In fact, demand has been relatively strong because of global economic growth over the last 10 years. The problems that Canadian pulp producers face can be explained mostly by increased competition from developing countries. For example, Brazil increased its hardwood pulp production by 150% between 1994 and 2007.⁵ In Brazil, and in developing countries in general, pulp is often made from fast-growing trees (e.g., eucalyptus) on plantations located close to very large processing facilities. For example, the average distance between tree plantations and the factory might be as little as 100 km. Also, the quantity of eucalyptus grown per hectare in Brazil is phenomenal. The eucalyptus can reach maturity in seven years, while Canadian species such as the Douglas fir and the eastern spruce take 45 and 90 years to mature, respectively.⁶ This rapid tree growth allows Brazilian processing plants to avoid having to go farther and farther away to maintain their timber supply, which is what has happened to Canadian pulp companies. This production method, along with technological innovations, has allowed developing countries to rapidly become key players in the pulp production market, thereby threatening North American producers. Graph 2 shows printing and writing paper production in Canada. As the graph illustrates, printing paper production in Canada has fallen drastically since its peak in 2004. It should be noted that the emerging popularity of e-books could also represent an important challenge to Canadian printing paper producers in the future. Graph 3 compares Canadian and Brazilian pulp production. Despite Brazil's rapid increase in pulp production, the graph shows that Canada still produces significantly more pulp. But for how much longer?

⁵ Brazilian Pulp and Paper Association (Bracelpa), <http://www.bracelpa.org.br/eng/estatisticas/index.html>

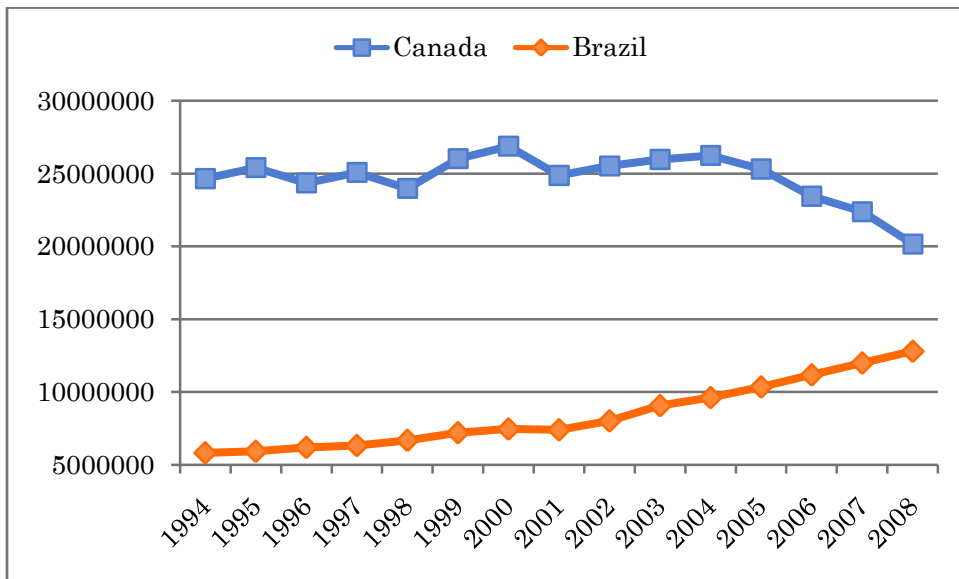
⁶ *The case for Brazil*, Perry J. Greenbaum, September 1, 2008, Pulp & Paper Canada

Graph 2- Printing and Writing Paper Production in Canada (tonnes)



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>

Graph 3- Pulp Production in Canada and Brazil (tonnes)



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>
 Brazilian Pulp and Paper Association (Bracelpa), <http://www.bracelpa.org.br/eng/estatisticas/index.html>
 Compilation: Parliamentary Information and Research Service, Library of Parliament

The secondary processing industries have also faced competition from Asian producers. China has replaced Canada as the leading exporter of furniture to the

United States with 50% of market share, leaving Canada a distant second with only 14% of market share. Furniture made in Asia also accounted for more than 50% of Canadian domestic demand in 2007.⁷ Although the Canadian kitchen cabinet industry was a growing industry before the economic recession Asian producers now have a foothold in the market for lower-end products. Secondary processing industries, like furniture and cabinets, buy significant amounts of panels and veneers, which means that when these industries are in trouble, the primary processing industries are negatively affected as well.

The sawmill industry has also been affected by the problems that pulp and panel board producers face. Sawmills produce by-products such as wood chips and sawdust that are consumed in large quantities by paper and panel board producers. Veneer companies use only 25% of a tree's fibre, and the rest must be sold for producing pulp, panels, wood pellets, etc. Therefore, when paper and panel board producers faced problems, certain sawmills suffer financially as a result.

c) Cyclical Decrease in Demand from the Construction Industry

We have gone from a peak of about 2.2 million housing starts down to 600,000. That is a 75 per cent drop in demand. (...) [Prices] have gone from over \$400 a unit to \$190 a unit; a 50 per cent decline. By simple calculations, a 50 per cent decline in volume and a 50 per cent decline in price results in 25 per cent of business remaining. Not many industries can survive at those rates, which is why today we see both permanent and temporary layoffs as well as closures.

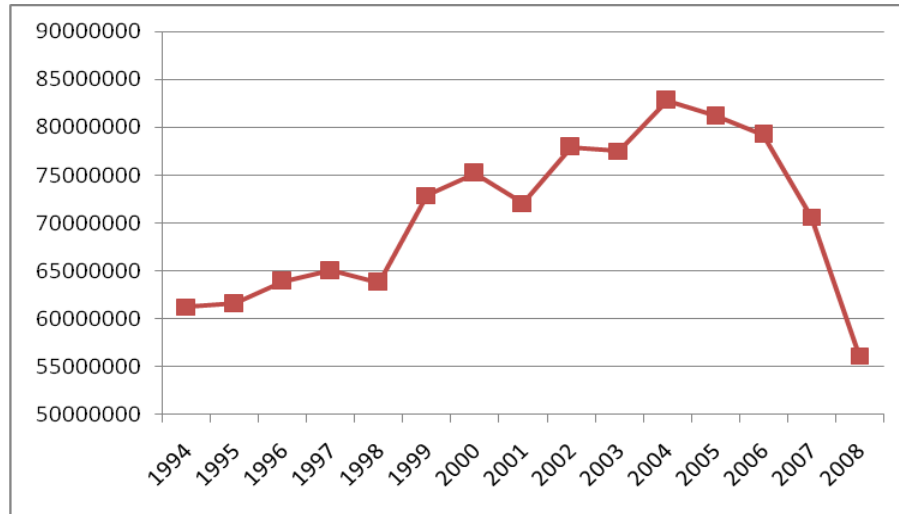
Bill Love, Chairman of the Board, Canadian Wood Council

While pulp production had been stagnant or in decline in Canada since the mid-1990s, until very recently the construction lumber industry was still growing, despite the softwood lumber dispute with the United States. When the real-estate bubble burst in the United States and residential construction collapsed, Canadian sawmills were seriously affected. The decrease in construction had an immediate effect on primary processing products (plywood, framing lumber, oriented strand board, etc.) as well as secondary processing products (kitchen cabinets, flooring, windows, etc.). The collapse of the housing market occurred at a time when sawmills were already facing a decreased demand for their by-products (wood chips and sawdust) due to the decline of the pulp industry. Graphs 4 and 5 show the

⁷ Terry Clark, President, Canadian Council of Furniture Manufacturers, statement before the committee, May 28, 2009.

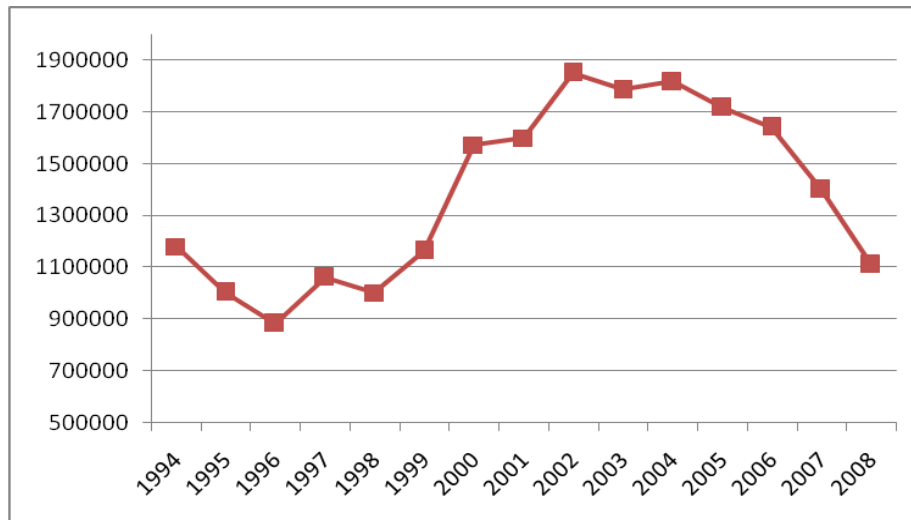
production of softwood and hardwood lumber in Canada between 1994 and 2008. Graph 6 shows the production of plywood and oriented strand board. These three graphs highlight the sharp decline in sectors associated with the construction market. This decline can be said to be “cyclical”, because residential construction in the United States is seen as a cyclical business. However, given the excess that marked the recent real-estate boom in the United States, the trough of this cycle could last for longer than previous experiences would suggest.

