



**HOUSE OF COMMONS  
CANADA**

# **CANADA'S FOREST INDUSTRY: RECOGNIZING THE CHALLENGES AND OPPORTUNITIES**

## **Report of the Standing Committee on Natural Resources**

**Leon Benoit, MP  
Chair**

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# **THE STANDING COMMITTEE ON NATURAL RESOURCES**

has the honour to present its

## **THIRD REPORT**

Pursuant to its mandate under Standing Order 108(2) and the motion adopted by the Committee on December 11, 2007, the Committee has studied the unique opportunities and challenges facing the forest products industry and has agreed to report the following:

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# CANADA'S FOREST INDUSTRY: RECOGNIZING THE CHALLENGES AND OPPORTUNITIES

## INTRODUCTION

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Many people see Canada as a country of water and woodland, a resource-rich country. With the third-largest area of forested territory in the world, Canada is indeed the classic example of a country whose development and inhabitants' well-being have, to a very great extent, been built on the wealth of its forests, thanks to a solid forest products industry found right across the country. However, because of structural and conjunctural factors, the Canadian forest products industry is now going through what many observers consider is the worst crisis in its history. Exports are falling, plants and mills are closing and jobs are being lost: all signs of an industry in transition and of communities seeking better times.

Given the scale of the crisis affecting Canada's forest products industry, the House of Commons Standing Committee on Natural Resources agreed in December 2007 to undertake a review of the opportunities and challenges facing the industry. By so doing, the Committee sought to contribute to the implementation of a market-driven action plan that would make it possible to lay the groundwork for the industry's renewal, prosperity and sustainability. To achieve this goal, the Committee held eight meetings between February and April 2008, at which it received evidence from some 25 organizations and individuals representing various spheres of forest industry activity and various perspectives on the industry as a whole.

This report outlines the chief characteristics of the forest resource and of Canada's forest products industry. It describes the crisis that the industry is currently experiencing, identifies the key causal factors, and highlights the impact of the crisis on forest communities. Lastly, it defines the factors likely to contribute to a resolution of the crisis so that the Canadian forest products industry can once again become prosperous, efficient and sustainable for the benefit of all Canadians.

The Committee is cognizant of the overall complexity of the current crisis affecting the Canadian forest products industry. In its study, the Committee decided to approach that crisis in a comprehensive manner, while mindful of the respective jurisdictions of the federal, provincial, territorial and Aboriginal governments.

# CHAPTER 1 — THE FOREST RESOURCE AND THE FOREST INDUSTRY IN CANADA

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## The Forest Resource

Covering more than 400 million hectares, or about half the country's total area, Canada's woodlands account for 10% of our planet's treed areas, and 30% of its boreal forest. But not all of Canada's woodlands are suitable for so-called commercial activities, in other words capable of producing forest products. It is estimated that commercial forest developed for industrial purposes covers just over 140 million hectares, less than one million of which is harvested every year. Another 150 million hectares of commercial forest remains untouched and has not been developed for production. This leaves close to 110 million hectares of non-commercial forest, better suited to non-timber values, where it is unlikely that commercial logging will ever take place.

The country's forest regions are classified by type of cover, as defined by the proportion of softwood (conifers) they contain. Softwood cover, concentrated mainly in the north and predominant in British Columbia, accounts for the largest area (66%). Mixed woodland, which is found in the Maritimes, central Quebec, Ontario and the Prairies, ranks second in area with 22%. Hardwood forests (mainly birch and maple) account for 12% of the total wooded area, in a wide band across southern Quebec and Ontario that narrows in southern Manitoba and Saskatchewan and widens again in Alberta, where poplar and aspen predominate.

British Columbia, Ontario and Quebec share almost 60% of Canada's inventoried productive forest land. The Prairie Provinces have just under 25%, and the four Atlantic Provinces almost 10%. About 93% of Canada's forested territory is Crown land, managed by governments: the provinces hold 77% and the federal government 16%. In Nova Scotia and Prince Edward Island, woodland belongs mainly to private owners. Federal Crown land is found especially in Yukon and the Northwest Territories, which, although they form 39% of the country's total surface area, have only 9% of non-protected productive woodland.

Private woodlots, which represent over 7% of the country's productive woodland, belong to some 450,000 owners, including individuals, families, corporations and communities. About 80% of these private woodlots are located east of Manitoba, most in the Maritimes and in Quebec. Their importance is by no means negligible; in fact, in these regions, they are located close to mills and processing plants, and they provide more wood than their proportion of forested area would suggest. For example, in Quebec the roughly 130,000 owners of private woodlots occupy 11% of the forest land base, but contribute more than 20% of the timber supplied to mills.

Under the Constitution, the provinces have management responsibility over the natural resources within their territory. This means it is the provinces that hold and manage forests on Crown lands within their borders, develop legislation, regulations and policies, issue logging permits, collect stumpage fees and compile forestry data. In the three territories, it was until very recently the federal government that managed natural resources. However, discussions and negotiations have now led to the implementation of a devolution process for entrusting these responsibilities to the territorial governments.

It is also important to state that environmental protection is not specifically mentioned in the *Constitution Act, 1867*. In practice, the environment is a matter of shared jurisdiction between the federal and provincial governments.

The federal government's responsibilities include trade and international relations, Aboriginal affairs, management of federal lands, and environmental protection. Over the years, Ottawa has played a leading role in research, particularly on control of the pests and diseases that attack the country's vast stands of trees, and more recently on global issues such as climate change.

The federal government also plays a role in helping to build consensus amongst stakeholders on important forest-related issues. The federal government notably works in a co-operative and collaborative manner with provincial and territorial governments through the Canadian Council of Forest Ministers (CCFM). The CCFM provides leadership on national and international issues, and sets direction for the stewardship and sustainable management of Canada's forests. Among other things, it is responsible for the National Forest Information System and the National Forestry Database Program, the Canadian Criteria and Indicators Framework, and the development of the next National Forest Strategy.

Canada is one of the few developed nations that still have vast natural forests untouched by human activity. This privileged situation, however, gives it a stewardship role in the eyes of many Canadians and of the international community. There are those who consider that greater protection should be given to Canada's forests, which includes a continued focus on sustainable forest management practices by industry and governments.

## **Canada's Forest Economy**

In 2006 the forest sector contributed \$36.3 billion to Canada's gross domestic product (GDP), which represents approximately 3% of Canada's total GDP. That same year, over 300,000 Canadians were directly employed in the industry, and another 500,000 to 600,000 indirectly depended on the forest industry for their employment.

Canada's forest industry is oriented toward foreign markets. No country in the world exports more wood products than Canada. Predictably, the bulk (78%) of Canada's exports of wood and wood products goes to the United States. In 2006, total exports of primary

wood products (logs, pulpwood, etc.) were valued at \$980 million, total exports of wood-fabricated materials (lumber, plywood, etc.) were valued at \$16.4 billion, and total exports of pulp and paper products were valued at \$20.9 billion. All told, the value of Canada's forest products exports exceeded \$38 billion dollars. Canada's forest industry also contributed some \$28 billion to Canada's trade surplus.

Canada's forest industry plays a central role in many rural and remote communities. Natural Resources Canada (NRCan) reports that there are over 300 such communities across the country that are economically dependent<sup>1</sup> on the forest industry. The Committee is cognizant that the well-being of rural Canada and that of the Canadian economy more generally depends significantly on a strong and vibrant forest products sector.

The nature and type of forest sector activities vary from region to region and from community to community, and reflect the comparative advantages of these various areas. Communities in Western Canada tend to specialize in the manufacturing of wood products (e.g., lumber) while those in Ontario, Quebec and the Atlantic Provinces are involved in everything from softwood lumber to pulp, paper and newsprint manufacturing. Forest biomass, meanwhile, has emerged as an important source of energy across Canada. Over half of the total energy used by Canada's forest industry for heating and for its manufacturing processes is derived from biomass (waste byproducts, sawdust, bark, etc).

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1 Economically dependent communities are defined as those where the forest sector makes up at least 50% of the economic base of these communities. Source: Natural Resources Canada, *The State of Canada's Forests 2007*.

## CHAPTER 2 — AN INDUSTRY IN CRISIS

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Canada's forest products industry is currently in the midst of one of the most difficult periods it has ever faced. As John Allan, president and CEO of the Council of Forest Industries, put it in his appearance before the Committee, "the industry is in a crisis of unprecedented proportion."<sup>2</sup> More than ever, it appears that large-scale structural adjustments will be necessary if the industry is to adjust to, and eventually move beyond, the current downturn.

Natural Resources Canada reports that since 2003, over 300 plants (pulp mills, paper machines, sawmills, etc.) have closed, and approximately 33,000 mill jobs have been lost.<sup>3</sup> Job losses have accelerated through 2006 and 2007. The type of jobs lost varies from region to region and from province to province. Overall, since 2003, roughly one-third of the job losses in the forest industry occurred in Quebec.

### Canadian Forest Industry Layoffs by Province January 2003 to January 2008

British Columbia	6,297
Alberta	1,247
Saskatchewan	1,364
Manitoba	15
Ontario	8,582
Quebec	11,329
New Brunswick	3,149
Nova Scotia	380
PEI	35
Newfoundland and Labrador	482
Canada (Total)	32,880

Source: Natural Resources Canada.

Plant closures and job losses have also had a ripple effect throughout the economy. Businesses that supply products and services to forest products companies are also negatively impacted by the crisis.

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2 John Allan, Council of Forest Industries, *Committee Evidence*, March 4, 2008.

3 Note that these figures do not include jobs lost in the forestry and logging sector.

These plant closures and job losses have had important socio-economic impacts; dozens of communities that are dependent on the forest industry for their survival face an uncertain future. The Committee received testimony from a number of forest community mayors and reeves that these closures and job losses are having a significant social and economic impact on their communities. Families are being dislocated, health and education services are eroding, and municipal infrastructure is not being renewed in many such communities.

Jim Scarrow, Mayor of the City of Prince Albert, Saskatchewan, told the Committee that Prince Albert has already lost in excess of \$3.3 million in annual tax revenue as a result of mill closures. Enrolment in local schools has also declined considerably. One estimate puts the loss in the number of students at over 1,000 throughout Prince Albert's school system.<sup>4</sup>

Community leaders and labour leaders who appeared before the Committee generally espoused the view that governments have not acted with sufficient haste, nor have they provided adequate resources, to help the many communities significantly affected by the downturn in the forest products industry. As Joe Hanlon put it in his appearance before the Committee:

The people of White River and Dubreuilville and other communities who are affected with the same fate deserve more. These are real people, real families and real communities. In many of these small communities there are no other jobs. How can these small northern Ontario towns afford to continue to provide public services if no one can pay the taxes? How can these people and families continue to live there? They can't, their EI will run out and they'll have no other means of income.<sup>5</sup>

The Community Development Trust, a 3-year \$1 billion investment by the federal government, was set up to help communities and workers facing adjustment challenges in the forestry and manufacturing sectors. Each province will receive \$10 million and each territory will receive \$3 million, with the balance of the funding allocated on a per capita basis. It is expected that funds from the Trust will be used by provinces and territories to help with worker retraining, to develop community transition plans, and to support economic diversification. It is yet too early to report on which projects are being financed and what outcomes are being achieved with the funding provided through the Trust. Some witnesses that appeared before the Committee expressed concerns that the Community Development Trust is too small, and its objectives too broad, to significantly help Canada's beleaguered forest communities. Others expressed the hope that provinces and territories would use the funds provided through the Trust to help workers affected by the downturn in the forest products industry.

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4 Jim Scarrow, City of Prince Albert, *Committee Evidence*, March 11, 2008.

5 See for example, the testimony of Joe Hanlon, United Steelworkers, *Committee Evidence*, March 13, 2008.

## **Contributing Factors to the Crisis Facing Canada's Forest Products Industry**

A number of factors, both domestic and international, have led to reduced production, a decline in profitability, mill closures and job losses in Canada's forest products industry. These include the downturn in the U.S. housing market, intensification of global competition, rapid appreciation of the Canadian currency, productivity deficits, etc.

