Review of the Forest Products Commission and the forest policy in Western Australia

August 2009

Prepared by:

Haydn Lowe
Management Consultant
29 Loch Street
CLAREMONT
Western Australia 6004

Telephone: +61 (08) 9386 3589
Mobile: 0408 524 886

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Cover images: Red-tailed Black Cockatoos (*Calyptorhynchus magnificus*) nesting in a marked habitat tree.

Letter of transmission

29 Loch Street
Claremont WA 6010

The Hon Terry Redman
Minister for Agriculture and Food, Forestry
Dumas House
Havelock Street
WEST PERTH WA 6005

Dear Minister,

Review of the Forest Products Commission

Thank you for the opportunity to conduct a review of the Forest Products Commission, the report of which is attached.

The review was commissioned in order to "run a ruler" over the Commission, based on the Functional Review of 2005, the Legislative Review of 2006 and developments that have occurred subsequently.

In my view, the Commission is a sound organisation, well regarded generally, and has much to offer Western Australia, particularly in the context of carbon mitigation and in the provision of forestry to meet the "triple bottom line" objectives of Government. The Commission has faced many hurdles, not of its own making, and given the opportunity is capable of significant achievement in the future.

I would like to thank your office for its support and acknowledge the contribution of many organisations and individuals to this review.

I would also like to acknowledge the openness and cooperation provided by the Forest Products Commission throughout.

I wish you and the Commission well in your future tasks.

Yours sincerely,

Haydn Lowe
August 25, 2009

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Executive summary

Government has traditionally played an important role in the forestry industry. This stems from the need for forest products, use of a publicly owned resource, long time frames in developing and renewing the resource and the range of environmental, social (public good) and economical benefits provided by the industry.

Given the present debate surrounding climate change and the environment, the industry will continue to evolve in size and importance. It is in this context that the following policy position is recommended.

Recommendations – Forest Policy

It is recommended the following be adopted as WA Government forestry policy:

1. Western Australia will continue to have a forestry industry.
2. This industry will consist of native hardwood (the quantity yet to be determined), plantations, sandalwood and a range of new physical and environmental products in line with the developing economy.
3. Carbon mitigation through sequestration/biomass is seen as important.
4. Forestry is seen as one of the solutions to erosion control and salinity management.
5. Industry development and employment are important objectives of the industry.
6. The Government will continue in its goal to meet the triple bottom line objective – in the forestry industry – of economic, environmental and social benefit.

In summary, it is recommended that delivery be through a Forest Products Commission re-configured as a Statutory Authority for its operations and as a Department for the purposes of the Public Sector Management Act. It is further recommended that the Authority be responsible to a Board consisting of people selected on the basis of their knowledge and experience of environmental management, community/social development, commerce and industry; that is, across the various environments within which the Commission operates.

It is proposed that State forest and regrowth forest not yet gazetted formal reserve (with some exception) be vested in the Forest Product Commission along with state held plantations and land allocated for that purpose. The FPC would develop its own Forest Management Plan, but would be subject to meeting environmental standards.

It is recommended that the FPC be funded from consolidated revenue, but that it includes a unit within it with responsibility for the marketing of forest products. Income from this will be allocated at the discretion of Government but should perhaps be targeted at the achievement of the "triple bottom line". Any "competition" in the commercial sector would be required to meet the requirements of National Competition Policy.

The FPC currently operates at a slight profit from pine plantations and sandalwood and a marginal gain from native hardwood. Its capacity to improve its financial performance is restricted by regulatory limitations and the size of plantations established over the past 30 years.

Investment in new plantations and tree farms must therefore come from new investment as it cannot come from the FPC's own resources. Given the changes and limitations in funding programs for salinity control and natural resource management, the most likely source of new capital is for carbon off-sets for the energy sector. The market for the carbon economy looks to be six to 18 months away, the FPC having companies indicating a willingness to commit to this investment at that time.

During this hiatus, it is recommended FPC be funded an additional one-off $10m over 2009 – 2010 (spread over two financial years). In the current economic climate this appears difficult. However, for reasons elaborated in the review, injecting this capital will generate considerable income for the State. Not to do so will result in the loss of at least this amount to the Government (redundancies and delayed forest maintenance) in the first 12 months. In addition FPC meets $10 -$15m in forest related expenditure annually which will still need to be found should the FPC cease to operate and which is a real risk if the FPC is reduced to a "harvest only" position. This will leave the State without the capacity to address its future carbon liabilities. It will also have a major negative effect on regional industry and communities.

This investment is seen as critical.

The Agency will need to be "rebadged" to reflect its triple mandate.

Rationale

The FPC has operated as a hybrid Government Trading Enterprise expected to make a profit and return a dividend to Government. At the same time it has been expected to undertake community service obligations, largely unrecognised financially and has suffered externally imposed resource constraints that would not be accepted by a purely commercial entity.

Solutions have been suggested that the "commercial" elements of FPC's operations be separated out from the rest so it becomes a purely commercial entity. Community service obligations would be met by another entity or by paying the FPC to undertake them in a way open to competition. Under these conditions, its policy role would be shifted to another agency.

This establishes a three tier structure separating regulator, policy and commercial operation, weakening the policy function and leaving responsibly for community service obligations even less clearly defined than now.