Graph 4- Production of Softwood Lumber in Canada (cubic metres)



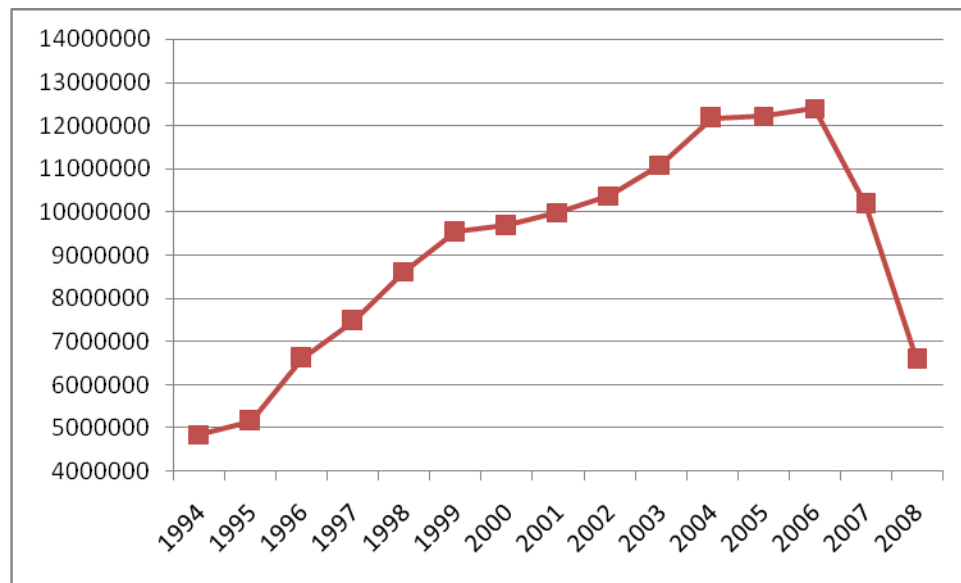
Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>

Graph 5- Production of Hardwood Lumber in Canada (cubic metres)



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>

Graph 6- Production of Plywood and Oriented Strand Board (cubic metres)



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/production>

d) Aggravating Factors

i) Exchange Rate and the Cost of Energy

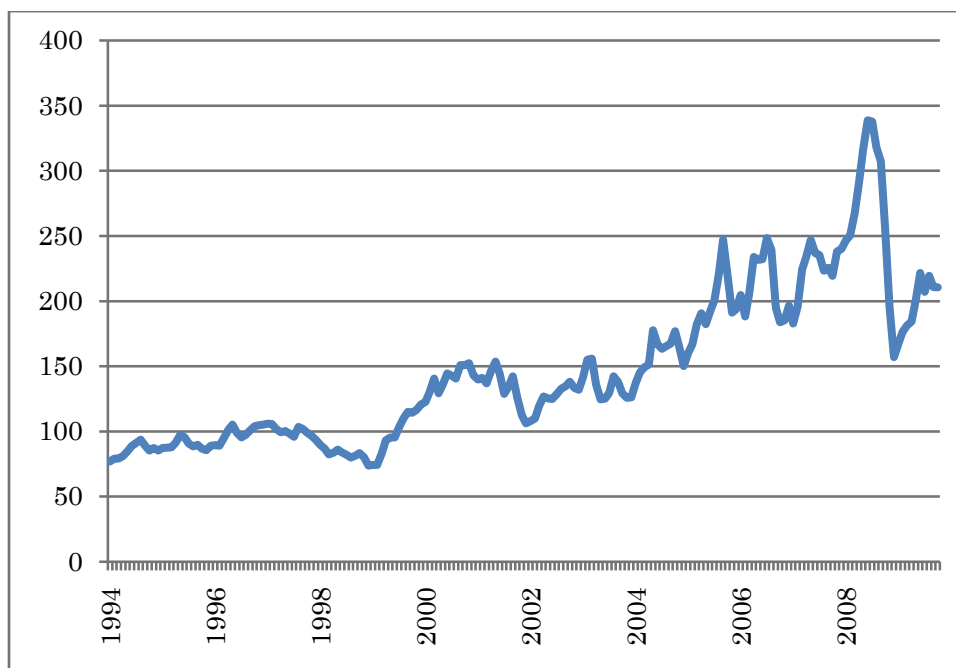
Regarding currency fluctuations, the higher the Canadian dollar, the higher its position on the hurdle list.

Russ Cameron, President, Independent Lumber Remanufacturers Association

The strength of the Canadian dollar over the last few years has exacerbated the forest industry's problems. As commodity prices are determined in U.S. dollars, any increase in the Canadian dollar compared with the U.S. dollar results in a direct decrease in price for Canadian producers. Some costs, such as salaries, are not influenced by the fluctuating exchange rate. Therefore, the profit margin for Canadian companies is often caught between an increase in the Canadian dollar and normal operating costs.

Similarly, rising energy costs over the last few years (see Graph 7) have also exacerbated the crisis, as the forestry industry consumes a lot of energy. The combination of a strong Canadian dollar and elevated energy costs has greatly affected the financial health of some companies.⁸

Graph 7- Evolution of Monthly Gasoline and Fuel Oil Prices since 1994 (industry price index, 1997=100)



Source: CANSIM, v1574558; Gasoline and fuel oil, other, industry price index.

⁸ It is important to note that the combination of a strong Canadian dollar and elevated energy costs is not a coincidence. There has been historically a certain correlation between the two factors.

ii) Access to Credit

We have been considered a high risk [industry] for several years now, and the expanding credit crisis is wreaking havoc. As companies scramble to cover debt in these difficult times, financial institutions are unwilling to lend at normal risk premiums, and in the rare chance that they do invest, it is usually at extremely high premiums, from 8 to 15 per cent. This makes it very difficult to look at any innovation, any new ideas, any new markets or any new product.

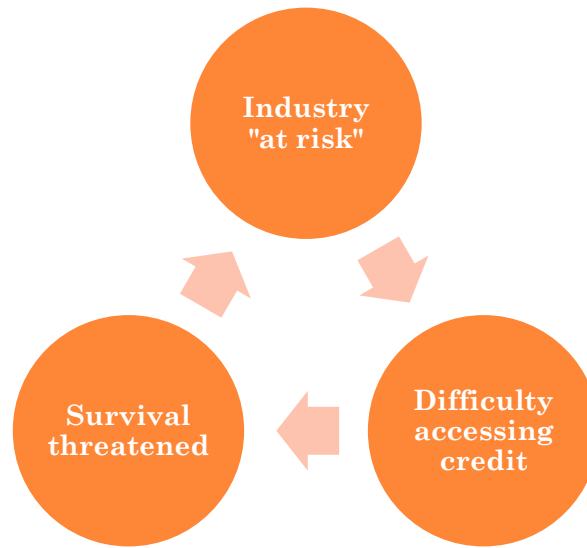
Mark Arsenault, President and CEO, New Brunswick Forest Products Association

Even before the economic crisis, the forest industry was seen as an industry at risk and therefore had restricted access to credit compared with other sectors in the economy. With the financial crisis, banks have become even more cautious in their lending policies, and forest companies have had even less access to credit than before⁹. Many forestry companies have found themselves in a vicious circle that threatens their very survival, as pictured in Figure 2.



⁹ Government entities such as Export Development Canada (EDC) and the Business Development Bank of Canada (BDC) have also expressed their views at Committee hearings on the risks pertaining to access to credit for the forest industry. This issue is discussed in further detail in Chapter 4.

Figure 2 – The Vicious Circle of Access to Credit for Forest Companies



Source: Parliamentary Information and Research Service, Library of Parliament.

iii) Black Liquor

The U.S. black liquor tax credit further aggravated the situation of Canadian pulp producers. Black liquor -a by-product of the kraft process- has a high energy content and is therefore reused in the pulp-making process to create steam. Since black liquor is considered a biofuel in the United States, it is currently eligible for a substantial tax credit. This credit can cover up to 50% of production costs, which gives U.S. producers an unfair advantage.¹⁰

iv) Timber Supply

(...) the remoteness and inaccessibility of our mature softwood forests [in Quebec]; the dispersion of pine and deciduous growth in our deciduous forests [...]

Yves Lachapelle, Forestry Director and Special Advisor, Strategic Issues, Quebec Forest Industry Council

¹⁰ This issue is addressed again later in this interim report. The federal government has implemented a green credit for black liquor production in Canada to lessen the effects of the U.S. tax credit.

(...) we are optimistic that the industry will recover, and when it does, we will have a wood supply problem again.