### **U.S. Housing Market**

The U.S. residential construction sector has long been the key market for Canadian softwood producers. Recently, demand for wood-fabricated materials, such as lumber and wood panels, has dropped considerably as a result of the slowdown in the U.S. housing sector. U.S. housing starts have declined by 27% year-over-year in 2007. Canada's wood exports to the U.S., in turn, have declined by about 25%. Competition from abroad, most notably from Chinese producers of plywood, has exacerbated this decline. According to Natural Resources Canada, prices for framing lumber in February 2008 reached their lowest levels since 1991.

### **Collapsing Demand for Newsprint and Intensification of Global Competition**

Canada has traditionally been an important producer of newsprint. North American demand for newsprint, however, is collapsing, which is putting enormous pressure on Canadian producers. Indeed, demand has fallen by over 30% since 2001 and is expected to continue to fall as consumers in industrialized countries increasingly reject newspapers in favour of the internet and other electronic media. For example, Natural Resources Canada reports that February 2008 marked the 57<sup>th</sup> straight month of year-over-year declines of U.S. newsprint consumption.

Moreover, Canadian newsprint producers find themselves unable to compete against low-cost producers in Asia and South America, and as a result are being crowded out of this once lucrative market. Many witnesses who appeared before the Committee firmly believed that the future for Canadian newsprint production is decidedly bleak.

### **Appreciation of the Canadian Currency**

The Canadian dollar has risen from a low of 62 U.S. cents in January 2002, all the way to parity (and beyond) in less than 6 years. The rapid appreciation of the Canadian currency vis-à-vis that of our main trading partner has significantly harmed the profitability of Canadian forest companies since most forest products are priced in U.S. dollars, whereas primary inputs (fibre, labour, energy) are priced in Canadian dollars. Most forest products companies found themselves simply unable to adjust quickly enough to the rapid run-up in the Canada/US dollar exchange rate.

PricewaterhouseCoopers estimates that each one-cent increase in the average annual value of the Canadian dollar costs the Canadian forest products industry about \$500 million.<sup>6</sup> The strength of the Canadian dollar vis-à-vis the American dollar has, according to the industry, negatively affected the competitiveness of Canadian firms in the short-term, with the result that most of the rationalization in the newsprint industry took place on the Canadian side of the border.

### **Underinvestment**

Several witnesses told the Committee that part of the reason why Canada's forest products industry is currently in trouble is because, for too long, it underinvested in research and development, new technologies and new mills and equipment. There are many plausible explanations for this; for example, it has been suggested that throughout the previous decade, many Canadian forest products companies relied on a low Canadian dollar as their main competitive advantage and failed to make the necessary investments to improve their productivity and shore up their international competitiveness.

While some Canadian forest products companies have upgraded their plants and equipment, it remains a fact that the capital stock of Canada's forest industry as a whole is older and less productive on average than that of its global competitors.<sup>7</sup> This has made Canadian forest products companies more susceptible to market downturns and less capable of competing globally. The current strength of the Canadian currency versus the American dollar presents an opportunity for some Canadian forest products companies to purchase cutting-edge machinery and equipment from U.S. manufacturers and thus improve their competitiveness.

### **Mountain Pine Beetle Epidemic**

British Columbia is in the throes of a mountain pine beetle outbreak beyond any bark beetle epidemic recorded in North American history. The mountain pine beetle has already devastated large swaths of British Columbia's lodgepole pine forests. Natural Resources Canada reports that at the current rate of spread, approximately 50% of B.C.'s mature pine will be dead by the end of this year, and 80% (representing roughly 1 billion cubic metres) will be dead by 2013. The consequences of this epidemic will have long-lasting consequences for British Columbia's forest industry and affected communities.

Having already crossed into Alberta, the epidemic threatens to expand further into Canada's boreal forest, threatening ecosystems and the economic well-being of many other forest-dependent communities.

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6 Forest Products Association of Canada, brief submitted to the Committee.

7 Forest Products Association of Canada, *Industry at a Crossroads: Choosing the Path to Renewal*, Report of the Forest Products Industry Competitiveness Task Force, May 2007.

The Government of Canada in Budget 2006 allocated upwards of \$200 million to combat the mountain pine beetle (MPB) infestation and to help the industry and affected communities manage the economic impacts of the infestation. Half of that amount went to NRCan to fund various MPB initiatives (see Table below). The remaining \$100 million was allocated to Western Economic Diversification (\$56M) and Transport Canada (\$44M), to provide needed infrastructure improvements and to support enhanced economic diversification.

<b>Federal Mountain Pine Beetle Program - NRCan Expenditure Summary</b>				
(In thousands of dollars)				
<b>Program</b>	<b>06/07</b>	<b>07/08</b>	<b>08/09 (preliminary)</b>	<b>Totals</b>
Controlling the spread	20,375	27,965	22,000	70,340
Recovering economic value	3,130	3,585	3,871	10,586
Protecting Forest resources and communities	1,650	4,416	6,220	12,286
NRCan Corporate		1,749	1,683	3,432
Communications		832	200	1,032
CFS (salaries)		1,224	1,100	2,324
<b>Totals</b>	<b>25,155</b>	<b>39,771</b>	<b>35,074</b>	<b>100,000</b>

Source: Natural Resources Canada (April 16, 2008).

## **Fibre Costs**

Several witnesses identified high wood fibre<sup>8</sup> costs as a competitive disadvantage for some Canadian forest products companies. Fibre costs vary regionally across Canada. In the B.C. Interior, wood costs are notably very competitive largely because of the significant but temporary increase in harvest volumes resulting from the mountain pine beetle infestation. By contrast, fibre costs across much of Eastern Canada are considered high by international standards, particularly when compared to the cost of fibre in emerging economies such as Brazil, where good quality trees grow very fast. Some witnesses suggested that the cost of fibre in Quebec is amongst the highest in the world.

## **Softwood Lumber Agreement**

There is no clear consensus on the impacts of the softwood lumber agreement between Canada and the U.S. (SLA) on Canada's wood producers and the communities that depend on them for their survival. Some witnesses, such as Bob Matters, Chair of the Steelworkers' Wood Council, told the Committee that the SLA has harmed Canada's industry and should be revisited if not abandoned altogether.<sup>9</sup> Others, such as John Allan of the Council of Forest Industries, said that the SLA was by far preferable to ongoing litigation and dispute with the United States.<sup>10</sup>

## **High Transportation and Energy Costs**

The cost of transporting wood fibre and finished products, and the cost of the energy required for processing, represent a significant part of total production costs for the Canadian forest products industry. The Forest Products Association of Canada (FPAC) estimates that "transportation costs are the sector's second largest cost component."<sup>11</sup> Soaring fuel prices in recent years have obviously also helped to drive up the cost of transporting forest products.

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8 NRCan defines wood fibre as the "material in which the wood is reduced to predominantly individual fibres by mechanical or chemical means, or a combination of the two. Virgin fibre is derived from trees not previously processed into paper; recycled fibre has been reclaimed from a previous product such as old newsprint and reprocessed and incorporated into a new product." In more general terms, the industry refers to the cost of wood fibre as the price it has to pay for its timber supply prior to its transformation into diverse forest products.

9 Bob Matters, United Steelworkers, *Committee Evidence*, March 13, 2008.

10 John Allan, Council of Forest Industries, *Committee Evidence*, March 4, 2008.

11 Forest Products Association of Canada, presentation to the Standing Committee on Natural Resources, April 1, 2008.

Energy costs are also an important cost driver. The pulp and paper sector is the largest industrial energy user in Canada. While the sector generates some 60% of its own energy needs from renewable sources, it has been hit hard by higher prices for fossil fuels and climbing industrial electricity rates. Despite these circumstances, some regions of Canada are still benefiting from competitive energy rates that, in the opinion of FPAC, give Canada a genuine global advantage in the production of softwood fibre.<sup>12</sup>

## Summary

While many of the factors outlined above were and remain largely outside the control of the industry, at least one witness felt that the severity of the crisis currently facing Canada's forest products industry can be explained by structural factors.<sup>13</sup> Amongst the factors cited, by far the most important is the Canadian industry's focus on the production of low-value products such as newsprint and lumber for export to the U.S. Another witness suggested that Canada's forest products industry is struggling to be competitive because it has for too long been on "automatic pilot."<sup>14</sup>

As will be explored later in this report, it is critical that the industry build on its strengths and expand into new value-added products and new markets, including the domestic market, if it is to survive and thrive.

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12 Energy costs can represent up to 20% of newsprint production costs in Eastern Canada, according to the Forest Products Association of Canada (2007), *op. cit.*

13 Hugo Asselin, Université du Québec en Abitibi-Témiscamingue, *Committee Evidence*, March 11, 2008.

14 Luc Bouthillier, Laval University, *Committee Evidence*, March 13, 2008.

## CHAPTER 3 — WHAT FUTURE FOR CANADA'S FOREST PRODUCTS INDUSTRY?

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There can be no doubt that Canada's forest products industry today is in the midst of a significant adjustment period. But the challenges facing the industry are not insurmountable. This is an industry with a long and successful history which continues to have tremendous potential for sustainable growth.

Witnesses who appeared before the Committee were emphatic: Canada's forest products industry is **not** a sunset industry. It **will** bounce back from this severe downturn.

This is, after all, a cyclical industry. Over the medium to long term, a host of new opportunities will present themselves. It is up to the industry, in concert with governments, forest communities and other stakeholders, to position itself to be able to seize these opportunities.

Opportunities will exist in both new and traditional markets. While the U.S. economy is currently in the throes of an economic downturn, most analysts agree that it will bounce back, and with it demand for new residential construction. Though this most important market for Canada's wood products is currently weak, it is unlikely that this weakness will persist for many more years.

On the pulp and paper side, the Committee received evidence that global demand for paper, led by emerging Asian economies, each year is growing by an amount equal to all of Canada's production. Canada can and indeed must take the necessary steps to further tap into that global market.

Besides the traditional wood and pulp and paper markets, there now exist entirely new markets for wood fibre. Global concerns about the environment, and concerns about climate change in particular, are expected to further stimulate demand for wood fibre (and other renewable resources) that can be used as a low-carbon energy source and fossil fuel substitute.

While global demand for wood fibre is growing, it is also the case that throughout the world, particularly in industrializing countries, land to grow such fibre is increasingly being diverted to other uses, namely food and biofuel crops.

The price of food and biofuel feedstocks, such as corn and soybeans, has risen considerably in recent years in response to surging food and biofuel demand in emerging economies, the U.S. and the EU. The Committee received evidence from Don Roberts of

CIBC World Markets that Asian and Latin America countries may not be able to continue to increase their production of wood and paper products as forest plantations increasingly compete with the agricultural and biofuel sectors for scarce land and water.<sup>15</sup>

According to Mr. Roberts, the amount of land available globally to grow wood fibre will in fact shrink as land in Asia and Latin America is used instead to grow crops for food and fuel. At the same time, Russia, which has huge forest resources and supplies roughly 40% of the world's harvest of logs, is expected to impose a substantial tax on log exports. Mr. Roberts testified that this move could affect the global supply of forest products as Russia does not at present have the capacity to process those logs domestically.<sup>16</sup>

These developments are advantageous to Canada. Canada has the land, the water and the energy to be a global leader in the forest products business. The emerging opportunities that stem from what Mr. Roberts calls the "convergence of the markets for fuel, food and fibre" will raise the value of Canada's forests and help Canadian producers become more competitive globally. After well over a decade of eroding competitiveness, the pendulum may in fact be shifting back from the southern hemisphere to the northern hemisphere.

The fact that markets are increasingly looking for sustainable forest products is also to Canada's advantage. Indeed, both the U.S. and the EU have taken some steps to reduce the import of illegally produced forest products into their markets. Illegal logging is widespread, notably in tropical countries such as Indonesia, and is having a major impact on the sustainability of these wood products. As markets come to demand sustainably harvested forest products, Canada will be able to take advantage of its environmental leadership position and capitalize on these opportunities.

Canada, with its vast forests, technological expertise and recognized leadership in the area of sustainable forest management, is well positioned to capitalize on any increased demand for wood fibre. Moreover, technological innovation in the area of composite materials and bio-products offers many new exciting potential market opportunities. Canada can and must build on its strengths. As one witness told the Committee, Canada's primary advantage is that "we have the best fibre in the world. No one can take that away from us."<sup>17</sup>

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15 Don Roberts, CIBC World Markets, *Committee Evidence*, March 4, 2008.