The State has always been clear that Forestry should deliver on the "triple bottom line" of economic, social and environmental benefit (in keeping with Whole of Government policy generally); nothing in this review process has suggested anything other is expected. These three elements, however, do not always operate in synchrony and balance is required in order to optimise a collective outcome.

Consider the present organisational climate. There is no one agency with the responsibility to achieve this balance. The FPC is expected to operate commercially, and to play a role in industry development. DEC is expected to operate as a regulator and manager of environmental matters, the Conservation Commission has a clearly environmental agenda. Each element of the triple bottom line has its advocates for a focus on one element in particular. It is argued that where balance is required, it is unlikely to be achieved by these "disparate" elements operating separately – there must be a pivotal point where the achievement of this balance is the focus.

So it is with the various elements of forestry and what can be achieved utilising forestry. Salinity management is less likely to be on a farmers mind if he cannot also gain a commercial return on timber. If hardwood is required by industry, for example, there must be the milling capacity to manage it. Ensuring that capacity remains is a responsibility of government (or market failure results). If Carbon sequestration is only undertaken in higher or middle range rainfall areas it will compete with agriculture, and if the trees are not harvested – at least in part, there is no downstream industry or community development. Each element of what can be achieved by forestry is interdependent on at least one other element of forestry – again requiring co-ordination and balance.

Structure

- **A Statutory Authority:** As balance is critical, the management of the Agency should include people with skills and experience in the different elements of the agencies objectives. The agencies role will include the commercial and a board is appropriate. The agencies strategic planning should reflect its triple role. It may be argued that this will put the agency under tension. Of course, but if these tensions cannot be balanced within, where can they? The skills required for each element of the bottom line will be "represented" (achieved by selecting people with those skills – not as representatives of any interest groups).

- **A Department:** It is recommended the agency also be a Department under the Public Sector Management Act for purposes of employee management, including appointment of the chief executive officer. Presently the FPC, although expected to operate as a commercial entity, is not empowered to recompense its employees as would a commercial entity, whilst at the same time employees have no protection as would be the case if they were public sector employees.

This structure also offers:

- The governance for vesting/ownership and management of land,
- The governance for policy roles and control over direct appropriation from the consolidated fund,
- A balance in Board expertise with respect to the areas of focus of interest groups, and
- Portability of service for employees.

Recommendations:

1. It is recommended that Part 3, Section 10 of the *Forest Products Act 2000* be re-written and simplified so as to provide a more general statement of functions.

2. It is recommended that the Introduction to the Act spells out the "triple bottom line" objectives of the agency

3. It is recommended that all native hardwood forest that is not already gazetted or planned for gazettal as Reserves (with some exceptions) be vested in the Forest Products Commission, or its successor if Government owned, and defined as "working forest", to be used under conditions of environmental sustainability.

4. It is recommended the State remain an active participant in the planting of softwood plantations to ensure the continuing generation of new plantings

5. It is recommended the following be adopted as WA Government forestry policy:

   - Western Australia will continue to have a forestry industry.

   - This industry will consist of native hardwood (the quantity yet to be determined), plantations, sandalwood and a range of new physical and environmental products in line with the developing economy.

   - Carbon mitigation through sequestration/biomass is seen as important.

   - Forestry is one of the solutions to erosion control and salinity management.

   - Industry and community development and employment are important objectives of the industry.

   - The Government will continue in its goal to meet the triple bottom line objective – in the forestry industry – of economic, environmental and social well being.

6. It is recommended that as State Agreements expire, the Forest Products Commission adopts the market rate for its timber pricing policy

7. It is recommended the State Government continue to be an active participant in the production of forest products.

8. It is recommended that the FPC be encouraged to continue development of carbon offset plantations supported in both policy and mechanisms for capital raising. This will afford the opportunity to develop regional centres for not only carbon purposes, but for timber processing, energy generation and catchment and salinity management.

9. It is recommended the Forest Products Commission be recast as a statutory authority for its operations and as a Department under the Public Sector Management Act.

10. It is recommended the agency be re-badged to reflect its forestry obligations under the "triple bottom line of economic, environmental and social responsibility.

11. It is recommended that DTF examine the above impediments to the financial performance of the FPC and adjust them accordingly.

12. It is recommended the FPC Human Resources and Financial Support Services

currently conducted by DEC be passed to the FPC with the financial resources currently paid to DEC for this purpose.

13. It is recommended that any Future Forest Management Plans operate over 15 years, in three 5 year segments, with the FPC being given flexibility to harvest across each 5 year segment.

14. It is recommended that harvest contracts not be limited by the length of the Forest Management Plan

15. It is recommended that FPC be advanced $10m to maintain operational capacity in the lead up to the 2011 carbon planting.

Note: Appendices 2 and 3 of the Report provides comment on the recommendations of reviews of the FPC conducted in 2006 and 2007.

Introduction

The Forest Products Commission (FPC) was established in 2000 by the passing of the *Forest Products Act 2000.*

Since that time the agency has undergone considerable transformation and has been the subject of a number of reviews. In 2005 a Functional Review of the FPC was conducted and subsequently followed by a Legislative Review which was completed in November, 2006. As a consequence, legislative amendments were drafted; however, they were not introduced into parliament prior to the 2008 election.

Since the 2006 review there has also been international debate on carbon mitigation, carbon sequestration and carbon emissions as well as community and business discussion in relation to trading schemes, all of which carry major implications for the forestry industry.