Tom Reid, Deputy Minister, Department of Natural Resources of New Brunswick

With the current decrease in demand, it may seem surprising to address the issue of timber supply. However, manufacturers in Eastern Canada are at a distinct competitive disadvantage due to the small stature of the trees and their relatively remote location. Furthermore, increasing energy costs add to the burden for forest companies struggling with the distance between the timber source and the processing location. It is worth noting that these trees were at one time larger and closer to the processing location. The change in circumstances may be a testament to poor forest management in the past.

In British Columbia, and to a lesser extent Alberta, the mountain pine beetle infestation has destroyed huge swaths of forest. The pine beetle attacks various species of pine, including the lodgepole pine, the most commercially exploited species in British Columbia. According to Natural Resources Canada, at the rate the mountain pine beetle is currently spreading, 80% of mature pine trees in British Columbia will have died by 2013. Pine trees in Canada's northern boreal forest, especially the jack pine, are also at risk. Paradoxically, this epidemic has led to an increase in the quantity of fibre available in the short term, because even once a pine tree has been attacked by the pine beetle, it retains its commercial value for a few years. However, this increased source of supply comes at a time when demand is in freefall. Beyond the short term, it is estimated that the infestation will negatively affect timber supply in the West for a very long time.

e) Industry Structure

The forest industry finds itself in an unfortunate situation, which could probably have been avoided if the industries' sectors and companies had had a broader long-term vision, extending beyond immediate concerns.

Guy Caron, National Representative for Special Projects, Communications, Energy and Paperworkers Union of Canada

I believe the main cause of the existing crisis is the fact that we have not adapted quickly to the new economic realities of the global economy. [...] We have not tried very hard to diversify out of our low-value, commodity-based products. We simply have not set our sights very high.

Tom Beckley, University of New Brunswick, Faculty of Forestry and Environmental Management, as an individual

A lack of diversity in the forest sector is the major cause of the current vulnerabilities. Natural resource management policies and practices that focus on primary producers have created a dependency relationship between communities, industry and government.

Joseph LeBlanc, student, Northern Ontario Community Economic Development Network

Why did industry not act more determinately when it had more options? In the 1970s, and even the 1980s, it had the capital, leadership and technological prowess to go forward and provide a stronger foundation for itself, but it did not do this. [...] In retrospect, it appears that their assessment of risk and reward of various investment alternatives was flawed because they were heavily dependent on Canada and on the U.S. market. There was also some complacency because the industry had been dominant for so long and they had it so good that they did not see that things had fundamentally changed.

Jeremy Williams, Forestry Consultant, Registered Professional Forester in Ontario, as an individual

Witnesses appearing before the committee often cited the following elements as major contributors to a weakened Canadian forest industry:

- excessive reliance on the U.S. market;
- an industrial structure that is concentrated, integrated and focused mainly on primary products;
- the lack of diversity in the manufacturing sector;
- out-of-date manufacturing facilities suffering from a lack of reinvestment.

The weakened state of the industry had been hidden for many years by a low Canadian dollar, low energy costs and a relatively healthy demand for products

made from Canadian wood. Once these factors were reversed, the industry's inherent weaknesses were revealed, creating a systemic crisis. The structure of the industry at the start of this crisis can be explained by a variety of reasons. They likely stem from a combination of historical factors, such as an inflated sense of confidence in the future given the relative prosperity the industry had experienced for years, public policies that did not adapt to the new reality, and poor business decisions.

The debate over what led to the current industry structure could go on forever. What should be retained is that the industry displayed traits, mainly a lack of diversity in its products and export markets, as well as the degree of concentration that made it vulnerable to significant changes in economic conditions. While this observation applies mostly to the pulp and paper business, many companies have both sawmill and pulp activities, making it sometimes difficult to distinguish between these two sectors.

2. The Effects of the Forest System Crises

As this section shows, the causes of the forest system crises have significant economic, social and ecological implications.

a) Economic Implications

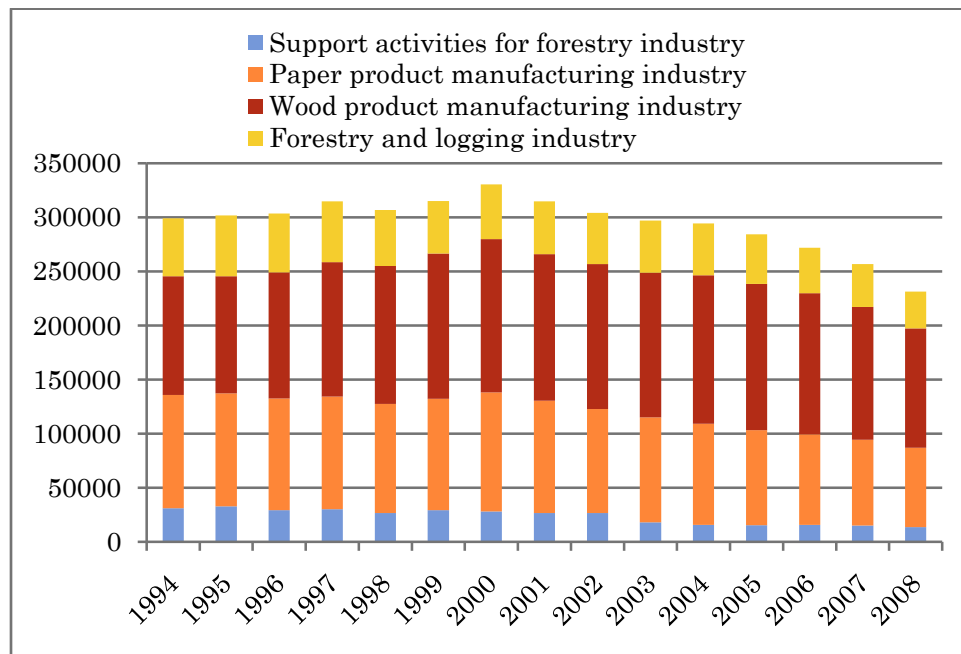
Tembec had a near-death experience last year, but we were able to recapitalize and avoided the fate of AbitibiBowater, which is bankruptcy protection. The pain continues; I have laid off 10 people in my group. Tembec employment has dropped from 10,047 people in 2004 to 6,727 in 2008. It is still dropping. We have laid off another 1,400 people this year. Our salary, payroll and benefits dropped from \$771 million in 2004 to \$508 million in 2008. That is a reduction of more than one-quarter billion dollars in salary and benefits.

Bill Love, Chairman of the Board, Canadian Wood Council

When the demand for Canadian wood products plummeted, the most immediate effect was a large number of layoffs in the forestry sector. The following graph shows the number of jobs in the forestry industry per year since 1994. The downward trend begins after 2000, and employment has decreased every year since. Between 2000 and 2008, the support activities for the forestry industry lost more than 50% of their labour force; the paper product manufacturing industry lost 33%; the wood product manufacturing industry lost 22%; and the forestry and logging industry lost 33%.

Table 1 shows mill closures in the forestry industry by province between 2003 and 2008. These closures, along with job losses, reduced the forestry industry's share of the Canadian economy, but more significantly, they exacerbated economic troubles in forest-dependent regions of Canada.

Graph 8- Number of Jobs in the Forest Sector



Source: Canada's Forests, Natural Resources Canada,
<http://canadaforests.nrcan.gc.ca/statsprofile/economicimpact/>

Table 1 - Permanent and Indefinite Mill Closures in the Forestry Industry by Province from January 2003 to June 2008

	Permanent Mill Closures	Indefinite Mill Closures	Total Mill Closures	Total Layoffs
Alberta	6	4	10	1,366
British Columbia	20	28	48	10,367
Manitoba	0	0	0	15
New Brunswick	10	3	13	3,046
Newfoundland and Labrador	1	0	1	485
Nova Scotia	0	2	2	430
Ontario	25	18	43	9,450

Prince Edward Island	0	1	1	35
Quebec	26	54	80	11,668
Saskatchewan	2	7	9	1,566
Total	90	117	207	38,428

Source: Forest-dependent communities in Canada, Natural Resources Canada,

http://canadaforests.nrcan.gc.ca/article/trend/top_suj/23

b) Social Implications

It is true that the suicide rate and the discouragement is greater now than it was, in the rural world, both for farmers and for private forest operators, I can tell you that. I am now working on things I can do with these people. These are people who do not open up easily. The owners and the farmers are proud people, but in a good sense. These people do not talk about their situation.

Pierre-Maurice Gagnon, President, Fédération des producteurs de bois du Québec

In addition to facing decreased revenue, communities face the social and economic impact of employment loss in the forest sector. Employment loss can affect the emotional well-being of residents. In addition, the obvious impact is a loss of income, at least temporarily. This means less spending power to support other businesses and activities in a community, such as restaurants, movie theatres, sports teams and schools. Especially in the case of a forestry dependent community, a loss of employment can force relocation to another community.