16 Ibid.

17 Emilio Rigato, as an individual, *Committee Evidence*, February 28, 2008.

It is up to the industry to restructure itself in order to be able to seize these emerging opportunities. As the Forest Products Association of Canada noted in its submission to the Committee, Canada is uniquely positioned to capitalize on these opportunities:

There are few places on Earth with a land base similar to Canada's that can meet the world's growing needs for wood fibre. There are even fewer, possibly none, that also have the knowledge and network of institutions required to make sure that this fibre is produced and processed in a socially and environmentally responsible fashion. If Canada fails to realize the opportunity that its forest resource base offers in the 21<sup>st</sup> century, it will be because of either a lack of will or imagination. It will not be due to a lack of opportunity.<sup>18</sup>

Governments, including the Government of Canada, have an important enabling role to play by creating and implementing a supportive policy framework. The rest of this report will therefore offer some recommendations for how the federal government, along with the provinces, the territories and the industry, can help the forest sector capitalize on these opportunities and in the process provide long-term benefits to forest workers and forest communities, including First Nations communities.

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18 Forest Products Association of Canada, brief submitted to the Committee.

# CHAPTER 4 — STRENGTHENING CANADA'S FOREST PRODUCTS INDUSTRY

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## Looking for Solutions

Canada's forest products industry is going through one of the worst crisis in its history. Some even describe the situation as a "perfect storm", with many elements coming together to produce devastating effects on several levels. A strong Canadian dollar, declining demand and reduced prices are just some of the factors that are shaking up the industry from one end of the country to the other. The extensive evidence heard by the Standing Committee on Natural Resources described the causes that have led the various sectors of the Canadian forest products industry to close a number of mills and processing plants either temporarily or permanently. The witnesses also made a variety of suggestions — economic, social and even environmental — designed to help resolve the crisis, or at least lay a solid foundation for the industry's revitalization. Everyone expressed the hope that the forest industry would once again, and as rapidly as possible, become prosperous, efficient and sustainable, for the benefit of all Canadians.

In this chapter, we describe possible solutions for resolving the current crisis as proposed by the witnesses who appeared before the Committee. Recommendations are also put forward for the federal government, and where applicable for its partners. Some aspects of the forest industry challenges are more a provincial than a federal matter; in such cases, the Committee has limited itself to identify those aspects and describe their significance.

### A Summit and a Strategy

The Committee heard from several witnesses that the Government of Canada should call a national summit of all forest industry stakeholders in Canada to address the current crisis and begin to put together a strategy for recovery and renewal. As one witness put it, "We don't accept that it's a sunset industry. We think if we put all the minds together we can find a way of rejuvenating this industry and moving forward."<sup>19</sup>

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19 David Coles, Communications, Energy and Paperworkers Union of Canada, *Committee Evidence*, February 28, 2008.

A number of reasons were put forward in support of holding a summit. First, the Committee heard that the forest products industry does not always speak with one voice. A summit, it was argued, would help “shake things up a little, to get everyone around the table and bury the past, and turn towards the future” all the while recognizing that each region of Canada is different and faces sometimes unique challenges and opportunities.<sup>20</sup>

The Committee was told that the different levels of government need to do a better job of looking at the big picture and must make a concerted effort to work together more proactively.<sup>21</sup> As the City of Kenora explained in their brief to the Committee,

We need to see the federal and provincial governments working together. This is more important than ever [...] The private sector and First Nations must also be engaged. We must come together unlike any time in our history.<sup>22</sup>

The Government of Canada has a clear leadership role to play in making sure that this happens.

Overall there was considerable optimism amongst many witnesses that a national forestry summit could be the first step toward the development of a national, visionary, and diversified forestry strategy:

One of our problems is that we're caught in this federal-provincial divide. Effectively, we need strong leadership and someone who is going to say, “this is the vision for our forest sector”, because it's not there right now. I think the federal government can provide that leadership for the short, mid and long-term. We need that vision.<sup>23</sup>

**The Committee has heard evidence from a number of stakeholders and believes it would be in the public interest for the Prime Minister to convene a National Summit, with all stakeholders, on the future of the Canadian forest industry with a view to developing a national strategy to support the renewal of the industry while respecting provincial and territorial jurisdictions.**

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20 Keith Newman, Communications, Energy and Paperworkers Union of Canada, *Committee Evidence*, February 28, 2008.

21 Jean-Pierre Dansereau, Fédération des producteurs de bois du Québec, *Committee Evidence*, February 28, 2008.

22 City of Kenora, brief submitted to the Committee.

23 Jack Saddler, University of British Columbia, *Committee Evidence*, March 13, 2008.

## A Vision for the Industry

The Committee heard compelling evidence that the production of primary commodities will continue to be of importance to Canada's forest products industry in the near to medium term. Those companies that continue to produce commodities must find ways of optimizing their production chains in order to be more flexible and better able to respond more quickly and more efficiently to market fluctuations and changes in market demand.<sup>24</sup>

Canada's industry must also look beyond commodities if it is to thrive in an increasingly competitive marketplace. Canada must intensify its efforts to develop a forest products industry that is also centered on high value-added products and that looks to new markets and finds cost-competitive ways of supplying them. As Jim Scarrow, Mayor of the City of Prince Albert told the Committee, "our industry must move away from high volume and toward high value production."<sup>25</sup>

Jack Saddler, Dean of Forestry at the University of British Columbia was even more emphatic:

[I]f we're trying to rely on market pulp or two by fours, we're not going to make it. We're basically going to have to be very innovative in terms of the products we get out of our forests.<sup>26</sup>

It was suggested to the Committee that while the production of primary commodities such as lumber and pulp will continue to be of importance, the industry must at the same time move towards selling higher margin housing and business solutions.

Another way for the industry to be more innovative is for it to use the forest resource more efficiently. The waste from one process must become the raw material for the next. Forest materials that have long been considered waste materials can be transformed into fuel for bioenergy, material for pellets, or new types of construction materials.<sup>27</sup> To some extent this is already being done, but more progress is needed, and much more rapidly.

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24 Hugo Asselin, brief submitted to the Committee.

25 Jim Scarrow, City of Prince Albert, *Committee Evidence*, March 11, 2008.

26 Jack Saddler, University of British Columbia, *Committee Evidence*, March 13, 2008.

27 David Cohen, University of British Columbia, *Committee Evidence*, March 13, 2008.

Others have been advocating in favour of a more fundamental transformation. The future of the industry, according to them, is centered on bio-refining (e.g. turning forest biomass into liquid fuels and other chemicals), green chemistry and the production of other innovative and sustainable products and materials the world will soon need.<sup>28</sup>

The idea is for Canada to become a world leader in these areas and be in a position to ultimately export equipment, technology and expertise throughout the world. This can be done in conjunction with partners in other industries. For example, a forest products company could partner with an energy or a chemicals company to find ways to develop and market products from a bio-refinery.<sup>29</sup>

Examples from Europe are instructive. In the forest products industry, Finland is a great example of a country that has embraced change and, through innovation, has become a leading exporter of not only forest products but also forest equipment and technology. The Committee heard evidence that Canadian companies buy logging equipment, paper machine equipment and technology from Finland.<sup>30</sup> Looking at the electricity production industry, we see that Denmark has not only embraced renewable energy but in fact has become an important producer of windmills and wind power technology. As Jack Saddler of the University of British Columbia told the Committee:

[W]hat we should be doing in Canada is aspiring to not only use our resources in a very innovative and effective way, but we should be basically the developers of the technology that we can sell to the rest of the world.<sup>31</sup>

The Government of Canada, working with the provinces, territories and industry, can play an important and unique role by developing a new vision for the forest products industry and helping it make the transition from tradition to innovation.<sup>32</sup>

## **Innovation, Research and Development**

So what's needed? The future health of Canada's forest sector depends on innovation. We need to find new uses for wood fibre, products characterized by higher value rather than higher volume. Investing in innovation, emerging technologies and new products have the potential to lead a transformation in the forest sector in Canada.<sup>33</sup>

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28 See, for example, the testimony of Emilio Rigato, *Committee Evidence*, February 28, 2008.

29 Ian de la Roche, FPIInnovations, *Committee Evidence*, February 28, 2008.

30 James D. Irving, J.D. Irving Limited, *Committee Evidence*, March 13, 2008.

31 Jack Saddler, University of British Columbia, *Committee Evidence*, March 13, 2008.

32 Corporation Agro Forestière Transcontinentale Inc., brief to the Committee, March 2008.

33 Cassie Doyle, Deputy Minister, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

If there is one element of the forestry issue about which people are unanimous, it is the need for research and development (R&D), as well as innovation in the broad sense. Contrary to what might be supposed, and despite the widespread impression that the Canadian forest products industry concentrates essentially on a few staple commodities, there is already a great deal of innovation going on in both the lumber and paper sectors. Many observers see R&D as the motor of innovation, which in turn stimulates productivity: the most competitive enterprises in any sector are usually the ones that are the most innovative and the most productive. However, some witnesses argued that the main R&D actors, particularly the industry itself, have not devoted sufficient resources to R&D.

According to Natural Resources Canada, Canada is “about in the middle of the pack”, in terms of both public and private forestry R&D spending, when compared with other countries that have significant forest industries.<sup>34</sup> In 2005, the public and private sectors invested a total of CAN\$685 million in forestry R&D: CAN\$174 million on “pre-manufacturing forestry” and CAN\$511 million on forest products. Of the total, the federal and provincial governments allocated CAN\$156 million<sup>35</sup> (mostly on forestry), and the industry spent the remaining CAN\$529 million (mostly on development of wood and paper products). According to NRCan, Canadian investment in R&D stands up quite well against that of Sweden (CAN\$299 million in 2005), Finland (CAN\$550 million in 2007) and the United States (\$675 million in 2004), but Canada ranks below these other three countries if one takes into account its relative share of global forest products sales.<sup>36</sup> Natural Resources Canada told us that there is no large-scale comparative classification for R&D investments in the forest sector. However, based on a scientific multi-criteria ranking, Canada has for the past 15 years been the fifth best country in the world for its performance in forestry research. Those research areas in which Canada excels are forest fires, entomology, silviculture and regeneration, and forest and landscape management.<sup>37</sup>

Forest research is carried on by most of the stakeholders in the forest sector: governments, private institutes, companies and universities, very often in partnership. The federal government and the industry are counting heavily on enhanced partnerships to revitalize the forest sector. R&D and innovation are at the heart of the Forest Industry Long-Term Competitiveness Strategy launched by the federal government in 2007 with \$127.5 million in funding over two years. Within the strategy one of the main initiatives has been to consolidate a number of separate components of the national forest innovation

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34 Jim Farrell, Assistant Deputy Minister, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

35 According to NRCan, the federal government spent approximately \$120 million on forestry R&D and the Department is aware of at least \$36 million spent by provincial governments. Because they do not report forestry R&D numbers to Statistics Canada (from which NRCan derives its information on provincial R&D spending), the remaining \$36 million provincial figure does not include spending by the governments of Quebec, Saskatchewan and the Maritime provinces.

36 Based on additional information provided by Cassie Doyle, Deputy Minister, Natural Resources Canada, March 12, 2008, further to her appearance before the Committee, February 12, 2008.

37 Ibid.

system and align them to focus on competitiveness. The result has been the creation of FPInnovations, now considered the world's largest public-private partnership in research and development.

FPInnovations<sup>38</sup> is a new Canadian research and development institution. It was created on April 1, 2007, by integrating the four existing private forest research institutes: Forestry Engineering Research Institute of Canada (FERIC), Forintek, Paprican and NRCan's Canadian Wood Fibre Centre. With almost 675 employees across Canada and a budget of around \$100 million, FPInnovations has united the individual strengths of each of the four internationally recognized forest research and development institutes into a single stronger force. Its goal is leadership in forest sector R&D and innovation in order to strengthen the Canadian forest sector's global competitiveness through research, knowledge transfer and implementation.

FERIC was set up in 1975 to improve Canadian forest operations within a framework of sustainable development. With offices in Montreal, Quebec City and Vancouver, it is funded by a partnership of leading forestry companies, the federal government and the provinces, plus Yukon and the Northwest Territories. It develops and helps to implement innovative and safe forest operational solutions covering the vast range of engineering, human, operational and environmental aspects of forestry and fire prevention. Its areas of R&D concentration include harvesting, transportation and roads, silvicultural practices, wildland fire operations, and precision forestry practices.