Following the 2008 State election the incoming Government set out to re-evaluate the Forest Products Commission.

Using previous reviews as a cornerstone the Government wanted to reassess the FPC and its role as the lead forestry agency in Western Australia, in order to better understand and identify the options available for best practice management of the States timber resources and related matters (see Appendix 1 for terms of reference).

Recommendations from these earlier reviews are presented as Appendices 2 and 3. Note also that comments appear under each of these recommendations as they are impacted by the recommendations of the present review.

Contextual considerations

It is in the context of considerable uncertainty that this review occurs.

Recent events suggest it may be some time before there is much clarification concerning the "carbon debate", emissions trading scheme(s) or financial return (carbon credits) for carbon mitigation through bio-mass as fuel.

In recent months the blue gum industry has seen two major MIS companies collapse. The will and capacity of the commercial sector to contribute to the further development of the timber industry in WA, at least in the short to medium term, are in doubt.

The Forest Products Commission is contending with the impact of Government policy from 2001 which has prevented harvesting in old growth forest. Moreover, there are now greater limitations on material that can be removed from re-growth forests. The effect on the operations of the FPC has been further exacerbated by the Varanus Island gas explosion (2008), two major wildfires (2009) and current the global financial crisis.

These events have contributed significantly to uncertainty over the future importance/ practicality of the timber industry in WA. However, the potential critical importance of carbon suggests that whatever else, the capacity of the Forest Products Commission (as the Governments agent in these matters) to respond must be protected as insurance for the future, at least until these uncertainties are resolved.

Section 1

The Role of the State in Forests and Forest Products, The Need for Government to be a Supplier of Forest Products (wood included) to Industry, The States Appropriate Interest and Responsibilities in Plantation and Farm Forestry.

The *Forest Products Act 2000* Part 3, Section 10, comprehensively spells out the functions of the Forest Products Commission. Very extensive clauses cover Government policy advice, native forests, plantations, research, sustainability, silviculture, planting, maintaining and harvesting, contracts, industry development and inter-departmental liaison – in short, just about everything to do with the production and marketing of timber. These functions have been described as too prescriptive and may act, paradoxically, to limit the FPC's opportunities; for example, claiming intellectual property rights on research should the area covered by that research not be covered specifically in the Act.

At the time of this report, the State Government's goals are the successful (profitable and sustainable) harvesting of native forests and generation and sale of plantation timber and sandalwood.

The industry development aspect of the agency's operations can be seen in the development of the blue gum industry and the community development side through the number of people and locations involved in the direct and downstream activities of the industry

The environmental factors of carbon sequestration and salinity management did not figure largely or at all in the development of the legislation or the objects/role it was meant to underpin. The availability of native hardwood timber and the capacity or will of the private sector to participate are also key elements in any decision making process.

The question as to what should be the role of Government needs to be resolved before the nature of any underpinning legislation or organisational structure required to achieve them can be considered.

Whole of Government objectives

It is relevant to explore the role of the FPC in the light of the whole of Government goals set in 2009.

- **State building – major projects**
  Building strategic infrastructure that will create jobs and underpin Western Australia's economic development.

- **Financial and economic responsibility**
  Responsibly manage the state's finances through the efficient and effective delivery of services encouraging economic activity and reducing regulatory burdens on the private sector for the benefit of all Western Australians.

- **Stronger focus on the regions**
  Greater focus on service delivery, infrastructure investment and economic development to improve the overall quality of life in remote and regional areas.

- **Social and environmental responsibility**
  Ensuring that economic activity is managed in a socially and environmentally responsible manner for the long term benefit.

- **Outcome based service delivery.**
  Greater focus on achieving results in key service delivery areas.

Implications of the above

The above goals are intended to balance the economic, social and environmental responsibilities of Government.

Throughout this review discussion of the appropriate tasks and form of the Forest Products Commission is focused on achieving a balance between the commercial outcomes of the Commission, (including industry development), the achievement of good environmental outcomes (not just in forest management, but, for example, also in carbon, salinity and erosion management) and desirable social effects (including jobs and rural community support and development).

Recommendation:

It is recommended that Part 3, Section 10 of the *Forest Products Act 2000* be re-written and simplified so as to provide a more general statement of functions.

It is recommended that the introduction to the Act spells out the "triple bottom line" objectives of the agency.

This second recommendation is regarded as important. Legislation based on a clear statement of intent has less need to be "all-inclusive" in defining the tasks of the agency.

This review will develop the case for re-defining the role of the FPC so that it becomes an agency with a brief requiring it to utilize the skills of forestry across environmental, social and economic considerations. That role will require the balancing of competing interests and will need to be well understood.