Tom Burton, Director, District 4, Alberta Association of Municipal Districts and Counties

Behind the impersonal job loss statistics are human stories that are difficult to tabulate. These stories are both individual and collective. The fate of the forestry industry will have an impact on the future of hundreds of Canadian communities. According to Natural Resources Canada, some 300 communities in Canada are at least 50% dependent on the forestry industry.¹¹ The collapse of the forestry industry threatens the social fabric of these communities, going far beyond a simple column of economic figures. Psychological distress, crumbling infrastructure, reduced services and increased crime rates often plague rural communities whose dominant industry is in decline.

¹¹ Source: <http://canadaforests.nrcan.gc.ca/article/topic/183>

c) Ecological Implications

The resource is in a very weakened state today. This brings us to a point where we have to talk about lowering the cost of timber. [...] If we want to address the cost of timber, we have to redesign the forest industry. This is a very long-haul process that communities can be part of.

Cherkaoui Ferdous, Corporate Secretary, Solidarité rurale du Québec

It might seem strange to discuss ecological implications when the lack of markets is one of the main problems wood producers face. However, a low price for fibre could mean a major slowdown in silvicultural activities and sustainable forest management practices. If the competitiveness of the forestry industry were based solely on low timber costs, it might lead private woodlot owners to abandon their forest management plans and encourage the overexploitation of natural, publicly owned forests. This could have serious long-term ecological consequences.

CHAPTER III: THE FEDERAL GOVERNMENT’S ROLES AND RESPONSIBILITIES IN THE FOREST SECTOR

To properly determine possible federal government involvement in the forest sector, it is important to examine its role and responsibilities in a historical and constitutional context. The following sections look at these aspects and present recent federal initiatives in the sector.

1. Federal Roles and Responsibilities in the Forest Sector: A Historical Timeline

The following three tables present the main milestones in Canadian forestry policy, beginning with the arrival of the first Europeans in North America. Table 2 gives an overview of events in the forest sector up until the *British North America Act, 1867*. Table 3 explains how the authority granted under the Act was shared. Table 4 shows the evolution of federal forestry policy since Confederation.

Table 2 – Government involvement in the forest sector in colonial times¹²

1672	Under French rule, oak trees are de facto “nationalized” to be used exclusively for building ships for the French Royal Navy.
1721	White pine is designated for making masts for the British Royal Navy in Nova Scotia.
1775	New England sawmills want to export their wood, including white pine, to other nations, which conflicts with the British Crown’s policy of reserving white pine for the exclusive use of the government to make masts. The American Revolution increases the strategic importance of Canadian timber because Britain’s previously guaranteed supply of white pine from New England is no longer available.
1806	Napoleon’s continental blockade attempts to prevent Great Britain from trading with the rest of Europe. This blockade considerably increases British dependence on Canadian timber. By 1811, the Canadian timber trade to Britain is well established.
1826	The first timber fees for wood cut on Crown lands are put in place in Upper and Lower Canada, New Brunswick and Nova Scotia.

¹² This table is largely inspired by information from *The State of Canada’s Forests 1996–1997*, Chapter 2 “A History of Forest Legislation in Canada,” pp. 24–45.

1838-39	Tensions between New Brunswick and Maine reach their peak in the Battle of Caribou over logging rights along the Aroostook River.
1846	The lumber industry is booming: it is profitable and competition is fierce. The provinces progressively pass legislation granting tenure and licences for wood production on Crown land.
1853	Wood trade is a key element in the Reciprocity Treaty between the United States and the British colonies in North America. The Reciprocity Treaty signed in 1854 establishes free trade between the two countries.
1866	Alleged support from Great Britain to the southern Confederate states and pressure from protectionist groups leads the United States to repeal the Reciprocity Treaty.

Table 3 – Forestry and the Constitution Act of 1867¹³

CANADA'S CONSTITUTIONAL FRAMEWORK FOR FORESTS	
Provincial Jurisdiction	<p>The Constitution Act of 1867 grants ownership and legislative authority over most publicly owned forest lands to the provinces, which control 71% of Canada's total forest land and 88% of Canada's commercial forest land. Each province is given ownership of "lands, mines, minerals and royalties" (s. 109), as well as the power to legislate for natural resources and environmental management. This includes authority over the management and sale of public lands...and of the timber and wood thereon (s. 92[5]), local works and undertakings (s. 92[10]), property and civil rights in the province (s. 92[13]), and matters of a local or private nature (s. 92[16]). The exclusive provincial jurisdiction over forest resources was confirmed by a Constitutional Amendment in the Constitution Act of 1982 (s. 92A), which also enables the provinces to levy indirect taxation on natural resource revenues and provides them with significant control over the interprovincial export of resources and energy.</p>
Federal Jurisdiction	<p>The federal government's jurisdiction over forestry is based on its ownership of 23% of Canada's total forest land (mostly in the Yukon Territory and Northwest Territories) and 2% of Canada's commercial forest land. Its constitutional authority also enables it to influence forest management indirectly. This authority includes powers related to trade and commerce (s. 91[12]); Indians and lands reserved for Indians (s. 91[24]); criminal law (s. 91[27]); the general power to make laws for the peace, order and good government of Canada (s. 91 opening paragraph); and the power to make and implement treaties (s. 132).</p>

¹³ Source: *The State of Canada's Forests 1996-1997*, Chapter 2 "A History of Forest Legislation in Canada," p. 31.

Table 4 – Federal involvement in the forest sector since 1867¹⁴

1899	Position of Chief Inspector of Timber is created within the Department of the Interior. This position led to the creation of the Forestry Branch in the same department. Ten years later the branch had 40 employees and a budget of \$100,000.
1915	Official opening of the first Forest Products Laboratory of Canada at McGill University in Montreal.
1918	Opening of the Forest Products Laboratory of Canada in Vancouver.
1936	The Forestry Branch becomes the Dominion Forest Service and constitutes one of the four units within the Lands, Parks and Forests Branch of the new Department of Mines and Resources.
1949	The <i>Canadian Forestry Act</i> of 1949 authorizes the federal government to enter into cost-sharing agreements with the provinces to establish forest resource development programs.
1950	The Dominion Forest Service becomes the Forestry Branch within the new Department of Resources and Development.
1953	The Forestry Branch moves to the Department of Northern Affairs and National Resources.
1960	The Department of Forestry is established.
1966	The Department of Forestry becomes part of the Department of Rural Affairs. The focus is on regional development policies and provincial cost sharing (e.g., access road construction and mill modernization).
1968	The new Department of Fisheries and Forestry assumes responsibility for the Forestry Branch, which is now called the Canadian Forestry Service (CFS).
1971	The CFS becomes a directorate of the Department of Environment. The Canadian Council of Resource and Environment Ministers is established; the federal government begins to focus on forest regeneration and management. Subsequent federal-provincial agreements reflect this theme.

¹⁴ This table is based in part on *The State of Canada's Forests, 1996-1997*, Chapter 2 "A History of Forest Legislation in Canada," pp. 24–45; and the 1990 report by the House of Commons Standing Committee on Forestry and Fisheries, *Forests of Canada: The Federal Role*, Chapter 2A "Some Lessons from History," pp. 37–40.

1978	CFS forest products laboratories in Vancouver and Ottawa are privatized; Forintek becomes a private, non-profit corporation.
1980	The Third National Forest Congress seeks to rejuvenate federal leadership in forestry. The congress results in a series of policy statements that lay the foundation for the <u>first National Forest Strategy</u> .
1982	The federal government gives the CFS responsibility for managing federal-provincial agreements on developing forest resources. ♦ The U.S. lumber industry calls for countervailing duties to be imposed on imports of Canadian lumber; the government does not take action.
1984	The portfolio of Minister of State (Forests) is created within Agriculture Canada. The CFS is transferred to Agriculture Canada.
1986	Canada and the United States reach an agreement to impose a tax on exports of Canadian lumber.
1987	The <u>second National Forest Strategy</u> lays out the federal government's responsibilities regarding forestry, particularly trade development, public education, and research and development.
1989	The <i>Forestry Act</i> establishes Forestry Canada. The role of the new department is to promote sustainable development of Canada's forests.
1991	The Canadian government withdraws from the 1986 memorandum of agreement on softwood lumber signed with the United States and stops collecting a tax on exports to that country. The United States responds with countervailing duties.
1992	The <u>third National Forest Strategy</u> marks a turning point: forest policy now focuses on managing and promoting entire forest ecosystems, not just timber resources. ♦ The Model Forest Program is introduced to develop approaches to sustainable forest development that involve economic, environmental and social objectives, and to share the resulting knowledge and practices with the entire Canadian forest sector.
1993	Forestry Canada merges with the Department of Energy, Mines and Resources to form the new Department of Natural Resources (NRCan). ♦ The federal government withdraws from certain forest research and development activities in favour of a national science and technology policy.