Forintek was formed in 1975 when the federal government's two forest products laboratories were privatized. Now as a division of FPInnovations, Forintek is still the national wood products research institute. Its role is to support the forest products industry in optimizing manufacturing processes, extracting higher value from the available resource and meeting customer expectations for performance, durability and affordability. Forintek's National Research Program (NRP) is built around the following key areas: resource assessment; lumber manufacturing; composites products manufacturing; value-added products; building systems; codes and standards; market and economics.

Paprican (the Pulp and Paper Research Institute of Canada) is a non-profit body that has been in operation for over 80 years. Today a part of FPInnovations, Paprican has laboratories in Quebec and British Columbia, where it carries out research and technology transfers based on its members' strategic and short-term needs. Its research programs are dictated by the industry's priority technical issues, such as product quality and value, cost competitiveness, the environment and sustainable development. They centre mainly on: fibre supply and quality; chemical pulping; mechanical pulping; papermaking; product performance; environment and sustainability.

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38 The information on FPInnovations is drawn mainly from its Internet site: [http://www.fpinnovations.ca/home\\_e.htm](http://www.fpinnovations.ca/home_e.htm).

The Canadian Wood Fibre Centre (CWFC) joined FPIInnovations in 2007. It reports to the latter's Board of Directors but continues to function as a component of NRCan's Canadian Forest Service (CFS). The CWFC's mandate is to create innovative knowledge that will expand the economic opportunities for the forest sector to benefit from Canadian wood fibre by procuring it a significant competitive advantage on the world market. Under its 2006-2009 Development Plan, the CWFC aims to become a key contributor to and participant in FPIInnovations programs, concentrating on: the characterization of Canadian wood fibre; the development of forest-inventory technology, forest-management planning tools, and reforestation techniques; and, the integration of Canadian wood fibre into a profitable forest-products value chain.

NRCan regards FPIInnovations as the flagship of its competitiveness strategy as well as a way of bringing together federal and provincial expertise on forest resources. The Board of Directors is therefore made up of representatives of most of the provinces and of a great many of the primary and secondary industries, as well as of the federal government. Discussions at this level are aimed at finding the best possible way of stimulating regional value and regional programs, in order to establish national and regional priorities. The Canadian Council of Forest Ministers (CCFM), on which all the provinces and territories are represented, is another key forum for dealing with broader political issues such as the Canadian Wildland Fire Strategy and the National Forest Pest Strategy.<sup>39</sup>

For a number of years now, governments and the industry have been seeking to revitalize the Canadian forest sector, but so far their success has been limited. Today they are attempting to focus more on the underlying issues on which the Canadian forest products industry's competitiveness depends. FPIInnovations has made it possible to address sector-wide issues along the entire value chain, from genetics to forestry, from production to manufacturing, all the way to market intelligence, market development, and product performance in the marketplace.<sup>40</sup> The FPIInnovations vision is to help facilitate the development of new products, based on renewable fibre sources with multiple uses and advantages, in areas that include greenhouse gas emissions, energy and chemistry, to name just a few.

While a great deal is already being done, more is necessary to support innovation according to FPIInnovations:

We're suggesting the creation of perhaps a national innovation trust for the Canadian forest sector that focuses on transforming the sector with transformative technologies and applications using the same private-public partnership approach. The initial investment could perhaps come from the Government of Canada. We're convinced that

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39 Jim Farrell, Assistant Deputy Minister, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

40 Ian de la Roche, FPIInnovations, *Committee Evidence*, February 28, 2008.

with that kind of leadership we can absolutely guarantee that the industry and the provinces will be quickly willing to come in line. In fact, they've [already] given that indication.<sup>41</sup>

A fund of this kind would support technology and innovation in areas vital to the industry, promote the distribution of information and technology, strengthen the coordination of academic research, and support national pilot projects and the holding of forums on technology and innovation that would bring together the entire industry. Means must be found to highlight the importance of R&D and its applications, as well as encourage the industry and other sectors to invest more in this area, as shown by the work of the Research Group on the Commercial Boreal Forest.

**The Committee therefore recommends that the federal government, in collaboration with provincial and territorial governments and the industry, establish a national forest industry innovation fund, and that this fund be provided with sufficient resources to ensure that the industry can be central in the development of the new bioeconomy.**

As we move toward the bioeconomy, in which the forest industry can play a pivotal role, it is crucial that the overall industry diversify as rapidly as possible and that the value of forest products be enhanced. The Government of Canada is already committed to promoting and using biomass for energy. The ecoENERGY program has been expanded to include support for electricity produced from biomass, so the program will now be accessible to the forest industry. In addition, the most recent budget provided for the creation by Sustainable Development Technology Canada of a fund worth half a billion dollars to advance next-generation cellulosic ethanol, which will be available for both agricultural-produced cellulose and forest-based cellulose<sup>42</sup>, although the Committee recognizes that there are different issues with the two types of cellulose.

## Bioenergy

The pulp and paper sector at present self-generates 60% of its energy needs from biomass. The industry believes that, with the right incentives, it could become a net source of renewable energy within the next decade or so. The efficient combustion of biomass for energy production results in a reduction of greenhouse gas emissions since it typically displaces fossil fuels.

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41 Ibid.

42 Cassie Doyle, Deputy Minister, Natural Resources Canada, *Committee Evidence*, February 12, 2008. Managed by Sustainable Development Technology Canada (SDTC), the NextGen Biofuels Fund™ will support up to 40% of eligible project costs for the establishment of first-of-kind large demonstration-scale facilities for the production of next-generation renewable fuels. The contribution will be repayable based on free cash flow over a period of 10 years after project completion (according to SDTC website: [http://www.sdtec.ca/en/news/media\\_releases/media\\_12092007.htm](http://www.sdtec.ca/en/news/media_releases/media_12092007.htm)).

Electricity derived from the combustion or gasification of forest biomass is currently eligible for federal renewable energy production incentives under the terms of the ecoENERGY for Renewable Power program.

Extending the scope of the program to also cover thermal energy and putting more money into it would further support the deployment of renewable energy systems. This would help the forest products industry better manage its energy costs and would contribute to reducing greenhouse gas emissions in Canada.

**The Committee therefore recommends that the Government of Canada consider putting additional funds into the ecoENERGY for Renewable Power program and consider extending its scope to cover the production of thermal energy from renewable sources such as biomass.**

### **Biomass and Bioproducts**

A number of witnesses heard by the Committee stressed the importance of rapidly developing the biomass industry. This industry has a number of potential advantages for the environment, as well as for the wood products and pulp and paper sectors. In the witnesses' view, biomass is a clean and renewable energy source that the federal government and its partners must support even more to accelerate its development.

NRCan officials pointed out that, as far as the forest industry is concerned, some 20-25% of the funding identified in the Long-Term Competitiveness Strategy's innovation envelope is already earmarked for bioproducts and biorefining. The Department wants to help implement the concept of being able to produce energy chemicals like ethanol (and other products) out of wood inputs, rather than just using them to make market pulp.<sup>43</sup>

Some academic researchers are also interested in biorefining and feel that it is a niche worth developing. According to Professor Robert Pelton of McMaster University,<sup>44</sup> Canada has fallen behind the Americans and, even more so, the Scandinavians in this area, in which the federal government could invest more. Others feel that we must be careful about widespread use of the forest biomass when it comes to harvesting waste in logging areas, since there is a risk that the soil will be impoverished if not enough organic material is left behind to decompose.<sup>45</sup>

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43 Jim Farrell, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

44 Robert Pelton, McMaster University, *Committee Evidence*, March 6, 2008.

45 Brief from the Canadian Parks and Wilderness Society submitted to the Committee on March 6, 2008.

**The Committee therefore recommends that the Government of Canada, working with the provinces and territories, assess the impacts of a more intensive use of biomass on forest ecosystems and on the environment, and where appropriate provide increased funding for research and development on bioenergy and bioproducts. Conditions for increased funding should be based upon energy conversion factors, greenhouse gas emissions, and impacts on regional forest economies.**

### **Value-added Products**

As with R&D, most witnesses agreed that finding ways to add value to forest products is critical:

For the last century, the forest industry has been oriented mainly to the export of commodity products such as market pulp, newsprint, and lumber. Competition for these products has become intense, and many countries can now produce them more cheaply than can happen in Canada. To survive in the new commercial environment, the industry must develop better synergies between industry and subcontractors in order to make more efficient use of the entire resource. The waste from one part must be the raw materials of the next. It should redirect itself toward high-value-added products for sawmills, the pulp and paper industry, furniture, doors, windows, pre-fabricated homes, wood-based insulation, sanitary products, etc.<sup>46</sup>

**The Committee concurs and therefore recommends that the Government of Canada, in partnership with the provinces and territories, actively pursue policies that encourage value-added manufacturing.**

The federal Value to Wood program, which was established in 2002 and extended for a further two years in March 2007, constitutes an important component in an innovation strategy for the forest sector. Based on partnerships between governments, regional agencies, FPInnovations and universities, it has both a research dimension and a technology transfer dimension. This enables it to move research related to secondary manufacturing to the shop floor more quickly, and to provide expert advice on site to mill owners and operators about how to improve their efficiency. For example, the Value to Wood program has over 35 industry advisers who visit small firms to offer advice on improving productivity.<sup>47</sup>

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46 David Coles, Communications, Energy and Paperworkers Union of Canada, *Committee Evidence*, February 28, 2008.

47 Jim Farrell, Assistant Deputy Minister, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

**Given the importance and scope of the Value to Wood program, your Committee recommends that it be extended beyond the current expiry date of March 2009 in a predictable fashion.**

## **Restructuring**

The Committee heard evidence that Canada's forest products industry is fragmented and, as a result, is struggling to adapt to the requirements of the global marketplace. Until the early part of 2007, no Canadian-based forest products company ranked among the 20 largest in the world. This is astounding given Canada's vast forest resource and geographical proximity to the world's biggest market.

The forest products industry is of the view that Canada's conventional forest products industry must restructure and consolidate in order to modernize and take advantage of economies of scale. Bigger companies are generally better able to manage the risks associated with technological innovation, develop new products, and raise capital. They also can benefit from economies of scale in production and marketing.

Industry leaders who appeared before the Committee were unanimous. The industry is not looking for government subsidies to individual companies or plants. The Committee heard compelling evidence that direct subsidies to individual companies or operations often only delay the inevitable, namely plant closures and job losses, and could in addition be interpreted as a violation of international trade agreements.

That is not to say that the industry would like to see the government take a "hands-off" approach. The Committee was told that *laissez-faire* is in many ways just as naïve a policy approach as interventionism.<sup>48</sup>

Many in the industry were clear: governments at all levels across the country must send the right signals and allow the industry to consolidate and restructure. Inefficient plants must be allowed to close, and companies must be allowed to merge and form strategic alliances if they are to emerge from this crisis and have a chance to be internationally competitive.

Restructuring, the Committee was told, "is terrible and painful, but it's necessary to have sustainable jobs"<sup>49</sup> and is a necessary condition for moving towards "a more productive and more efficient industry."<sup>50</sup>

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48 Avrim Lazar, Forest Products Association of Canada, *Committee Evidence*, 14 February 2008.

49 Ibid.

50 Hughes Simon, AbitibiBowater, *Committee Evidence*, February 14, 2008.

Some community leaders agreed with this approach. Terry Fiset, Reeve of the Township of James, in Ontario, testified that “we believe that governments need to allow this rationalization to occur in order for the sector as a whole to survive.”<sup>51</sup>

According to the Forest Products Association of Canada (FPAC), the Competition Bureau, an independent government agency charged with promoting competitive markets, has over the years dampened the Canadian forest products industry’s ability to restructure and consolidate by preventing certain mergers and acquisitions within the industry.