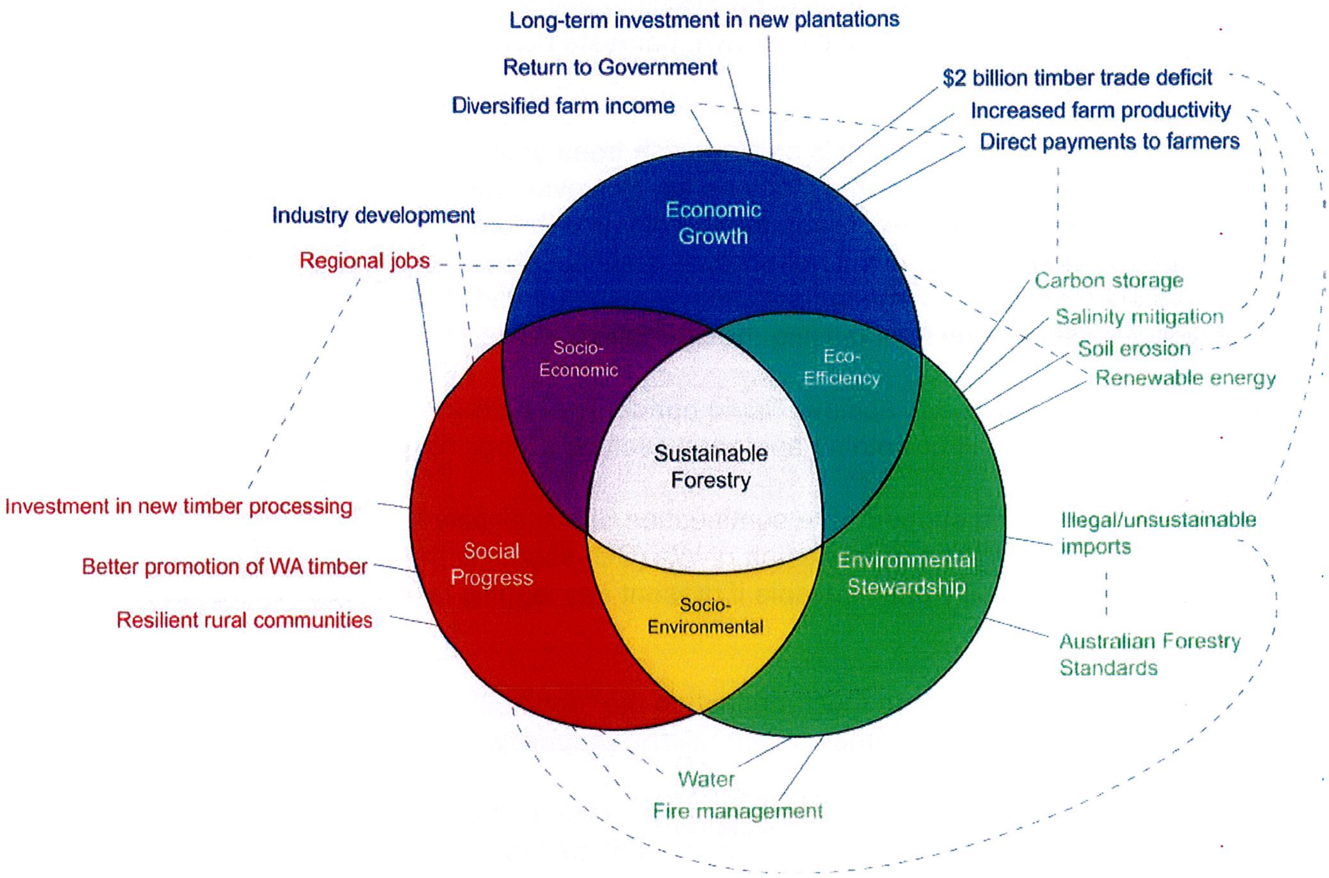

Figure 1: demonstrates the inter-linkages between the economic, environmental and social factors in the practice of forestry and the role of the Forest Products Commission

Native forests

Views on the native hardwood industry have often been focused on whether the industry should exist at all, or whether it should be a "boutique" industry, producing small quantities of quality hardwood for basically a local cottage industry.

This has been brought about largely as a result of the decision to cease harvesting of old growth forests and the subsequent further reduction of re-growth forest available to the industry.

In 1992 Western Australia signed up to a national initiative (National Forest Policy Statement) to declare a proportion of native hardwood as reserves for environmental protection purposes. Under this Agreement a proportion of the State's timber reserves was designated as "working forest", providing industry with some certainty in regard to the future availability of timber supplies.

What has happened since has been the erosion of that part of the "contract" which was perceived as belonging to the industry. Forests represent something from which Western Australians can gain an appreciation of the terrestrial environment, fauna and flora can be provided with natural habitat and protection and families/communities can enjoy them.

Forests also represent a resource which is available to Western Australians for access to good quality timber for furniture, building materials, jobs, communities and so on.

Important also is that native timber is of far greater value environmentally - in so far as carbon mitigation is concerned – if it is grown, harvested and re-grown than if it is merely left to age and eventually die.

(There is some conjecture about this point. Jarrah trees grow for some 300 to 400 years and continue to sequester carbon as they do so. However, this carbon is sequestered more slowly later in the life of the tree. Given that no old growth forest may now be logged, it is appropriate to consider re-growth forest, which is all that remains available. Here, should (re-growth) trees be grown for some optimal time, then harvested and re-planted, more carbon will be sequestered in total than leaving the one tree.)

There needs to be balance to achieve "triple bottom line" outcomes. - a strategy which does not rely on an extreme all-or-nothing approach such as all logging or no logging at all.

Whilst publicly declaring support for a continuation of sustainable logging of native hardwood, the Conservation Commission of WA (CC) seems to behave in a way which makes future sustainability unachievable if present day logging targets are to be used in the future.

In actual fact, the CC places so much priority on the "don't cut down trees" side of the debate that "lack of sustainability" becomes a self-fulfilling prophesy.