1996	Federal-provincial funding agreements for forest management activities end in 1996 and 1997. ♦ The First Nations Forestry Program is introduced to provide funding and support to First Nations to participate in the forest sector. ♦ Canada and the United States agree to limit Canadian exports to the United States for five years.
1998	The fourth National Forest Strategy reiterates the major themes from the third national strategy. ♦ The four-year Value-Added Program is introduced to improve the competitiveness of the value-added wood processing industry.
2001	The United States reintroduces countervailing duties at the end of the 1996 agreement; a long series of trade disputes are brought before the World Trade Organization and the North American Free Trade Agreement authorities.
2002	The Canada Wood Export Program is launched; the national, five-year initiative is designed to develop markets and increase exports of Canadian wood products to foreign markets. ♦ The Value-Added Program is expanded and renamed the Value-Added Research Initiative (it later becomes the Value to Wood Program).
2003	The vision of the fifth National Forest Strategy is as follows: “The long-term health of Canada's forest will be maintained and enhanced, for the benefit of all living things, and for the social, cultural, environmental and economic well-being of all Canadians now and in the future.”
2006	Canada-United States softwood lumber agreement. ♦ The federal budget allocates \$400 million over two years to combat infestations of the mountain pine beetle; \$127.5 million to support the sector's long-term competitiveness; and \$72.5 million for workforce adjustment initiatives.
2007	Forintek, Feric, Paprican and the Canadian Wood Fibre Centre merge to form FPInnovations. The organization is the largest not-for-profit forest research centre in the world. ♦ The North American Wood First Initiative is launched and the Value to Wood Program is renewed.
2008	The sixth National Forest Strategy identifies two major national priorities: transformation of the forest sector and climate change. ♦ The Community Development Trust is introduced and given a \$1 billion budget (administered by the provinces and territories) to help vulnerable communities. ♦ The London Court of International Arbitration determines that Canada has contravened certain provisions of the 2006 softwood lumber agreement.

2. Federal Roles and Responsibilities in the Forest Sector: Recent Initiatives

a) The sixth National Forest Strategy

The sixth National Forest Strategy, *A Vision for Canada's Forests: 2008 and Beyond*, was released in December 2008 by the Canadian Council of Forest Ministers. The council is made up of 14 governments from the federal, provincial and territorial levels. The document contains the following vision statement:¹⁵

To be the best in the world in sustainable forest management and a global leader in forest sector innovation.

Unlike previous national strategies that had several themes, this strategy focuses on two priorities of national importance: forest sector transformation and climate change. In terms of the first priority, traditional industries (wood and pulp) will continue to play an essential role in the economy. However, transformation of the forest sector will focus primarily on new opportunities created through innovative products and technology. Climate change initiatives centre on two areas: mitigation and adaptation. Mitigation involves using the forest to increase carbon storage and thereby lessen the effects of greenhouse gas emissions. Adaptation refers to adjusting forest practices to reduce the negative impacts of climate change.

b) Additional Assistance in 2009

In view of Canada's worsening forest crisis, the federal government provided the industry with the following additional assistance in 2009:

- \$80 million over two years to Natural Resources Canada for the Transformative Technologies Program delivered by FPInnovations;
- \$40 million to Natural Resources Canada in 2010–2011 to develop demonstration projects highlighting the commercial use of new products;
- \$40 million over two years to Natural Resources Canada for the Canada Wood Export Program, the Value to Wood Program and the Wood First Program to help companies market innovative products internationally;
- \$10 million to Natural Resources Canada in 2009–2010 to support large-scale demonstrations of the “Canadian-style” use of wood for

¹⁵ *A Vision for Canada's Forests: 2008 and Beyond*, Canadian Council of Forest Ministers
(<http://www.ccfm.org/english/coreproducts-nextnscf.asp>)

Source of picture : Centre d'expertise sur la construction commerciale en bois (Cecobois)

construction in targeted offshore markets, and non-traditional uses of wood in domestic markets;



- \$1 billion to the Community Adjustment Fund (CAF), to be delivered through the federal government's regional development agencies, to support job creation in communities that have been hit hard by the global recession. Projects eligible under the CAF include reforestation and silviculture projects, investments in equipment, and initiatives to increase access to international markets;
- various initiatives to facilitate forest companies' access to credit (e.g., \$13 billion in additional funding to financial Crown corporations)_ and an increase in lending limits. The Business Development Bank of Canada also received \$100 million to establish an operating line of credit guarantee program;
- \$1 billion to help Canadian pulp and paper producers increase the energy efficiency and environmental performance of their operations. Pulp and paper companies will be eligible for a credit of \$0.16 per litre of **black liquor** produced.

3. Federal Roles and Responsibilities in the Forest Sector: Summary and Analysis

The provincial governments' exclusive jurisdiction over forest resources has an important historical foundation. Fee systems for timber cut on Crown land, which were introduced in 1826, eventually became a reliable and lucrative source of revenue for the colonies of British North America. As a condition for entering Confederation, the provinces therefore demanded that control over natural resources and the revenues from Crown lands be granted to the provincial governments. It is also interesting to note that pressure from U.S. protectionists as of 1866 contributed to the U.S. government's repeal of the Reciprocity Treaty (the term used at the time to describe free-trade agreements) with British North America. This event reinforced the need to develop east-west trade in Canada and is seen as an important catalyst for Confederation in 1867.

Although forest resources are under exclusive **provincial jurisdiction**, we can see from the chronology in Table 4 that the federal government has played an

increasingly important role in the forest sector. Its initial role focused mainly on establishing the Canadian forest laboratories to conduct research and development. Federal involvement in forestry then took the form of cost-sharing agreements under the 1949 *Canadian Forestry Act*.

Regional development policies represented indirect means of supporting the forest sector in the 1960s. In the 1970s, federal policies began to emphasize forest regeneration and development. Subsequent federal-provincial agreements focused on the same themes. The first National Forest Strategy in the 1980s was a milestone as it confirmed the federal government's role in areas under its jurisdiction, such as trade development, public education, and research and development relating to forestry. In the 1990s, the Canadian government's role focused on sustainable development and ecosystem-based management. Market development and resolution of trade disputes assumed greater importance throughout the decade. These responsibilities are still key elements of federal jurisdiction in the forest sector. It is also important to note that regional and community development programs have occupied a more central place in federal activities in recent years.

This historical overview allows to define the federal government's major areas of involvement in forestry:

- research and development;
- sustainable development, ecosystem-based management and climate change;
- regional and community development;
- development of international markets and resolution of international trade disputes

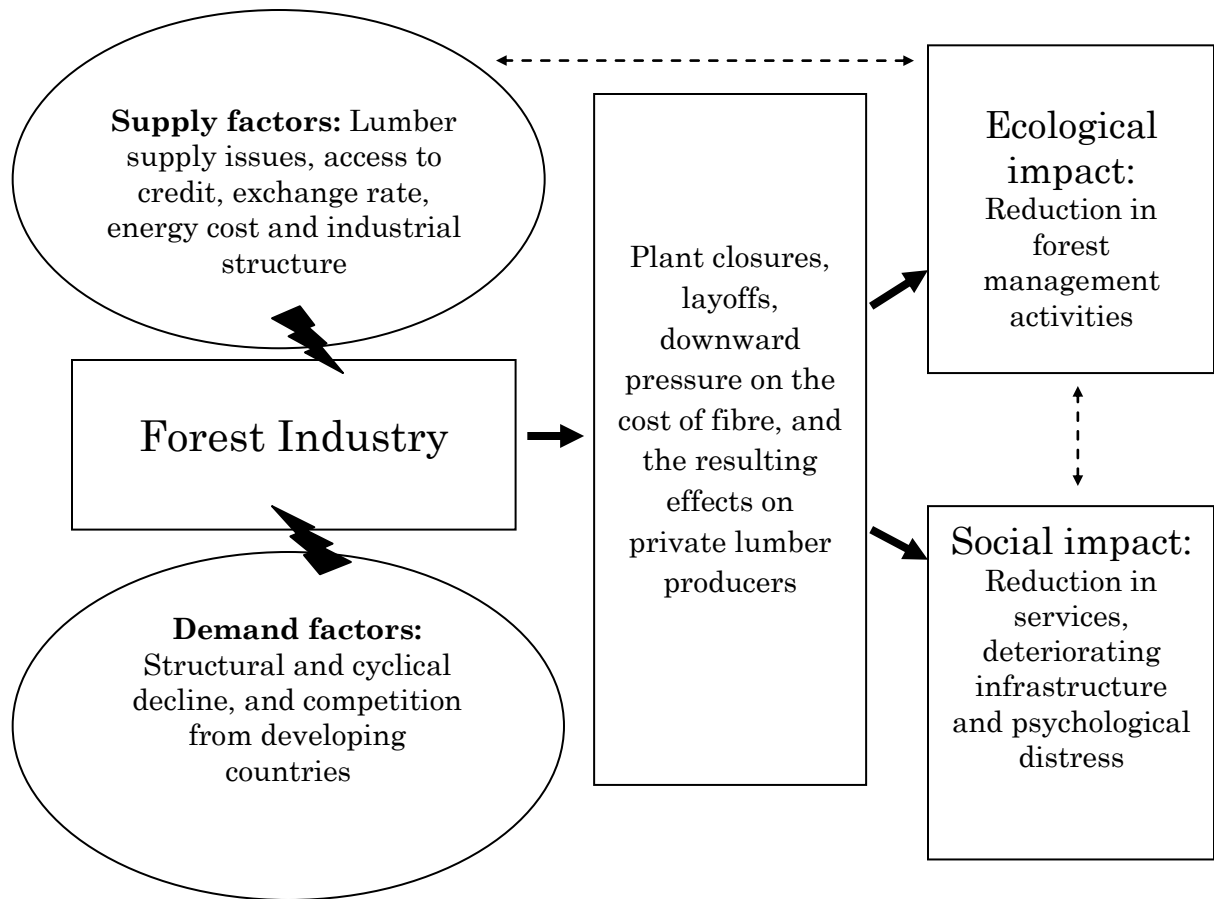
CHAPTER IV: CONTINUATION OF THE STUDY

This section presents themes that the Committee will explore as it continues its study and formulates recommendations to the government for immediate action. In light of the preceding analysis, certain statements can be made that will serve as guidelines for identifying issues for further study:

- The causes of the problems facing the various sub-sectors of the forest system are so diverse that we can appropriately talk about the *crises within the forest system*.
- Any forest policy must strike the right balance between the economic, ecological and social roles of the forest.
- Any government intervention must take into account how the various sub-sectors of the forest system interact with one another so as not to create any undue bias towards a particular user.
- Although the provinces have exclusive jurisdiction over forest resource management, the federal government has been playing an ever-increasing role in the forest sector in recent years.
- The federal government, along with the 13 provincial and territorial governments, adopted a new National Forest Strategy in 2008. The strategy sets out two national priorities: **climate change** and **industry transformation**.

The federal government can try to tackle the causes of the forestry crises directly or try to mitigate their effects. Figure 3 illustrates the causes and effects of the forestry crises. The causes are broken down into two categories: supply factors and demand factors. Potential intervention by the federal government is examined based on these factors. Although Figure 3 lists timber supply as a supply factor, it should be noted that timber supply does not fit neatly into a single category. The crises in the forest system can have a negative impact on investment in forest management thus worsening timber supply problems in the longer term. Therefore, timber supply can be considered both a cause and an effect of the crises in the forest system; timber supply is covered in a separate section of this chapter.

Figure 3 - The causes and effects of the forestry crisis



Source: Parliamentary Information and Research Service, Library of Parliament

1. Possible Actions to Influence Demand Factors

In the short term, we must develop the Canadian market and increase the use of wood in commercial buildings. For example, the federal government could put in place a policy to encourage the use of wood in its structures.

Carl-Éric Guertin, Communications Director, Quebec Wood Export Bureau

One key component is looking at beginning to work through the cogeneration and the energy process by using biomass and wood products to generate energy. That will spur on a whole world of new technology.

Mark Arsenault, President and CEO, New Brunswick Forest Products Association

It is also important to develop new markets for low-quality wood so that we can use all our resources.

Jean-Pierre Dansereau, Director General, Fédération des producteurs de bois du Québec

(...) architects and engineers — the specifiers — are trained to design with steel and concrete. They make decisions on the building material, and, typically, it is not wood. It requires a tremendous effort to convert any job to wood from steel or concrete once the design is finished. Considering that commercial buildings are our — and, by association, the forestry sector's — biggest opportunity to grow in the construction field, we must convince specifiers to use wood in the early stages of projects.

Jerry Cvach, Executive Secretary, Canadian Wood Truss Association

We have to encourage the use of more wood in building products. (...) The federal government has a key role to play in helping industry to diversify by finding new uses for wood products.

Robert Matters, Chair, Steelworkers Wood Council, United Steelworkers

Among the many reasons why they [Southeast Asian exporters] can sell their products so cheap is that they have low wages. (...) In other instances, we do not know where the wood comes from; it is "black wood," as in black market.

Robert Kiefer, Vice-President, Government Relations, Commonwealth Plywood Ltd, Canadian Hardwood Plywood and Veneer Association

Government measures alone, no matter how innovative, will not be enough to kick-start the demand for newsprint or the construction market. Other options need

to be explored. The Committee notes that a number of witnesses stressed the importance of **creating** demand, not kick-starting it. This approach consists of promoting the demand for wood products through new construction standards, better communication with architects and engineers in the commercial sector, and more extensive marketing and advertising efforts. During his testimony, in May 2009, Mr. Jerry Cvach, Executive Secretary of the Canadian Wood Truss Association, stressed the need to convince and train professionals in the non residential construction industry to use wood. With respect to marketing, it should be noted that these measures are not intended solely to help the industry; wood is in fact the best choice from an environmental standpoint. Life-cycle analyses of wood as a building material have shown that wood uses the least amount of energy, and generates the least amount of greenhouse gases and air pollution.¹⁶ However, the Senate committee regrettably notes that this scientific evidence does not match the public's perception.

In addition, public opinion often holds that logging is by definition bad for the environment when, in fact, logging—practiced according to sustainable forest management rules—can increase the forest's capacity to store carbon. Currently, there are a number of federal initiatives in place to help export and promote Canadian wood to foreign markets, initiatives that the Senate committee fully supports. Nevertheless, the Senate committee feels that more could be done to promote the use of Canadian wood domestically. For example, it may be appropriate to put forward a national strategy on the use of wood as a building material of choice in Canada.

Proposal 1

For the continuation of the study, the Senate committee undertakes to examine more closely the advantages of using wood as a building material in the non residential sector and will propose methods for promoting its use within Canada.

Regarding the role of building codes in increasing the use of wood in the non residential construction sector, the Senate committee is conscious of the significant role of the provinces in this aspect and notes the importance of having an integrated federal-provincial approach. Given the typically long process in changing and revising codes, the Senate Committee is convinced that the sooner this subject is

¹⁶ Based on the findings in the presentation by Bill Love, Chairman of the Board, Canadian Wood Council, at an open meeting of the Standing Senate Committee on Agriculture and Forestry on April 23, 2009.

placed on the agenda of Federal-Provincial ministerial meetings, the better. Therefore:

Recommendation 1

The Senate committee recommends that the Minister of Intergovernmental Affairs undertakes to place the issue of the harmonisation of building codes across Canada in order to facilitate the use of wood in the non residential sector on the agenda of future Federal-Provincial Ministerial meetings.

Whether one is in favour or against the softwood agreement reached in 2006 between Canada and the United States, one thing is certain: growing the market for wood products internationally is to the benefit of both countries. In this regard, the Senate committee would like to stress the importance of establishing a partnership with the United States that would seek to grow the demand for wood products on international markets. While developing the market for innovative products in North America is important, Asian countries, like China and India, also represent a fantastic market opportunity for both Canada and the United States.

Proposal 2

For the continuation of the study, the Senate committee will liaise with U.S. officials in order to establish a cooperative approach between the two countries with the goal of growing the demand for wood products in North American and emerging markets.

In relation to climate change, several witnesses appearing before the committee suggested that governments should put forward policies to encourage the use of forest biomass in space heating. These witnesses testified that such measures would help increase the demand for sawmill by-products and low-quality wood, fight climate change and create more jobs locally as compared with the use of fossil energies. Other witnesses, however, had reservations, saying that if the government encouraged the use of wood chips and sawdust in energy production, it could

negatively impact those currently using sawmill by-products, namely pulp mills and panel producers.

Furthermore, some witnesses expressed concerns about the number of jobs created by wood pellet plants as compared with alternative uses of wood chips and sawdust. Despite these issues, the Senate committee believes that a more thorough examination of the advantages and potential disadvantages of using forest biomass (for example, sawmill by-products and low-quality wood) for space heating or electricity production is necessary before the committee can make any concrete recommendations for government measures. Moreover, the committee notes that the experiences of certain European countries, particularly Sweden, would serve as useful case studies with respect to promoting and encouraging wood pellet heating.

Proposal 3

For the continuation of the study, the Senate committee undertakes to weigh the advantages and disadvantages of using government measures to promote the use of forest biomass (such as sawmill by-products and low-quality wood) in heating, electricity generation and biofuels production. Further to this analysis, the Senate committee will make recommendations to the federal government.

Regarding the drop in demand for wood products due to increasing competition from developing countries, the Senate committee notes that some witnesses suggested imposing import tariffs on finished wood products such as furniture, floors and decorative hardwood plywood. However, the Senate committee is of the opinion that unilaterally imposing increased import tariffs could violate Canada's international obligations vis-à-vis the World Trade Organization and free trade agreements. Such a move could rapidly lead to a trade war in which Canadian exports would be the target of reprisals, a situation where all sides could end up losing. Consequently, at this time, the Senate committee does not favour the imposition of import tariffs on finished wood products from Asia. Nevertheless, it believes that the Canadian government is justified in imposing minimum environmental conditions on finished wood imports, such as requiring products to be free from contraband wood. The use of contraband wood is a serious problem in certain developing countries. The importation of products made of contraband wood negatively impacts the Canadian forest sector and the furniture industry in particular. The onus of proof that the

wood comes from a legitimate source should rest with the exporter, not the importing country. Therefore:

Recommendation 2

The Senate committee recommends that the Department of Foreign Affairs and International Trade impose minimum environmental conditions on wood product imports such as proof that contraband wood was not used.