The Competition Bureau, FPAC argues, should recognize the **global** nature of forest products markets and of competition. A merger between two Canadian forest products companies would not significantly restrict competition or harm Canadian consumers since commodity prices are set on international markets. Canadian operations and firms, the argument goes, should therefore be allowed to merge in order to be globally competitive:

They assume that if we consolidate, prices will go up. Well, we export most of what we make. We take the global price, and whether we're fragmented or consolidated, the global price is whatever Brazil or China pushes it down to. Our customers, both in Canada and all over North America, are more consolidated than we are, so if two companies come together and find efficiencies, do you think our customers give us a break? If we find three cents a tonne efficiency, they'll take three and a half cents out of our hides, because they are more consolidated and have more market power than we do. It's just an empirical fallacy that when you consolidate, prices go up, because the marketplace continually squeezes you down. We disagree with their economics, and empirical studies support the simple fact that consolidation actually leads to synergies and price reductions. Would it lead to more outside ownership? On the contrary, it would not. If you're a company headquartered in Canada and you want to acquire Canadian assets, the Competition Bureau is standing right in your way, because they don't want to see consolidation in Canada; as a result, you have to invest your money in the U.S. or Europe to find new acquisitions, because if you invest in Canada, they say it's too much consolidation. Getting a large Canadian champion has been a fight against the Competition Bureau, which tells you not to become big in Canada; become big by investing outside Canada. I don't think that's what we want; I think we want investment in Canada.<sup>52</sup>

**The Committee therefore recommends that Canada’s Competition Bureau examine its methods for analyzing mergers and acquisitions in the forest products industry and explicitly take into account the international nature of forest products markets.**

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51 Terry Fiset, Township of James, *Committee Evidence*, March 6, 2008.

52 Avrim Lazar, Forest Products Association of Canada, *Committee Evidence*, February 14, 2008.

While there was considerable consensus amongst witnesses that consolidation and restructuring were needed to strengthen Canada's forest products industry, some did caution that moving towards such a model would not solve all of the problems the industry has been experiencing.

These witnesses acknowledged that small firms with few resources have been hard hit by the downturn, but also noted that the largest mills have also been quick to close. Middle-sized companies and facilities, they argued, are more resilient to market fluctuations (e.g. they can more easily switch to producing different products) and more in tune with the needs of the communities in which they operate.<sup>53</sup> As David Cohen of the University of British Columbia noted, "I think those small- and medium-sized enterprises are the ones that really drive successful industry structures. They're the ones that create jobs, they're the ones that pay taxes, they are the ones that innovate the most."<sup>54</sup> Francis Albert of the Corporation Agro-Forestière Transcontinentale Inc. similarly argued that medium-sized enterprises are leaders in the development of value-added forest products.<sup>55</sup>

**The Committee recommends that the federal government, in conjunction with the provinces and territories, consider investments in innovative research and development programs that stimulate cooperation and facilitate the formation of industrial forest clusters as in Finland.**

### **Attracting Investment**

Canada's forest products industry urgently needs to modernize. The only way to modernize is by investing in new equipment and new technologies. According to FPAC, "the core challenge facing Canada's forest products industry is the requirement to attract the investment necessary to renew its capital stock."<sup>56</sup>

The investment needs are significant. After all, the forest products sector is capital-intensive. A new paper mill can cost well over one billion dollars. Making these kinds of investments in the present economic climate is a challenge for most Canadian forest products companies.

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53 Francis Albert, Corporation Agro Forestière Transcontinentale Inc., *Committee Evidence*, March 11, 2008; Hugo Asselin, Université du Québec en Abitibi-Témiscamingue, *Committee Evidence*, March 11, 2008.

54 David Cohen, University of British Columbia, *Committee Evidence*, March 13, 2008.

55 Francis Albert, Corporation Agro Forestière Transcontinentale Inc., *Committee Evidence*, March 11, 2008.

56 Forest Products Association of Canada, *Industry at a Crossroads: Choosing the Path to Renewal*, Report of the Forest Products Industry Competitiveness Task Force, May 2007.

Today Canada is lagging behind many other countries when it comes to attracting investment in its forest products industry. For example, the Committee received evidence that Finland's forest products industry is attracting approximately seven times as much investment as Quebec's forest products industry (Quebec and Finland's economies are roughly the same size).<sup>57</sup> There are some forest products companies in Canada that simply do not invest enough to even renew their capital stock.

In some instances, certain forest companies' capital stock has been shrinking for over a decade as capital has not been renewed quickly enough to compensate for depreciation. The result is that mills and equipment in Canada are in some cases outdated and less efficient, which hampers productivity and competitiveness. The Committee was told that in Quebec mills are on average 30 years old, compared to seven years in Finland, where the industry invested some \$2 billion in 2007 alone.<sup>58</sup>

This is an unsustainable situation. Steps must be taken to encourage investment in Canada's forest industry. Literally billions more in capital investments are needed to renew the Canadian forest products industry's capital stock.

The industry is calling on governments to introduce tax reforms that will encourage capital investment. Some steps have already been taken. Capital taxes are in the process of being eliminated in most Canadian jurisdictions. Corporate income taxes have been cut significantly at the federal level and in many provinces. But more needs to be done. Further incentives are needed to stimulate the renewal of capital. James D. Irving called on governments to "be bold about it. We fiddle around the edges...We're not aggressive enough, certainly not to compete in the global market from this point of view."<sup>59</sup>

In a bid to stimulate capital investments in ailing industries, Budget 2007 announced a temporary two-year 50% straight-line accelerated capital cost allowance (CCA) rate for investments in manufacturing or processing machinery and equipment undertaken before 2009.<sup>60</sup> Budget 2008 extended that accelerated CCA treatment for three more years, but at a gradually declining rate. It is estimated that this extension will reduce federal revenues by about \$1 billion in total over the period from 2009-2013.

Testimony from forest products industry officials suggested that the accelerated CCA extension introduced in Budget 2008, while a step in the right direction, does not go far enough to improve the investment climate in these difficult times. It was argued that

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57 Luc Bouthillier, Laval University, *Committee Evidence*, March 13, 2008.

58 Ibid.

59 James D. Irving, J.D. Irving Limited, *Committee Evidence*, March 13, 2008.

60 The capital cost allowance system determines how much of the cost of a capital asset a business may deduct each year for income tax purposes.

forest products companies should be allowed to write off new investments in eligible machinery and equipment at an accelerated CCA rate of 50% per year, and this for the next five years.

Similarly, industry officials argued that Canada's scientific research and experimental development (SR&ED) tax incentive program, which offers a 20% investment tax credit on eligible expenditures, should be changed in order to make the tax credit refundable.

Under the current structure of the SR&ED program, companies that have no taxable income derive no direct tax benefit from undertaking investments in scientific research and experimental development. As a result, forest products companies have less of an incentive to invest in SR&ED during a market downturn, which results in less innovation and development. This is in some ways a missed opportunity, as "it's really innovation and development that will help this industry recover."<sup>61</sup>

**The Committee therefore recommends that the Government of Canada examine ways to improve the scientific research and experimental development (SR&ED) tax incentive program, such as by offering refundable tax credits, to ensure that it plays a critical role in supporting the recovery of the forest products industry.**

**Similarly, the Committee recommends that the Government of Canada consider fully extending for the next five years the accelerated capital cost allowance (CCA) treatment for investments in manufacturing or processing machinery.**

Extending tax deductions and tax credits in such ways may be costly. But it was suggested to the Committee that this may well be the wrong way of looking at the problem.<sup>62</sup> The Canadian economy, and ultimately government revenues, could end up taking a bigger hit if new investments in Canada's forest products industry are not made.

### **Expanding into International Markets**

Canada has long relied on the U.S. to absorb its considerable production of forest products. The recent and precipitous decline in U.S. consumption of forest products, particularly lumber, has, in the words of John Allan, president and CEO of the Council of

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61 William Candline, Weyerhaeuser Company, *Committee Evidence*, March 11, 2008.

62 Avrim Lazar, Forest Products Association of Canada, *Committee Evidence*, February 14, 2008.

Forest Industries, “starkly expose our vulnerability to single-market dependency. We need to develop a balanced customer base, with particular emphasis on emerging Asian markets.”<sup>63</sup>

The industry must indeed look to China, India and other emerging economies as potential growth markets as these are the world’s two most populous countries. With GDP growth rates neighbouring 10% (in the case of both China and India), such countries are becoming wealthier, and millions of their citizens are joining the ranks of the middle-class each year. These populations are showing a tremendous appetite for wood and paper products. The Committee was told that at present only 5% of China’s population has access to tissue paper. Demand for such a product that we in Canada take for granted is expected to grow substantially in these emerging economies in the coming years.<sup>64</sup> Canada’s forest products companies, with the help of the federal government, need to understand what the needs of these new customers are and see how Canadian producers can meet that demand.

Canada has already taken steps to tap into these Asian (and other) markets. Natural Resources Canada’s Canada Wood Export Program is the central pillar of federal efforts to diversify export markets for Canadian wood products. Since the inception of the Canada Wood program in 2002, Canadian lumber shipments (by volume) to China have increased by 350%, to South Korea by 290%, and to the U.K. by 320%.

Canada has a reputation as a responsible forest steward. Through the International Forestry Partnerships Program and in partnership with the Canadian Council of Forest Ministers and industry, NRCan is working to increase international awareness and acceptance of forest products from Canada’s sustainably managed forests.

In the 2008 Budget, the federal government announced that it was setting aside \$10 million over two years to promote Canada’s forest sector as a model for environmental innovation and sustainability. While this is a step in the right direction, it remains a relatively small amount for such an important initiative. More should be done to deliver facts and information on Canada’s forests and forest products industry in important emerging markets so as to develop new markets and uses for Canada’s wood products. Any new efforts to educate buyers and diversify Canada’s exports of wood products should build on the strengths of existing programs.

**The Committee recommends that the Government of Canada consider expanding the life, the scope and the funding of the Canada Wood Export Program and the International Forestry Partnerships Program in**

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63 John Allan, Council of Forest Industries, *Committee Evidence*, March 4, 2008.

64 Jim Scarrow, City of Prince Albert, *Committee Evidence*, March 11, 2008.

**order to inform foreign buyers about the economic and environmental benefits of Canada’s wood products, with the aim of further developing export markets.**

Additional efforts must also be put into developing the non-residential wood construction market. NRCan estimates that this market, which includes hospitals, schools and other institutional buildings, including government buildings, is valued at up to \$25 billion annually in North America alone. Canada’s forest products industry would benefit greatly if it was able to capture even a small portion of this vastly important market.<sup>65</sup>

### **“Wood is Good”**

Canada is a global leader in forest stewardship and forest certification. It is also a global leader in the development and application of efficient wood construction techniques.

Canada has more third-party certified forest area and more protected forest area than any other country in the world. This is something to be proud of and something we can and should boast about. Canada can, and should, be a supplier of choice because of its exemplary environmental practices.

The fact that Canada is a leader in the sustainable management of its forests is in fact a competitive advantage for Canadian forest products companies. The market for certified products has grown exponentially over the last decade and that growth is expected to continue. According to Hugo Asselin of the Université du Québec en Abitibi-Témiscamingue, Canada is in a good position to take the lion’s share of this growth.<sup>66</sup> Already companies like Tembec and Cascade, that are offering certified forest products, are finding it easier to secure contracts with big buyers such as Home Depot.

More needs to be done, however, to promote wood in particular as a green, renewable building material, both here in Canada and abroad. While the great majority of witnesses who appeared before the Committee would agree with the statement that “wood is the most sustainable building material you can find”<sup>67</sup>, this fact does not seem to resonate widely in Canada or abroad. As Luc Bouthillier of Laval University told the Committee, domestically at least “we have to express to the consumer that there is an advantage to buy a green product made from the Canadian forest by Canadian companies

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65 Hughes Simon, AbitibiBowater, *Committee Evidence*, February 14, 2008.

66 Hugo Asselin, Université du Québec en Abitibi-Témiscamingue, *Committee Evidence*, March 11, 2008.

67 Ian de la Roche, FPInnovations, *Committee Evidence*, February 28, 2008.

through Canadian workers who are highly skilled and trained.”<sup>68</sup> Internationally, a greater focus can be put on Canada’s leadership in forest certification and sustainable forest management practices.