The Victorian Government clearly determined that a line in the sand had to be drawn when it separated forests for conservation from those nominated for harvesting and renewal.

The Victorian "Draft Timber Industry Strategy" faces a more critical drop in available and sustainable native hardwood than Western Australia. It has, however, reacted by endorsing the continuation of native hardwood forestry and has established "working forests" to be managed commercially and environmentally, calling for an increased flexibility with which VicForests can operate.

Should the Western Australian Government make the decision to follow suit, then, operating with caution, there will be the capacity to sustain a long term native hardwood industry – complemented by environmental, community and economic benefits.

In an environmental context the Conservation Council and other interest groups have asserted that Western Australia's native forests have not been well managed over the past century and as a result are now in a vulnerable state.

It is the case that current forest conditions reflect the influence of past management practices; however, it is not true that careful management of the forests cannot sustain a native timber industry – albeit one perhaps somewhat reduced in size. It is considered the FPC has the will and capacity to do this, and that the future of forestry in WA will require the continuation of a capacity to mill hardwood.

This review will recommend that all native hardwood forest not already gazetted or planned for gazettal as Reserve (with some exceptions) be vested in the FPC, and defined as "working forest", to be used under conditions of environmental sustainability. If there are areas of "difficulty" in this, commonsense negotiation under expert mediation should be able to achieve a sensible resolution.

This situation then becomes analogous to that of the Fisheries Department, where operations in the open ocean are conducted – by Fisheries – in an environmentally sustainable manner, with marine parks and reserves under control of the Marine Parks and Reserves Authority (MPRA) and Department of Conservation and the Environment (DEC).

Presently Gunns and Whittakers are taking steps to restructure their WA milling business to cope with the very tight financial position current in the industry. These companies contribute to the economy of Western Australia significantly and their mills have the capacity to support future hardwood plantations.

These facilities, under whatever future ownership, are important to the future of any Western Australian attempt to maximize the value of timber.

Ensuring a supply of native hardwood by securing "working forest" will provide economic benefit to the state now, whilst leaving open the prospect of far greater future benefit (from plantation timber produced, at least in part, for milling).

To judge the financial return on native timber only on the "profit" or otherwise of the FPC is missing most of the point. The native hardwood industry as a whole provides significant economic and social benefits to Western Australia.

As will be illustrated later, it is also true that much of the "profit" that would be achieved by the FPC is in fact used for unfunded environmental management.

Table 1: Areas covered by reserves and state forest.

Forest Regions	Existing Reserves		Proposed Reserves		State forest[*1]					
						Areas where timber harvesting is not permitted[*3]			Net area available for harvesting	
	Total area[*2]	Old-growth forest	Total area[*2]	Old-growth forest	Total area[*2]	Informal reserves	FHZ	Old-growth forest[*4]	Total	Native forest
Swan	217,730	7,250	93,740	6,820	432,300	57,150	21,960	2,480	355,460	288,190
South West	200,790	45,400	70,830	10,900	535,700	73,560	30,310	5,240	432,730	374,930
Warren	649,130	232,720	35,540	8,080	264,870	55,760	10,580	20,320	187,390	184,610
Total	1,067,650	285,370	200,110	25,800	1,232,870	186,470	62,850	28,040	975,580	847,730

As can be seen from Table 1 above, the total area of existing reserve is 1,067,650 hectares. Reserves proposed but not yet gazetted amount to 200,110ha including 25,800ha of old growth forest.

Much of the proposed new reserve is either old growth, located in the eastern forest zone, required for habitat, or included as a result of public pressure. It is estimated, however, that approximately 50,000 hectares are free from these constraints and should be added to the area to be vested in the Forest Products Commission as above, with expert mediation utilised in the event of disagreement. (Note that when areas of old growth forest were set aside from any future logging, a considerable area set aside actually contained large areas of re-growth forest).

This would mean having approximately 1.2million ha of forest reserved and 1.025million ha available for harvesting. To separate the forest into reserve and working forest would meet the intent of the 1992 National Forest Policy Statement in a manner which is appropriate and clarifies responsibilities for forest management.

It is important to note that State Forest is reserved for production values, specified in Section 55(1)(a) of the CALM Act. Today, significant uses of State Forest include mining, water production, timber, and recreation as well as conservation. Vesting in and management of the State Forest by the FPC is entirely appropriate given that the FPC can pursue economic and social objectives in balance with the required environmental values.

Management of land vested in the FPC

State Forests are largely managed by DEC. Whilst there have been continuing disputes between the FPC and DEC surrounding a Memorandum of Understanding as to what is being done and how it is paid for, there is nevertheless a need for coordinated management practices within the forests.

Reference is made elsewhere to a coordinated response to fire, but there are other arrangements for management of weed control, fire suppression, and so on. Should the FPC simply take over these responsibilities in areas vested in them, then there is a risk of duplication.

This is manageable either by a continuing agreement between the two agencies, or by formulating an agreed plan and proper accountability for work undertaken, but affording the FPC the opportunity to carry out its own work where this is not duplicative or administratively clumsy.

A further possibility is to place responsibility for all forest management including reserves under the FPC, to be managed by the one agency. DEC has an environmental but not commercial role. The FPC has both, so is arguably better able to work in an "environmental" reserve than is DEC in a working forest.