2. Possible Actions to Influence Supply factors

One of the things that I have thought of is that we have a history of a Farm Credit Corporation in Canada, which was put in place specifically to provide credit where banks did not want to provide credit, to a sector that they did not have much trust in. It has been particularly useful for farmers to run and build their businesses. Maybe we need a Canadian forest credit corporation that will help us to rebuild the industry here.

Andrew Clark, President, New Brunswick Federation of Woodlot Owners

The Senate committee is well aware of the negative impact of the exchange rate and energy prices on the forest sector, but governments have a very limited ability to influence these factors directly. Nevertheless, the government clearly has a role to play in helping the industry adapt to these new economic conditions. Therefore, the committee commends the recently announced federal initiative to grant green subsidies to Canadian pulp producers. These subsidies are conditional upon environmental improvements, either in the form of energy efficiency or environmental performance of pulp operations.

Although the committee also recognizes the efforts that the Canadian government has made to improve access to credit, it is clear that it is still extremely difficult for forestry companies to access credit. This is a very sensitive issue for the government from an economic standpoint. Governments must compensate for the market's failures when companies are denied credit or made to pay very high interest rates

for reasons that may not be commercially valid. For example, banks may prefer to hoard capital instead of lending it, or they may not want to lend to a particular company simply because it belongs to an industry that is at risk. It should also be noted, however, that it would be a mistake for governments to force institutions to make credit available to companies that are not commercially viable. It is important to remember that one of the leading causes of the financial crisis and ensuing global recession was the widespread practice of granting very high-risk loans in the United States. Therefore, governments must be careful not to force institutions to make credit available to businesses that would not be profitable regardless of the loan conditions. The goal of any government intervention should be to ensure that forestry companies have fair and equitable access to credit based on business criteria. Testifying before the Senate committee, the vice-president of Export Development Canada (EDC), a Crown corporation, described EDC's lending policy as follows:

*It is important to note that EDC operates in the commercial sphere, just like any bank. Like any bank, our customers must be credit-worthy, they must be recourse-worthy and we must believe in their business plan and understand how they will repay our loans over time.*¹⁷

EDC has a policy of not competing in the same market segments as private chartered banks. Thus, if chartered banks become overly cautious in their traditional market segments by imposing very high interest rates or by denying access to credit for reasons that are not commercially valid, the following question must be asked: which financial institution will step up? Some of the comments made by EDC's vice-president suggest that there is little competition between chartered banks in the forest sector:

*Unfortunately, I would say that many of our customers, especially some of the smaller and mid-size ones, are now viewed to be much riskier prospects. Many people would say we have to increase rates to that level. There is very little competition for forestry business, as you can imagine, amongst lenders today. Therefore, they are probably paying, on average, higher than many other sectors. Unfortunately, however, it is not out of line with the kinds of risks people face. The markets are so significantly depressed that it is almost anyone's guess as to when they come back for some parts of the industry. Therefore, the risks are almost unquantifiable for some lenders. They will look at that and say, "Well, if I cannot be sure, either I say no or I want 25 per cent." It would not be an unheard of conversation, I am sure. It is very difficult for smaller companies.*¹⁸

¹⁷ Carl Marcotte, Vice-President, Resources Group, Export Development Canada, Proceedings of the Standing Senate Committee on Agriculture and Forestry, Issue 6 – Evidence – Meeting of June 9, 2009

¹⁸ Ibid.

In the agricultural sector, this issue was resolved by having Farm Credit Canada (FCC) compete directly with chartered banks. Furthermore, FCC is a commercial success given that it is a fully self-financed Crown corporation that has generated \$212 million in profits and posted growth for the 16th consecutive year as of 2008–2009. The committee believes that it is time to consider the possibility of creating a “Forest Credit Canada” that would be involved in market segments where there is little competition between chartered banks. Therefore:

Recommendation 3

The Senate committee recommends that the Department of Natural Resources, together with the Minister of Finance, explore the possibility of creating a viable “Forest Credit Canada” entity in order to compensate for the lack of competition between chartered banks in certain market segments.

In terms of the industry’s structure as a cause of the current forestry crisis, the committee notes that the structure is currently undergoing significant changes. In this particular case, the government should focus more on trying to lessen the impacts of these changes on the families and communities in question, than on trying to prevent or reverse the changes to the forest sector’s industrial structure. During meetings of the Senate committee, industrial structure was among the most frequently cited leading causes of the forestry crisis; thus, the government would be ill advised to go to great lengths to keep that structure intact. The Senate committee notes that the Community Development Trust and the initiative to facilitate workforce adjustments included in the 2006 Budget, as well as the Community Adjustment Fund announced in the 2009 Budget, are good examples of programs designed to help workers and communities survive the restructuring of the forestry industry without trying to stop it.

One measure, however, that the federal government could adopt immediately to improve structural competitiveness in the forestry industry would be to make the tax credit for scientific research and experimental development (SR&ED) fully refundable for all firms. Currently, this tax credit is refundable only for small Canadian-controlled private corporations (CCPCs), with taxable income of up to \$400,000 and taxable capital of up to \$10 million. Investment tax credits earned by a Canadian corporation that is not a CCPC is non-refundable, but may be used to reduce any taxes payable (i.e., a business that is not profitable cannot claim the

credits, and must carry the credits forward for use at a future time when the business returns to profitability). There is a certain paradox in requiring that a business be profitable before it can take advantage of the program since a company may decide to invest in research and development precisely because it is generating losses and in an effort to return to profitability. The Senate committee feels that this situation should be rectified. Therefore:

Recommendation 4

The Senate committee recommends that the Department of Finance make the scientific research and experimental development tax credit fully refundable for all classes of companies.

The Senate Committee also wishes to stress the importance of investing in research and development today as a fundamental criterion for ensuring the industry's success in the future. In particular, commercialisation and mass production of new, innovative products could be an important structural factor for the industry in the medium term.

Proposal 4

For the continuation of the study, the Senate committee will look at how to improve research and development efforts in the forest sector in Canada with a particular emphasis on how to speed up the commercialisation of products resulting from research and development initiatives.

3. Managing the Causes and Effects of the Crises: Forest Management, Value-Added Activities and Community Involvement

(...) the federal government should embrace the principles of the New Relationship and efforts to harmonize and fully engage First Nations in the forest sector through shared decision-making and jurisdiction regarding the access to and use and management of forest resources and natural resources in general.

Keith Atkinson, CEO, BC First Nations Forestry Council

The public perception has been that forest preservation is the means to combat climate change and the cutting of any trees is a bad thing to do, when in fact sustainably-managed forests have been shown to sequester more carbon and forest products are generated from a renewable resource, have negative net emissions through their processing and retain carbon throughout their lifespan. Wood products are a wise ecological choice for consumers, especially when compared to other building products like steel, concrete and plastics. (...) Forest owners that make personal investments in the long-term productivity of their forest are actually penalized by the income tax system in Canada, which does not recognize a small-scale forest as a business investment, as they do with farm properties. I would argue that forests are just as deserving of favourable income tax treatment with respect to investment because of the ecological function of these lands throughout their life cycle.

Carla Grant, Executive Director, Ontario Forestry Association

There needs to be assistance with certification in order to meet market needs. (...)The establishment of a community energy investment fund would give communities the opportunity to acquire equipment and set up infrastructure to use lumber for energy production at the local and regional level

Jean-Pierre Dansereau, Director General, Fédération des producteurs de bois du Québec

It is entirely possible that the value of the water, the carbon-neutral energy and the other bioproducts that are produced from Canada's forests now equal or exceed the value of the fibre. The problem is obviously that we do not have markets for all of those things. If you think for a minute about what it would take to replace the drinking water that comes from Canada's forests, I think you can make a good argument that the value of the water may be as high as or higher than the value of all the pulp, paper and lumber we produce.

Don Floyd, Chair, Canadian Institute for Forest Policy and Communications,
University of New Brunswick, Faculty of Forestry and Environmental Management,
as an individual

In short, we do not want to go forward with the same vulnerabilities that led to the current state of the forest industry. Our focus is on improving the well-being of communities and the diversity of the forest and not on revitalizing the traditional forest industry. The barriers to diversification, adaptation and transformation must be addressed, and community-based management planning can provide a tenure option capable of dealing with these barriers.

Joseph LeBlanc, Student, Northern Ontario Community Economic Development
Network

As previously mentioned, timber supply is not an immediate concern given the collapse of demand, as well as the temporary wood surplus created by the mountain pine beetle infestation in the West. Nevertheless, the committee notes that timber supply is a long standing issue, one that has certainly contributed to the current crises and has the potential to hold up the recovery of business activities. On the one hand, the industry's current slump could in fact bring about a major slowdown in forest management activities, a situation that would have obvious long-term effects on timber supply. On the other hand, an attempt to restore the industry's ability to compete by drastically reducing the cost of fibre would likely have a positive impact on the size of the industry in the very short term. However, such a measure could worsen timber supply problems in the longer term, be extremely detrimental to private woodlot producers and more than likely revive the softwood lumber dispute with the United States.