Canadian wood can and should be marketed as a building material of choice from an environmental perspective. Some studies suggest that it is superior to both steel and concrete in part because its production requires much less energy and water and is less greenhouse gas intensive. Moreover, as Réjean Gagnon of the Université du Québec à Chicoutimi told the Committee, “the forest is a natural and renewable resource [...] wood is [...] non-toxic, it captures CO<sub>2</sub>, it is renewable, recyclable and compostable [...]”<sup>69</sup>

**The Committee therefore recommends that the Government of Canada, in conjunction with the provincial governments and in partnership with the industry, architects, engineers, builders, suppliers of construction materials and the media, launch a campaign called “Building with Canadian Wood”, to inform decision-makers about wood’s superior environmental characteristics, ease of use as a building material, durability and excellent lifecycle cost. The campaign would highlight the possibilities of construction with wood as provided for under the standards, regulations and building codes, and would also have a technical aspect: the computerization of engineers’ framing calculations.**

**Moreover the Committee recommends that the Government of Canada call upon the National Research Council of Canada (NRC) to include in the National Building Code’s objectives the use of wood in all its forms for construction, and of on-site fireproofing techniques, new flame retardants and all other building technology developments, in light of the latest research and the availability of composite products. In other words, that the opening-up of the Code begun in 2005 be confirmed and continued.**

Leonard Compton, Mayor of the City of Kenora, suggested that Indian and Northern Affairs Canada should make a concerted effort to address the critical housing shortage on Indian reserves while the wood products industry is in a downturn: “Indian Affairs should be using our wood supply to put housing on reserves. If you stand in downtown Kenora, within 40 miles we have 10 reserves.” These reserves, and others like them, have a pressing need for housing, schools and other buildings. Why not get those built now using Canadian wood products?<sup>70</sup>

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68 Luc Bouthillier, Laval University, *Committee Evidence*, March 13, 2008.

69 Réjean Gagnon, Université du Québec à Chicoutimi, *Committee Evidence*, March 4, 2008.

70 Leonard Compton, City of Kenora, *Committee Evidence*, March 11, 2008.

## Climate Change, Carbon Sequestration and Carbon Credits

Climate change is having an important impact on Canada's forests. The emergence of the mountain pine beetle epidemic epitomizes the fact that climate change constitutes a major challenge to the sustainable management of Canada's forests. It is probable that the frequency and severity of insect pest outbreaks and other such challenges will increase in the coming years and decades. Jim Scarrow, mayor of the City of Prince Albert, Saskatchewan, testified that as a result of climate change, "Saskatchewan's boreal forest may disappear as we know it today [...] Today's forests are projected to move north."<sup>71</sup>

The forest has an important role to play in mitigating climate change. Governments must continue to support climate-friendly forest management practices and explore ways to contain the carbon that is stored in Canada's forests.

There are massive quantities of carbon locked up throughout the boreal region, particularly in the soil and peatlands. There may be market opportunities for forest companies, forest communities and First Nations that find innovative ways to ensure that that carbon stays locked up through sustainable land use practices. Canada, as custodian of one of the world's largest forested areas, has a great responsibility to explore mechanisms to keep the carbon that is stored in forests from being released into the atmosphere.<sup>72</sup>

Forests, the Committee was reminded, have value beyond just the fibre resource. As David Cohen of UBC testified,

The crisis is with the wood, not with the forest. There are values in the forest that there are opportunities to commercialize [...] We don't know what the most valuable resource in our forest is going to be in 20 years, it could be water, it could be carbon sequestration, it could be biodiversity credits, but we have to manage so that we can maximize the value of the forest, not of the wood resource, and that requires a bit of a different mindset.<sup>73</sup>

Governments in Canada can encourage forest management and forestry practices that sustain biodiversity and encourage carbon sequestration. For example, there may be forested areas that are not particularly valuable for harvesting fibre but could nevertheless have economic value as stores of carbon. It was suggested to the Committee that such areas could be set aside. Companies that set aside a portion of their land tenures could be granted carbon or biodiversity credits once such systems are developed.

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71 Jim Scarrow, City of Prince Albert, *Committee Evidence*, March 11, 2008.

72 Mary Granskou, Canadian Boreal Initiative, *Committee Evidence*, March 4, 2008.

73 David Cohen, University of British Columbia, *Committee Evidence*, March 13, 2008.

One practical way in which the federal government can do its part to encourage climate-friendly forest management practices is by designing a carbon offset system that offers carbon credits to forest companies, and forest communities that undertake forestry activities that either remove greenhouse gases from the atmosphere or avoid emitting greenhouse gases in the first place. The Committee heard from several witnesses that a properly designed offset system could be of significant benefit not only to the environment but also to the forest industry and to forest communities, including Aboriginal communities.

Carbon credits under an offset system could conceivably be generated by activities such as forestation, reforestation, avoided deforestation and forest management that increase carbon sequestration or avoid/reduce emissions in a way that goes beyond business as usual practices. In a recently released document, the federal government indicated that it would consider recognizing forest management projects of the type outlined above as possible generators of carbon offset credits.<sup>74</sup> Firms that are to be regulated under the Clean Air Regulatory Agenda may also be able to undertake forest carbon sequestration projects as a way of meeting their greenhouse gas emissions reduction targets. The Committee was informed that Natural Resources Canada and Environment Canada are currently developing provisions for forest carbon sequestration projects as a compliance mechanism for regulated firms.<sup>75</sup>

**The Committee recommends that the Government of Canada emphasize the deployment of its greenhouse gas regulatory framework and any other mechanisms, including offsets, that could further promote climate-friendly forest management and conservation practices.**

**The Committee further recommends that the forest products industry's efforts to reduce emissions since 1990 be taken into consideration by the Government of Canada as it develops new emissions regulations.**

The Committee was reminded by a number of witnesses that the establishment of a carbon market will not solve the industry's troubles. As Don Roberts of CIBC World Markets told the Committee, "It's one positive step, but it's not your single solution, partly because we do not grow trees fast enough. But it will help" as long as our competitors also operate under a similar system.<sup>76</sup>

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74 Environment Canada, *Canada's offset system for greenhouse gases*, March 2008.

75 Cassie J. Doyle, Deputy Minister, Natural Resources Canada, letter to the Committee, March 12, 2008.

76 Don Roberts, CIBC World Markets, *Committee Evidence*, March 4, 2008.

## Fibre Pricing and Tenure

While these are not areas of federal responsibility, the Committee did hear evidence that the current system of land tenure and stumpage in some provinces is uncompetitive in this age of increased global competition.

The cost of fibre is the industry's single biggest cost component and can represent up to 60% of variable costs. Many witnesses testified that the cost of fibre in Canada, particularly in Quebec, is high. A related problem is that while there is abundant high-quality wood fibre in many regions of the country, the link between price and quality is in many instances rather tenuous. It was suggested to the Committee that stumpage fees should reflect the quality of the wood fibre.

It bears repeating that land tenure and stumpage systems are the responsibility of individual provinces. Some witnesses suggested that one way to reduce fibre costs, notably in Quebec, would be by stimulating intensive planting on private woodlots located close to existing mills. This is important because, in Quebec for example, private woodlot owners supply some 20% of the wood fibre destined for mills. Because private woodlots are typically closer to mills, transportation distances and costs are reduced, which incidentally also reduces transportation greenhouse gas emissions.<sup>77</sup>

The Committee heard testimony that with markets at an all-time low, "now is the time to invest in our forests so that planning and silviculture activities can be undertaken. [...] This would be the best way for private woodlot owners to contribute to the recovery of the forestry sector".<sup>78</sup>

**The Committee recommends that the federal government, in collaboration with the provinces and territories, promote and support silviculture on private and Crown Lands within their relevant jurisdictions.**

Ideally, land tenure and stumpage systems should be transparent and market based. Appurtenancy<sup>79</sup> policies which tie forest tenure to local mill jobs, the Committee was told, seldom achieve the desired results as they ultimately prevent the emergence of

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77 Francis Albert, Corporation Agro Forestière Transcontinentale Inc., *Committee Evidence*, March 11, 2008.

78 Jean-Pierre Dansereau, Fédération des producteurs de bois du Québec, *Committee Evidence*, February 28, 2008.

79 Appurtenancy refers to the requirement of a forest tenure holder to construct, modify or maintain a timber processing facility.

globally competitive companies.<sup>80</sup> Transparent and market based tenure and stumpage systems will help companies make appropriate investment decisions and facilitate a more efficient use of the resource by allowing wood fibre to flow to its highest value and best use.

### **Taxation of Woodlot Owners**

The Committee received evidence that under the current tax system, woodlot owners pay higher taxes on revenue earned compared to other taxpayers as they tend to receive a large, single payment when their wood is harvested and are restricted in what they can deduct as expenses (and on the timing of these deductions).

Private woodlot owners, who engage in activities to salvage killed or damaged stands of timber following natural catastrophes, are particularly likely to have a large, one time “revenue hit” which can give rise to a sizeable tax burden.

**The Committee therefore recommends that the Government of Canada introduce changes to income tax rules and regulations to facilitate the deduction of forest management expenses and to allow for income averaging from woodlot management activities, notably when the income shock is the result of natural disasters such as the mountain pine beetle epidemic.**

### **Aboriginal Communities**

Aboriginal communities have enormous needs when it comes to training and capacity development. While many such communities are located in or near forests, not all benefit from the forestry activities they see occurring around them. First Nations and other Aboriginal communities must become meaningful partners in forest planning, management, and development activities. This is an important component of the sustainable development of Canada’s forests. The Government of Canada, by virtue of its constitutional responsibilities, has an important role to play in making sure that Aboriginal Canadians become active participants and partners in the forest industry of the 21<sup>st</sup> century.

**The Committee therefore recommends that the Government of Canada continue to work with First Nations and other Aboriginal communities to enable them to become active partners in the sustainable development of Canada’s forests.**

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80 Avrim Lazar, Forest Products Association of Canada, *Committee Evidence*, February 14, 2008.

## Log Exports

Raw logs are typically exported for various economic reasons. In British Columbia, raw logs can only be exported from private lands once an export license has been granted by Foreign Affairs and International Trade Canada. While raw logs represent only a very small proportion of Canada's total forest products exports, some, particularly in British Columbia and Ontario, have expressed concerns that the export of logs is tantamount to the export of jobs. These logs, it is argued, should be processed in Canada.

**The Committee therefore recommends that the Government of Canada work with the provinces and territories and with Aboriginal communities to explore opportunities for adding value, in Canada, to the logs that would otherwise be exported in an unprocessed state.**

## Resource Protection and Management

Canada's forest ecosystems have always been subject to cyclical changes resulting from infestations of pests and forest fires, and Natural Resources Canada has long taken an interest in forestry science. For several years now, British Columbia's forests have been affected by what will undoubtedly turn out to be the worst insect infestation in recent history. The infestation of the interior forests by the mountain pine beetle now extends as far as Alberta and has destroyed almost 600 million cubic metres of valuable wood, which has led to a reduction in the value of the resource.<sup>81</sup> This situation has affected many communities that derive their livelihood from the forest, and it is likely to get worse when the affected trees can no longer be processed into forestry products. They could however become an important source of biomass for bioenergy.

In Budget 2006, the Government of Canada has allocated \$200 million — of a commitment of \$400 million for forest related initiatives — specifically to mitigate the effects of the mountain pine beetle infestation and help curb its spread. It is working closely with British Columbia and Alberta to assess the risks and target efforts in order to limit the infestation's eastward spread. For the moment, it appears that these efforts, combined with an exceptionally cold winter, are having a positive impact. Roughly half of the \$200 million was earmarked for establishing measures designed to slow the spread, find ways to make better use of the affected trees and work with the communities to protect the trees at risk. The other half was allocated essentially to mitigate the infestation's economic impact.<sup>82</sup>

However, according to some of the witnesses the Committee heard, there is still a lot to do. The situation is particularly worrisome for communities in the infested areas because of the heightened risk of forest fires. The federal government is working with the

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81 John Allan, Council of Forest Industries, *Committee Evidence*, March 4, 2008.

82 Jim Farrell, Natural Resources Canada, *Committee Evidence*, February 12, 2008.

First Nations and communities of British Columbia on strategies to reduce the risk, both on reserves and on the public lands around them. It nevertheless seems that the needs in this area remain pressing.

According to Chief Bill Williams,<sup>83</sup> some 100,000 Aboriginal people in 103 communities are surrounded by dried-out forests in which the forest fire risk keeps rising. There are 13 million hectares of affected forest, and Chief Williams says the trees would have to be cut down in a 2-kilometre cordon around 109 Aboriginal reserves to ensure the reserves' safety. This would mean harvesting 135,000 hectares of trees at a cost of approximately \$1000 a hectare, or \$135 million in total.