An added advantage is that DEC would not receive payment from the FPC for work undertaken in commercial forests and the negative perceptions which such payments induce in the public mind.

Plantations

The blue gum industry owes its genesis in Western Australia to the FPC and its predecessor, the Department of Conservation and Land Management (CALM). The fact that two major blue gum corporations are facing receivership is not the fault of the FPC. In fact, it was the precision and accuracy of FPC modeling which revealed that the quantity of blue gum harvested would be far less than corporate predictions.

The FPC describes the sandalwood industry as analogous to blue gum in that it is a "work in progress" on the way to development of a commercial industry such as is being stimulated in the Kimberley.

One of the oft cited reasons for Government to play a role in the market is when the market is failing or when it is in danger of doing so – another is to create a market in the first place to establish essential or desirable industry.

In the case of timber production, lead times are very long and few Companies have the desire to wait so long for returns. The Victorian Government, for example, found no difficulty in finding a buyer for its stake in softwood plantations. However, it is in the generation of new plantings where private enterprise is less forthcoming and in Victoria there is actually very little by way of new plantation plantings.

In 2008, the total planted area of softwood in Victoria (all corporate or privately owned) was 219,910 hectares, the largest of any jurisdiction other than New South Wales (WA 109,158ha).

By comparison, in 2008, new softwood plantations in Victoria totaled only 484 hectares amounting to 0.2% replacement – about one sixth of Western Australia, (2,496 ha).

One consistent feature of forestry within Australian Government jurisdictions is that reduction of their stake in forestry has led to an industry that has suffered consequently and which now returns less benefit economically, environmentally and socially.

For reasons stated above, removal of plantations completely from State ownership carries too many risks. If it is possible to sell WA's plantations at a fair price and if the Victorian experience is anything to go by, it will be necessary for the State to reinvest that income into planting new plantations.

The purpose of plantations

Initially, plantations were seen primarily as a source of timber, both soft and hardwood, for the typical uses of furniture/building materials, etc. More recently, plantations are being considered for carbon sequestration or for use as fuel (bio-mass).

However, commercially it is more efficient for companies to grow timber in high rainfall areas with good soil; in short, on the best farm land in demand for agricultural purposes.

A senior executive within a large public company looking to invest in plantings for carbon in WA made the following observation:

"A company might go to the private sector to plant plantations as a way to address its "carbon debt". This would result in the planting of trees mainly in large blocks not for harvest. However, it would not "value add" in any secondary way. Not being for future harvest, no downstream industry or rural community would benefit. Plantings would be in the "best" (agricultural) areas and not used in conjunction with addressing salinity concerns for example.

None of the profits accrued by the plantation industry would be available for government to use in environmental management or conservation of its parks and reserves.

Many companies emitting carbon wish to be good corporate citizens. As part of the process of addressing their carbon responsibilities they would, in addition, like to address "secondary" considerations such as those mentioned, at least with a part of their mitigation program."

The same executive also made the observation that if the "carbon economy" becomes anything like the size predicted, there will be a huge space for companies to grow into. The need will mean there is more than enough room for the participation of government and the commercial sector alike; in fact the presence of both will be required.

The participation of Government also provides a check against which claims can be judged and offers a measure of security for participating companies.

Government owned enterprises such as Verve and Synergy have their own emission challenges. The predicted liability under the Carbon Pollution Reduction Scheme is 10 million tonnes per annum at a cost of $100 to $200 million per annum or more (it has been suggested the carbon debt could be as high as $500million) depending on the carbon market price.

Options for addressing them include paying the Commonwealth for credits (and increasing electricity charges, or at a cost to the state but no benefit), to employ private enterprise to plant and manage on their behalf (still at a cost to the state but with the benefit of tree planting for the environment) or to purchase the same service from the state, via the Forest Products Commission (in which case all benefits flow to the state).

These plantations can be established where secondary benefits are available as above. Land that should never have been used for agriculture could be planted with trees so as to restore it to health – in areas no purely commercial carbon company would consider.

This is an example of where there would be no market without Government participation.

Farm forestry can be seen as a part of this, in restoring land that has been damaged by erosion or salinity, and in doing so earning carbon credits or generating income through wood sales.

Farm forestry has not been taken up wholeheartedly by farmers for investment purposes as it is not always profitable for its own sake and is not of particular interest to public companies, However, farm forestry has major benefits if both the commercial income and secondary benefits are considered.

In addition, if farm forestry was to become a major commercial exercise, then it would need to be undertaken across many farms in a coordinated fashion so as to address issues such as distance from mills, available local infrastructure and so on. Government is considered the most likely catalyst for making this happen.

Recommendation:

It is recommended that all native hardwood forest that is not already gazetted or planned for gazettal as Reserves (with some exceptions) be vested in the Forest Products Commission, or its successor if Government owned, and defined as "working forest", to be used under conditions of environmental sustainability.

It is recommended the State remain an active participant in the planting of softwood plantations to ensure the continuing generation of new plantings

It is recommended the following be adopted as WA Government forestry policy:

1. Western Australia will continue to have a forestry industry.
2. This industry will consist of native hardwood (the quantity yet to be determined), plantations, sandalwood and a range of new physical and environmental products in line with the developing carbon economy.
3. Carbon mitigation through sequestration/biomass is seen as important.