The Senate committee is of the opinion that these scenarios must be avoided. The time to invest in forest management activities is now, and the federal government has a clear role to play in promoting and encouraging best practices. Much has already been done; Canada is the undisputed world leader in forest certification.

Thus, it would be all the more damaging if the current forestry crises jeopardized past efforts.

For example, La Grappe agroénergétique des Coteaux plans to set up a trust to purchase abandoned land in order to prevent speculation and invest in the establishment of energy plantations. A contribution to the trust from the Government of Canada would be very helpful in attracting substantial private investment. The Government of Canada would thus be promoting a new rural development option.

Charles Provost, Director, La Grappe agroénergétique des Coteaux

First and foremost, it is essential to set out clear guidelines for any potential federal intervention. As mentioned by a Senate committee witness, federal and provincial policies must favour the development of productive and diverse forests that contain quality wood and that are capable of sustaining a range of activities, including a diverse processing industry. It is the Senate committee's opinion that federal investments should also take into account the forest's three primary roles and thus reflect economic, social and ecological objectives. Economically speaking, it is clear that larger investments in forest management would likely improve long-term timber supply and therefore strengthen the industry's ability to compete.

From an ecological standpoint, faster tree growth rates help to increase the forest's ability to absorb carbon. Moreover, compensation for the environmental goods and services that forests provide would finally attach monetary recognition to their ecological role, recognition that is sorely lacking within traditional market mechanisms. When it comes to the social role of the forest, a recent compilation by Natural Resources Canada¹⁹ shows that the communities that do the best job of weathering threats to their resource industry are those that take an active role in monitoring, planning and engaging in local economic activities. Similarly, community involvement is key to Aboriginal communities. A Senate committee witness testified that locally owned sawmills with value-added activities demonstrated the greatest determination in the face of the industry's problems.

A number of witnesses suggested measures that the federal government could adopt to promote community involvement in forest management and encourage investment in value added-activities. The Senate committee would like to examine these diverse options in more detail before making any firm recommendations. In addition, the Senate committee recognizes that the provinces have a leading role

¹⁹ *Forest Communities: Weathering Economic Change*, August 2008, Natural Resources Canada, <http://canadaforests.nrcan.gc.ca/article/economicreliance/?lang=en>

when it comes to forest management and thus notes the importance of a coordinated approach.

Proposal 5

For the continuation of the study, the Senate committee undertakes to identify the best tools available to the federal government to encourage best forest management practices, support value-added activities and promote community involvement, in an effort to strengthen the economic, ecological and social roles of Canada's forests.

Areas that will be studied in more detail include:

- **help for best forest management practices;**
- **personal silvicultural savings and investment plan for private woodlot owners;**
- **support for environmental certification and “tree to finished product” traceability initiatives;**
- **compensation for environmental goods and services provided by woodlot owners;**
- **an investment fund pool to encourage the involvement of communities in local forest management and to support value-added activities.**

CONCLUSION

The purpose of this interim report by the Standing Senate Committee on Agriculture and Forestry was to identify the issues to be addressed by the Senate committee as part of its ongoing work on the study in the fall of 2009 and the spring of 2010, and to formulate specific recommendations to the government for immediate action. To that end, Chapter I provided a brief overview of the roles and historical importance of Canada's forests. Chapter II examined the leading causes of the forest system crises, and Chapter III presented the historical roles and responsibilities of the federal government. Lastly, Chapter IV formulated recommendations and specified areas that the Senate committee will explore as it continues its work.

Four recommendations were presented in Chapter IV. Three of them address the immediate problems facing the industry—access to credit, “unfair” import competition and the tax credit for research and development. One recommendation deals with the long-term goal of harmonizing the provincial building codes in Canada in order to facilitate and increase the use of wood in the non-residential sector. The proposals for the continuation of the committee's work, also included in Chapter IV, are designed to evaluate and explore possible long-term policies for the industry. These policies include:

- the promotion of wood as a building material of choice in the non residential sector;
- a cooperative approach with the United States to grow the market for wood products internationally;
- the use of wood waste and forest by-products for energy generation;
- improving research and development efforts;
- and finally, developing a national strategy to encourage forest management activities, the development of value-added products and involvement of local communities in an effort to strengthen the economic, ecological and social roles of Canada's forests.

The Standing Senate Committee on Agriculture and Forestry plans to present its findings on these issues in a final report to be tabled in 2010.

APPENDIX: WITNESSES

ORGANIZATION	NAME, TITLE	DATE OF APPEARANCE
Alberta Association of Municipal Districts and Counties	Tom Burton, Director, District 4	May 12, 2009
	Gerald Rhodes, Executive Director	May 12, 2009
As individuals	Tom Beckley, PhD, University of New Brunswick, Faculty of Forestry and Environmental Management	May 26, 2009
	Don Floyd, PhD, Chair, Canadian Institute for Forest Policy and Communications, University of New Brunswick, Faculty of Forestry and Environmental Management	May 26, 2009
	Jeremy Williams, PhD, Forestry consultant, Registered Professional Forester in Ontario	May 26, 2009
Atlantic Association of Community Business Development Corporations	Basil Ryan, Chief Operating Officer	May 12, 2009
BC First Nations Forestry Council	Keith Atkinson, CEO	June 16, 2009
Canadian Bankers Association	Terry Campbell, Vice-President, Policy	June 18, 2009
	Marion G. Wrobel, Director, Market and Regulatory Developments	
Canadian Council of Furniture Manufacturers	Terry Clark, President	May 28, 2009

ORGANIZATION	NAME, TITLE	DATE OF APPEARANCE
Canadian Federation of Woodlot Owners	Peter deMarsh, President	April 23, 2009
	Jean-Pierre Dansereau, Director General, Fédération des producteurs de bois du Québec	
Canadian Hardwood Plywood and Veneer Association	Steve Umansky, President	May 7, 2009
	Michel Tremblay, Executive Vice-President	
	Robert Kiefer, Vice-President, Government Relations, Commonwealth Plywood Ltd	
	Christian Noël, General Manager, Columbia Forest Products	
Canadian Institute of Forestry	John Pineau, Executive Director	April 28, 2009
Canadian Kitchen Cabinet Association	Caroline Castrucci, President	May 5, 2009
	Richard Lipman, Board Member	
Canadian Wood Council	Bill Love, Chairman of the Board	April 23, 2009
Canadian Wood Truss Association	Jerry Cvach, Executive Secretary	May 5, 2009
Coast Forest Products Association	R.M. (Rick) Jeffery, President and CEO	June 16, 2009
Communications, Energy and Paperworkers Union of Canada	Guy Caron, National Representative for Special Projects	May 7, 2009
Department of Natural Resources of New Brunswick	Tom Reid, Deputy Minister	June 2, 2009

ORGANIZATION	NAME, TITLE	DATE OF APPEARANCE
Export Development Canada	Carl Marcotte, Vice-President, Resources Group	June 9, 2009
Fédération des producteurs de bois du Québec	Pierre-Maurice Gagnon, President	June 4, 2009
	Jean-Pierre Dansereau, Director General	
Forest Products Association of Canada	Avrim Lazar, President and CEO	April 23, 2009
Independent Lumber Remanufacturers Association	Russ Cameron, President	June 16, 2009
Justice Canada	Éric P. LeBlanc, Legal Counsel, Legal Services	June 11, 2009
La Grappe agroénergétique des Coteaux	Charles Provost, Director	May 14, 2009
National Aboriginal Forestry Association	Harry Bombay, Executive Director	April 28, 2009
Natural Resources Canada	Jim Farrell, Assistant Deputy Minister	April 21, 2009
New Brunswick Federation of Woodlot Owners	Andrew Clark, President	June 2, 2009
New Brunswick Forest Products Association	Mark Arsenault, President and CEO	June 2, 2009
Northern Ontario Community Economic Development Network	Joseph LeBlanc, Student	May 14, 2009
Ontario Forestry Association	Rob Keen, President	May 28, 2009
	Carla Grant, Executive Director	
Quebec Forestry Industry Council	Yves Lachapelle, Forestry Director, Special Advisor Strategic Issues	June 4, 2009

ORGANIZATION	NAME, TITLE	DATE OF APPEARANCE
Quebec Wood Export Bureau	Carl-Éric Guertin, Communications Director	June 4, 2009
Rural Ontario Municipal Association	Eric Rutherford, Member, President of the Ontario Good Roads Association	May 14, 2009
Solidarité rurale du Québec	Claire Bolduc, President	May 14, 2009
	Cherkaoui Ferdous, Corporate Secretary	
United Steelworkers	Robert Matters, Chair, Steelworkers Wood Council	May 7, 2009