In easternmost Canada, the brown spruce longhorn beetle has proven problematic. In this case, it is not so much the extent of the infestation that is causing concern, but the phytosanitary measures established to deal with it. Unlike British Columbia's mountain pine beetle, the brown spruce longhorn beetle is not indigenous; it is a non-native invader from Europe and Asia. It is thus up to the Canadian Food Inspection Agency (CFIA) to evaluate the phytosanitary risk and take measures to limit the spread of the insect, first detected in Nova Scotia in 1999. Initially confined to the Point Pleasant Park sector in Halifax, the brown spruce longhorn beetle has spread out to 25 other locations outside the original containment area. Although the level of infestation is low,<sup>84</sup> the pest is nevertheless subject to strict regulatory control measures by the CFIA, particularly with respect to the transportation of wood fibre. Some representatives of the Maritimes' forest industry are asking the federal government to acknowledge the brown spruce longhorn beetle's potentially devastating affect on the region's forestry sector and to provide the necessary resources to manage this problem adequately.<sup>85</sup>

**The Committee recommends that the federal government, along with the provinces, territories and Aboriginal governments, focus specifically on protecting all vulnerable communities threatened by forest fires in the areas affected by the mountain pine beetle and on addressing the spread of the brown spruce longhorn beetle. To that end, the federal government must provide the necessary resources, both to conduct research on these insects and to directly fund the necessary protection measures.**

In addition to the question of protecting forests against insects, diseases and fires, many Committee witnesses also raised the whole issue of planning and sharing the forestry resource among various users. Of course, forest management as such is primarily a provincial and territorial responsibility, but certain aspects require the federal

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83 Chief Bill Williams, *Committee Evidence*, March 11, 2008.

84 Canadian Food Inspection Agency, *Questions and Answers – Brown Spruce Longhorn Beetle*, CFIA's website (<http://www.inspection.gc.ca/english/plaveg/pestrava/tetfus/bslbqueste.shtml>).

85 Diane Blenkhorn, Maritime Lumber Bureau, *Committee Evidence*, March 6, 2008.

government's participation, particularly in connection with responsibilities for Aboriginal peoples. The representatives of the Canadian Boreal Initiative (CBI) also said that some 60% of the boreal region is currently the subject of various planning exercises. The CBI feels that the issue of Aboriginal land rights can be a source of great uncertainty for logging companies, and that the main way to resolve this uncertainty is through regional land use planning.

Regional planning conducted in partnership with Aboriginal peoples, governments and other stakeholders can determine the areas to develop or protect in a way that reconciles ecological and cultural values and promotes sustainable development of the forestry resource. In order to improve the climate of certainty for the industry and to meet the federal government's obligations to Aboriginal peoples, the representative of the Canadian Boreal Initiative recommended that the Committee support "significantly increasing federal funding for regional land use planning, in collaboration with the provinces, territories and Aboriginal peoples and respective stakeholders."<sup>86</sup>

**Recognizing that the management of natural resources, including forests, is primarily a provincial responsibility, the Committee recommends that the federal government work with the provinces and territories to establish regional land use planning processes that respect the jurisdiction of the different levels of government.**

The Canadian Boreal Initiative's primary objective in the medium and long term is to protect roughly half the Canadian boreal forest and to ensure sustainable management of the forestry resources in the other half. Many feel that Canada, as the trustee of some of the largest intact forests in the world, has a duty to ensure that they can remain an important economic resource for the communities and provide a wide array of ecological services such as carbon storage. At the present time, "only about 9% of Canada's boreal forest, where most of the logging occurs, is permanently protected from industrial activity and oil and gas development."<sup>87</sup>

The representative of the Canadian Parks and Wilderness Society also insisted on the importance of guaranteeing the protection of a significant portion of the forest ecosystems, particularly in the north where natural forests are still abundant. Both the Canadian Boreal Initiative and the Canadian Parks and Wilderness Society feel that one of the environmental advantages both the clientele and public are calling for is protected forest zones alongside logging areas.

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86 Brief of the Canadian Boreal Initiative presented before the Committee by Mary Granskou, Senior Policy Advisor, March 4, 2008.

87 Tim Gray, Canadian Parks and Wilderness Society, *Committee Evidence*, March 6, 2008.

**The Committee therefore recommends that the federal government, working with its provincial and territorial partners, increase its conservation efforts in the natural forest ecosystems, particularly in the boreal zone.**

## **Forest Certification**

While stressing the need to protect and manage the forests, a number of witnesses from a wide range of backgrounds and organizations also stressed the importance of the role and promotion of forest certification. In general terms, forest certification is a voluntary, non-regulatory, and market-based instrument designed to recognize and promote environmentally-responsible forestry and sustainability of forest resources. The certification process involves an evaluation of management planning and forestry practices by a third-party according to an agreed-upon set of standards that takes environmental, economic and social values into consideration.

Given that Canada is a leader in the certification of forestry operations — 138 million hectares of forest are now third-party certified in Canada “which account for 40% of the total amount of certified forest in the world”<sup>88</sup> —, many witnesses heard by the Committee see it as a distinct advantage for the industry at the international level. Some feel that our ability to manage our forests sustainably may become a major advantage over our competitors — especially the Russians — if we continue on this path and market this aspect intelligently.<sup>89</sup> Others said that some forestry companies were better able to resist the crisis of recent years because they chose to certify their operations and to produce niche products that are increasingly attractive to the large chains and consumers.

Mr. Dansereau of the Fédération des producteurs de bois du Québec stated that “Woodlot owners can contribute in a number of different ways: We are involved in the production of traditional forest products, [... and] we could play a role in providing Canadians with forest-based environmental good and services”<sup>90</sup>. To do that the woodlot owners suggested that the government could assist with specific aspects of forest management on private land including land development and management and tax policy.

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88 Forest Products Association of Canada, *Ask\* – FPAC 2007 Annual Review*.

89 Don Roberts, CIBC World Markets, *Committee Evidence*, March 4, 2008.

90 Jean-Pierre Dansereau, Fédération des producteurs de bois du Québec, *Committee Evidence*, February 28, 2008.

**The Committee recommends that that federal government, in collaboration with the provinces and territories, explore implementing a program for woodlot owners similar to the Beneficial Management Practices (BMP) program delivered by Agriculture and Agri-Food Canada and the provinces.**

Of course, certification is primarily the responsibility of the industry, which must choose among three very different certification systems, managed by the Forest Stewardship Council (FSC), the Canadian Standards Association (CSA) and the Sustainable Forest Initiative (SFI). The federal government has never wanted to get involved by advocating one system over the others. However, a number of stakeholders feel that the FSC approach is preferred by more of the large retail chains and by consumers because it is entirely independent of the forest products industry and has greater international recognition. Whatever the preferred certification system, the Committee concurs with those witnesses who suggested that Canada must encourage and promote forest certification as a trademark of the Canadian forest products industry.

**The Committee recommends that the federal government, working with the provinces and territories, provide full support for the certification of Canadian forest products and operations and that it actively promote them in its programs and campaigns for the Canadian forest industry, such as the “Value to Wood” program. The ultimate goal should be that 100% of Canada’s forest operations and products be certified.**

### **Labour Force and Expertise**

The evidence given before the Committee clearly established that it is important and urgent not only to invest in research, technology and factories, but also in people. Many confirmed that fewer and fewer students are entering the forestry engineering faculties and specialized pulp and paper programs. The same is true of the technical programs that train specialized workers, for both the factory and the forest. Young students find the health and business sectors more attractive than the science sector. And yet it is engineers and chemists that the industry desperately needs to work in wood processing, both in the lumber and pulp mills and in the emerging bio-economy.

**In light of the Canadian forest industry’s need for a first-rate labour force and expertise in all areas, the Committee recommends that Natural Resources Canada and its partners undertake an assessment of the forestry sector’s labour force and expertise needs.**

## The Problem of Rail Transportation

The problem of transporting lumber was raised a number of times, especially in the context of railway transportation in Western Canada. The problem emerged as sufficiently important for the Committee to decide to dedicate an entire meeting to it. Witnesses said that Canadian rail shipping rates are amongst the highest in the world and that the rail service provided to wood and forest products shippers is below their expectations.

The Committee received evidence that the forest products industry is the biggest user of rail services in Canada and the second-largest consumer of trucking services. Overall, the Forest Products Association of Canada said that about 70% of the industry's merchandise is shipped by rail and 30% by truck. The ratio is higher in the West and a little lower in the East. The forest sector alone accounts for some 25% of Canadian railways' total revenues. In all segments of the Canadian forest products industry, transportation costs represent a significant portion of the price of the delivered product, and rank second among the cost components in this sector. That is why FPAC considers that a cost-effective and efficient transportation system that is responsive to its users' needs is a critical competitiveness factor for the forest products industry.<sup>91</sup>

The industry has noted a significant deterioration in rail services while costs have continued to climb. The witnesses heard by the Committee indicated that rail service is inadequate and irregular both in the West and in Ontario, where plants are systematically assigned fewer rail cars than they require to meet their clients' needs. The Buchanan Group (Pulp and Timber), for example, testified that it needs 120 cars a week but is receiving only 70, so that the company is forced to store a significant portion of its production anywhere it can find, if not to cut back on production.<sup>92</sup> At a time when the forest products industry is going through an unprecedented crisis, it would be extremely unfortunate to have to close more plants, even if only temporarily, simply because their products could not be shipped to clients, the Committee was told.

The witnesses heard by the Committee explained that high costs and mediocre service are attributable to the monopoly situation that today characterizes the rail transport sector. Lack of competition is most damaging for companies situated in remote regions that are captive to this mode of transportation, which incidentally applies to most Canadian forest products companies. According to an FPAC study, the "Canadian forest products companies are paying \$280 million annually more to the railways than they would be paying if they had effective competition".<sup>93</sup>

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91 Presentation and evidence by the Forest Products Association of Canada to the Standing Committee on Natural Resources, April 1, 2008.

92 Evidence of Pino Pucci and Hal Brindley, Buchanan Pulp Sales and Buchanan Timber Sales, April 1, 2008.

93 Forest Products Association of Canada, presentation to the Standing Committee on Natural Resources, April 1, 2008.

The industry representatives are nevertheless encouraged by the recent passage of Bill C-8, *An Act to Amend the Canada Transportation Act (railway transportation)*, and by the federal government's commitment to proceed with a rail service review in the 30 days following the Bill's passage. The Committee supports the industry's demand that the review be comprehensive, independent and allow for the full participation of shippers.

The Committee agrees that rail transportation constitutes a key element in the functioning and prosperity of Canada's forest products industry. Railways are indispensable from both an economic and an environmental standpoint, and the current situation affecting the forest products industry must be rapidly addressed.

**Therefore, the Committee recommends that, in addition to the rail service review undertaken following the adoption of Bill C-8 (including issues affecting the forest industry), the federal government undertake a study on the issue of railway rates and consider developing an intermodal transportation strategy that could address the concerns raised by the forest products industry.**

## CONCLUSION

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Canada's forest industry has a long and largely successful history. Forests and forest-related activities have contributed greatly to the development of this country; hundreds of communities and hundreds of thousands of Canadians are economically dependent on the forest industry.

Today the industry is in the midst of a serious crisis; numerous mills and plants have been closed or are closing and job losses number in the tens of thousands. Many forest communities face an uncertain future.

A number of factors, both domestic and international, explain the precarious situation in which Canada's forest industry now finds itself. Chief among them are the depressed U.S. housing market, the rapid appreciation of the Canadian dollar, the mountain pine beetle epidemic, and the intensification of global competition coupled with years of underinvestment in Canada in new technologies and equipment.

The Committee is of the view that the challenges facing the industry are not insurmountable. This is an industry which continues to have tremendous potential for sustainable growth. Canada has the land, the water, the energy and the institutions to be a global leader in this industry.

The Committee hopes that this report and its recommendations will galvanize the industry, governments and other stakeholders to work together to lay the groundwork for the industry's renewal, prosperity and sustainability.

## **LIST OF RECOMMENDATIONS**

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### **RECOMMENDATION 1: (p. 20)**

The Committee has heard evidence from a number of stakeholders and believes it would be in the public interest for the Prime Minister to convene a National Summit, with all stakeholders, on the future of the Canadian forest industry with a view to developing a national strategy to support the renewal of the industry while respecting provincial and territorial jurisdictions.