4. Forestry is seen as one of the solutions to erosion control and salinity management.

5. Regional industry and community development and employment are important objectives of the industry.

6. The Government will continue in its goal to meet the triple bottom line objective – in the forestry industry – of economic, environmental and social well being.

Forestry Policy

An examination of the Whole of Government Objectives in Part 1 and the recommended Forestry Policy above demonstrates a great deal of symmetry.

Given the multiple opportunities forestry represents to the people of Western Australia and the complex issues in meeting the triple bottom line, the FPC is ideally placed to manage the State's forestry agenda. In fact, it is the only agency in the position to do so. The mandate represented by the suggested policy statement is critical to the successful achievement of the multiple agendas in the industry.

Section 2

The States Role in Encouraging and Regulating Private Sector Investment in commercial tree crops for the accrual of social, environmental and economic benefits. The Appropriate Policy Regulatory and Institutional Arrangements to Support Sustainable and Developing Forest Products Industries. The State's national and international obligations with regard to forests and plantations.

Australia is a signatory to international conventions for a range of issues, including biological diversity and ecologically sustainable development. These are operationalised through vehicles such as the Montreal Process Criteria and Indicators for Sustainable Forest Management and the commitment of all jurisdictions to the Australian National Forest Policy Statement.

The FPC draws two key elements from these national and international obligations:

- The first element is the management (particularly of natural forests) in line with principles of Ecologically Sustainable Forest Management (ESFM as it is known), which is explicitly contained in the *Forest Products Act 2000* (s12(2)) and requires a long and short-term outlook on economic, environmental, social and equitable considerations.
- The second element is the national targets set for plantations in the national "Vision 2020". All jurisdictions including Western Australia, signed up in 1997 for a target of trebling the national plantation estate by 2020 (to three million hectares). The initiative was aimed at helping to address Australia's balance of trade deficit in forest products as well as developing sustainable industry in rural areas. Accounts from the National Plantation Inventory show the estate is now nearly two million hectares, but an additional one million hectares is required over the next decade.

The states role in timber has been addressed in SECTION 1. The international situation is that the world generally (and Western Australia in particular) faces a timber shortage which has been buffered by use of timber from Asian and other native forests on a non-sustainable and non-replacement basis. These supplies will not be available for much longer.

In Western Australia the native hardwood industry has been markedly reduced and unless something is done to guarantee continuing access to re-growth forests (what is not yet gazetted reserve) it will be difficult for it to survive as more than a cottage industry.

However, the native forest "industry" can survive and make positive changes if impediments to its successful operations are reduced. Presently the FPC is hamstrung by the processes through which it is supplied timber, which are needlessly restrictive and bureaucratic.

In its submission to this Review the FPC made four recommendations related to investment. These were:

- Re-invigorate the native forest industry by developing an agreed mechanism to deliver certainty for investment over contract terms beyond the periodic management plans. This industry would have a balance of saw logs, other wood fibre products and renewable energy fuel supply.
- A mandate for plantation development based on regional hubs for timber processing and

energy, with carbon offsets and salinity management delivered to the surrounding region

- Legislated powers to pursue commercial arrangements to secure necessary investment.
- Raising capital investment directly or in alliance with other State trading entities for the transition period prior to a fully functional carbon trading market.

The Review endorses each of these recommendations.

In addition to this the state has pressing needs in the areas of salinity, a potentially huge Carbon "debt", the energy industry faces a huge liability, a great need exists for renewable energy and so on.

The State, through the FPC, has established a blue gum industry, now with exports of around three million tonnes per annum.

The State Salinity Strategy and National Land and Water Resources Audit estimated that of the 18 million hectares of land in the states agricultural zone, approximately 3 million hectares will become saline within our lifetime.

In order to address the requirements of renewable energy, salinity management and carbon mitigation over the next 15 years, the FPC estimates the forest products industry will need to be trebled.

As stated above, this creates a huge market space for the private (and public) sector to grow into.

The question becomes how to stimulate investment or entice new players to the industry?

Industry development and investment

One aspect of the softwood plantation industry that needs to change is the way in which prices have been set (state agreements) in the softwood plantation industry. Initially, prices were set low in order to entice companies into the industry for the purpose of milling timber for sale to downstream processors in furniture/building, etc. This was effective for that market segment, but had the undesirable effect of keeping potential plantation developers out of the market. Investors could not invest with confidence given the artificially low prices charged by Government. As agreements lapse prices should be set by normal "market forces".

Recommendation:

It is recommended that as State Agreements expire, the Forest Products Commission adopts the market rate for its timber pricing policy, consistent with other settings to attract investment.

Victoria sold its plantations to stimulate the private sector at what was regarded by Government as a fair price, with a view to stimulating the private sector. However, as stated elsewhere, there has been far less subsequent development than hoped. The issue of investing now for a return in 30 years has continued to act as a deterrent to large investors.

The FPC has discussed sale of its own plantation stock with potential investors, but found that investors were only interested in maturing plantations at a price very advantageous to themselves, meaning an unsatisfactory return to the Forest Products Commission.

"Carbon Conscious" has recently announced the signing of a contract to plant trees in medium rainfall areas on behalf of Origin Energy for the purpose of creating a carbon sink.

Should it achieve its target this will be the largest program of its kind in Australia.

Synergy entered into a contract worth $25million with the FPC in 2008 for the same reasons. The FPC and other forestry companies are currently negotiating similar contracts, and conducting due diligence studies.