### **RECOMMENDATION 2: (p. 26)**

The Committee therefore recommends that the federal government, in collaboration with provincial and territorial governments and the industry, establish a national forest industry innovation fund, and that this fund be provided with sufficient resources to ensure that the industry can be central in the development of the new bioeconomy.

### **RECOMMENDATION 3: (p. 27)**

The Committee therefore recommends that the Government of Canada consider putting additional funds into the ecoENERGY for Renewable Power program and consider extending its scope to cover the production of thermal energy from renewable sources such as biomass.

### **RECOMMENDATION 4: (p. 28)**

The Committee therefore recommends that the Government of Canada, working with the provinces and territories, assess the impacts of a more intensive use of biomass on forest ecosystems and on the environment, and where appropriate provide increased funding for research and development on bioenergy and bioproducts. Conditions for increased funding should be based upon energy conversion factors, greenhouse gas emissions, and impacts on regional forest economies.

**RECOMMENDATION 5: (p. 28)**

**The Committee concurs and therefore recommends that the Government of Canada, in partnership with the provinces and territories, actively pursue policies that encourage value-added manufacturing.**

**RECOMMENDATION 6: (p. 29)**

**Given the importance and scope of the Value to Wood program, your Committee recommends that it be extended beyond the current expiry date of March 2009 in a predictable fashion.**

**RECOMMENDATION 7: (p. 30)**

**The Committee therefore recommends that Canada's Competition Bureau examine its methods for analyzing mergers and acquisitions in the forest products industry and explicitly take into account the international nature of forest products markets.**

**RECOMMENDATION 8: (p. 31)**

**The Committee recommends that the federal government, in conjunction with the provinces and territories, consider investments in innovative research and development programs that stimulate cooperation and facilitate the formation of industrial forest clusters as in Finland.**

**RECOMMENDATION 9: (p. 33)**

**The Committee therefore recommends that the Government of Canada examine ways to improve the scientific research and experimental development (SR&ED) tax incentive program, such as by offering refundable tax credits, to ensure that it plays a critical role in supporting the recovery of the forest products industry.**

**Similarly, the Committee recommends that the Government of Canada consider fully extending for the next five years the accelerated capital cost allowance (CCA) treatment for investments in manufacturing or processing machinery.**

**RECOMMENDATION 10: (p. 34-35)**

**The Committee recommends that the Government of Canada consider expanding the life, the scope and the funding of the Canada Wood Export Program and the International Forestry Partnerships Program in order to inform foreign buyers about the economic and environmental benefits of Canada's wood products, with the aim of further developing export markets.**

**RECOMMENDATION 11: (p. 36)**

**The Committee therefore recommends that the Government of Canada, in conjunction with the provincial governments and in partnership with the industry, architects, engineers, builders, suppliers of construction materials and the media, launch a campaign called "Building with Canadian Wood", to inform decision-makers about wood's superior environmental characteristics, ease of use as a building material, durability and excellent lifecycle cost. The campaign would highlight the possibilities of construction with wood as provided for under the standards, regulations and building codes, and would also have a technical aspect: the computerization of engineers' framing calculations.**

**Moreover the Committee recommends that the Government of Canada call upon the National Research Council of Canada (NRC) to include in the National Building Code's objectives the use of wood in all its forms for construction, and of on-site fireproofing techniques, new flame retardants and all other building technology developments, in light of the latest research and the availability of composite products. In other words, that the opening-up of the Code begun in 2005 be confirmed and continued.**

**RECOMMENDATION 12: (p. 38)**

**The Committee recommends that the Government of Canada emphasize the deployment of its greenhouse gas regulatory framework and any other mechanisms, including offsets, that could further promote climate-friendly forest management and conservation practices.**

**The Committee further recommends that the forest products industry's efforts to reduce emissions since 1990 be taken into consideration by the Government of Canada as it develops new emissions regulations.**

**RECOMMENDATION 13: (p. 39)**

**The Committee recommends that the federal government, in collaboration with the provinces and territories, promote and support silviculture on private and Crown Lands within their relevant jurisdictions.**

**RECOMMENDATION 14: (p. 40)**

**The Committee therefore recommends that the Government of Canada introduce changes to income tax rules and regulations to facilitate the deduction of forest management expenses and to allow for income averaging from woodlot management activities, notably when the income shock is the result of natural disasters such as the mountain pine beetle epidemic.**

**RECOMMENDATION 15: (p. 40)**

**The Committee therefore recommends that the Government of Canada continue to work with First Nations and other Aboriginal communities to enable them to become active partners in the sustainable development of Canada's forests.**

**RECOMMENDATION 16: (p. 41)**

**The Committee therefore recommends that the Government of Canada work with the provinces and territories and with Aboriginal communities to explore opportunities for adding value, in Canada, to the logs that would otherwise be exported in an unprocessed state.**

**RECOMMENDATION 17: (p. 42)**

**The Committee recommends that the federal government, along with the provinces, territories and Aboriginal governments, focus specifically on protecting all vulnerable communities threatened by forest fires in the areas affected by the mountain pine beetle and on addressing the spread of the brown spruce longhorn beetle. To that end, the federal government must provide the necessary resources, both to conduct research on these insects and to directly fund the necessary protection measures.**

**RECOMMENDATION 18: (p. 43)**

Recognizing that the management of natural resources, including forests, is primarily a provincial responsibility, the Committee recommends that the federal government work with the provinces and territories to establish regional land use planning processes that respect the jurisdiction of the different levels of government.

**RECOMMENDATION 19: (p. 44)**

The Committee therefore recommends that the federal government, working with its provincial and territorial partners, increase its conservation efforts in the natural forest ecosystems, particularly in the boreal zone.

**RECOMMENDATION 20: (p. 45)**

The Committee recommends that that federal government, in collaboration with the provinces and territories, explore implementing a program for woodlot owners similar to the Beneficial Management Practices (BMP) program delivered by Agriculture and Agri-Food Canada and the provinces.

**RECOMMENDATION 21: (p. 45)**

The Committee recommends that the federal government, working with the provinces and territories, provide full support for the certification of Canadian forest products and operations and that it actively promote them in its programs and campaigns for the Canadian forest industry, such as the “Value to Wood” program. The ultimate goal should be that 100% of Canada’s forest operations and products be certified.

**RECOMMENDATION 22: (p. 45)**

In light of the Canadian forest industry’s need for a first-rate labour force and expertise in all areas, the Committee recommends that Natural Resources Canada and its partners undertake an assessment of the forestry sector’s labour force and expertise needs.

**RECOMMENDATION 23: (p. 47)**

**Therefore, the Committee recommends that, in addition to the rail service review undertaken following the adoption of Bill C-8 (including issues affecting the forest industry), the federal government undertake a study on the issue of railway rates and consider developing an intermodal transportation strategy that could address the concerns raised by the forest products industry.**

# APPENDIX A LIST OF WITNESSES

Organizations and Individuals	Date	Meeting
<p><b>Department of Natural Resources</b></p> <p>Cassie Doyle, Deputy Minister Jim Farrell, Assistant Deputy Minister, Canadian Forest Service</p>	2008/12/02	15
<p><b>AbitibiBowater Inc.</b></p> <p>Hugues Simon, Vice-President, Value-Added Wood Products</p>	2008/02/14	16
<p><b>Forest Products Association of Canada</b></p> <p>Avrim Lazar, President and Chief Executive Officer Tom Rosser, Chief Economist</p>		
<p><b>Quebec Forest Industry Council</b></p> <p>Michel Vincent, Director, Economics, Markets and International Trade</p>		
<p><b>As an individual</b></p> <p>Emilio Rigato</p>	2008/02/28	17
<p><b>Communications, Energy and Paperworkers Union of Canada</b></p> <p>David Coles, President Keith Newman, Assistant to the President</p>		
<p><b>Fédération des producteurs de bois du Québec</b></p> <p>Jean-Pierre Dansereau, Director General Pierre-Maurice Gagnon, President</p>		
<p><b>FPInnovations</b></p> <p>Ian de la Roche, President and CEO</p>		
<p><b>Canadian Boreal Initiative</b></p> <p>Mary Granskou, Senior Policy Advisor</p>	2008/04/03	18
<p><b>CIBC World Markets</b></p> <p>Don Roberts, Managing Director</p>		
<p><b>Council of Forest Industries</b></p> <p>John Allan, President and CEO</p>		
<p><b>Université du Québec à Chicoutimi</b></p> <p>Réjean Gagnon, Research Professor, Director and Coordinator of the Consortium de recherche sur la forêt boréale commerciale (CRFBC) , Department of Basic Sciences</p>		

# APPENDIX A LIST OF WITNESSES

Organizations and Individuals	Date	Meeting
<p><b>Canadian Parks and Wilderness Society</b> Tim Gray, Chair, Conservation Committee of the Board</p> <p><b>Maritime Lumber Bureau</b> Diana Blenkhorn, President and Chief Executive Officer</p> <p><b>McMaster University</b> Robert Pelton, Professor of Chemical Engineering</p> <p><b>SENTINEL Bioactive Paper Network</b> George Rosenberg, Managing Director</p> <p><b>Township of James and Town of Elk Lake</b> Jeff Barton, Community Development Forester Terry Fiset, Reeve, Township of James George Lefebvre, Community Development Advisor</p>	2008/06/03	19
<p><b>City of Kenora</b> Leonard Compton, Mayor</p> <p><b>City of Prince Albert</b> Jim Scarrow, Mayor</p> <p><b>Corporation agro-forestière Trans-Continental Inc.</b> Francis Albert, President and Chief Executive Officer</p> <p><b>First Nations Forestry Council</b> Bill Williams, Director</p> <p><b>Université du Québec en Abitibi-Témiscamingue</b> Hugo Asselin, Professor, Department of Humanities and Social Development</p> <p><b>Weyerhaeuser Company</b> William Candline, Plant Manager, Kenora Laminated Strand Lumber Facility</p>	2008/11/03	20
<p><b>J. D. Irving Limited</b> James D. Irving, President Christopher MacDonald, Director, Government Relations</p>	2008/03/13	21

# APPENDIX A LIST OF WITNESSES

Organizations and Individuals	Date	Meeting
<b>United Steelworkers</b>		
Joe Hanlon, President, Local 2693		
Bob Matters, Chair, Steelworkers' Wood Council		
<b>Université Laval</b>		
Luc Bouthillier, Full Professor, Department of Wood and Forestry Science, Faculty of Forestry and Geomatics		
<b>University of British Columbia</b>		
David Cohen, Professor, Faculty of Forestry		
Jack Saddler, Dean of the Faculty of Forestry and Professor of Forest Products Biotechnology		
<b>Buchanan Lumber Sales</b>	2008/01/04	22
John Adams, Transportation Manager		
Hal Brindley, President		
<b>Buchanan Pulp Sales</b>		
Pino Pucci, President		
David Church, Director, Transportation, Recycling and Purchasing		
Marta Morgan, Vice-President, Trade and Competitiveness		
<b>Terrace Bay Pulp Inc.</b>		
Hartley Multamaki, Vice-President, Planning and Development		

# **APPENDIX B LIST OF BRIEFS**

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## **Organizations and Individuals**

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**Railway Association of Canada**

**Canadian Boreal Initiative**

**Canadian Parks and Wilderness Society**

**McMaster University**

**J. D. Irving Limited**

**United Steelworkers**

**Buchanan Pulp Sales**

**Communications, Energy and Paperworkers Union of Canada**

**CIBC World Markets**

**City of Kenora**

**City of Prince Albert**

**Council of Forest Industries**

**Corporation agro-forestière Trans-Continental Inc.**

**Fédération des producteurs de bois du Québec**

**First Nations Forestry Council**

**Forest Products Association of Canada**

**FPIinnovations**

**Maritime Lumber Bureau**

**Terrace Bay Pulp Inc.**

**Township of James and Town of Elk Lake**

**University of British Columbia**

**Université du Québec en Abitibi-Témiscamingue**

# MINUTES OF PROCEEDINGS

A copy of the relevant Minutes of Proceedings ([Meetings Nos.15-29 and 31-34](#)) is tabled.

Respectfully submitted,

Leon Benoit, MP  
Chair