The above indicates that a market is developing; however, this market is not yet mature and it is patchy in the products it produces.

The market currently needs State and Territory Governments to continue participating as suppliers. Potentially, it will be vast enough to require very many players with some companies wishing to enter the market through Government for the purposes of deriving secondary benefits for the community. Therefore, Government will need to stay in the market for many years to come. There is also a safety factor in Government having the expertise and long term presence in such an important market. With that in mind, the FPC has considerable expertise.

At this stage the carbon market is in its infancy and the growing of timber for biomass is embryonic. There are too many "ifs" for Government not to be a participant as a producer/ researcher and adopt a stimulation role from within, not simply act as a regulator.

Recommendation:

It is recommended the State Government continue to be an active participant in the production of forest products.

Attracting investment

The stimulation of investment at a time of uncertainty and with some of the constraints mentioned above is problematic; however, there are strategies that will improve opportunities.

Doubt exists in relation to a number of National and State policy settings. Clarification of the use of biomass resulting from native forest harvesting residues and the treatment of forest residues in relation to the Federal Government's Renewable Energy Target and clarification of the State Governments policy will assist in stimulating greater investment.

The nexus between native forest log contracts and the Forest Management Plan must be broken if there is to be increased investment in native forest and a continuing milling industry.

The Government of WA might also consider making the investment environment more positive by contributing financially. For example, in the past, State Governments have supported investment through State Agreement Acts which provide resource security and infrastructure support. Security guarantees have also been used to directly target perceived investment risk.

Tasmania has adopted a model that has been proactive in developing two major investment-ready forest industry nodes, including one where a variety of end-use industries are integrated into one location maximizing merchandising and transport efficiencies. These "wood centres" are developed using public/private investment and form a financially viable (and equitable) example of Government support of industry.

Recommendation

It is recommended that the FPC be encouraged to continue development of carbon offset plantations supported in both policy and mechanisms for capital raising. This will afford the opportunity to develop regional centres for not only carbon purposes, but for timber processing, energy generation and catchment and salinity management.

Section 3

The success of FPC in implementing the objectives of the *Forest Products Act 2000*;

The primary objective of the FPC was conceived as to maximise the State's return on forest products from south-west native forests. In its original concept the FPC would not have a role within the forests other than the selling of the produce to private enterprise, setting prices and providing ministerial advice. The Minister for Forests would have an equal say to that of the Minister for the Environment insofar as the extent of the harvest, but the then Department for Conservation and Land Management would be responsible for all matters of forest management.

Subsequently, the mandate was extended (prior to the Bill being tabled) to include a range of other functions, including plantations, research, ministerial advice on forestry, nurseries, propagation, silviculture, share-farming, industry and technological development, and others.

With the continuing importance of salinity management and the growing carbon debate, the FPC began to take on greater responsibility for tasks of a community service obligation (CSO) nature. The Statutory Review of the *Forests Products Act 2000* (November 2006) describes the FPC as "not a textbook Government Trading Enterprise" in that it is required to take into account not only commercial, but also social and environmental considerations. The Review highlighted that the "triple bottom line" programs provided employment but also environmental advantages. Given the balancing required, the FPC was certain to attract criticism from those with differing views of priority.

The FPC has increased its involvement in these activities since the Review was completed.

The 2006 Review also notes that the FPC had not achieved the commercial results that were expected of it, a situation which has not changed.

However, as the 2006 review and earlier Functional Review of the FPC (2005) noted, there were very good reasons for this and they are no less valid today.

The first cause of this was the "Protecting Our Old Growth Forest" policy and the 2004 – 2013 Forest Management Plan, which drastically reduced the availability of timber (as well as its quality) to the FPC. This had a major impact on the "profitability" of the FPC and an immediate and continuing major detrimental effect on the forest industry as a whole.

The role of the Minister for Forests was also weakened by removing his concurrence powers for the Management Plan. The Minister for the Environment now has these powers unilaterally.

However, apart from the reduced income from native hardwood, the FPC has had successes in meeting the Governments agenda.

The 2006 Review points to success in the development of new plantations. The FPC received strong support as the Government lead agency with policy and strategic responsibilities.

In fact, the development of the blue gum industry owes much to the initiative of the FPC and is a case of both community and industry development. The FPC sees its role in the development of the sandalwood industry in the same light, this being a "work in progress".

The agency has national accreditation as a forestry manager (Australian Forestry Standard and the ISO 14001 Environmental Management System). The CC and DEC both expressed the view that in the past the FPC was deficient in some of its management practices. However, the DEC, which is responsible for the day-to-day monitoring of the FPC forest practices no longer views the FPC as a deficient environmental manager.

That the FPC carries out its policy/Government advisory role satisfactorily is evident in that the 2006 Review saw no reason to change the Commissions functions in this regard.

In fact, both reviews referred to above treated the FPC "kindly" as did the large majority of those providing comment.

The same is true of feedback received throughout this current review.

Many issues were addressed by commentators; however the predominant theme was how to further assist the FPC by making its mission clearer, removing impediments confronting it and so on.

These difficulties will be addressed later; however, the evidence is that the FPC has performed very well in terms of achieving objectives set for it, particularly given the impediments with which it has had to deal.

Independent evidence

The Reviewer was given a copy of a Due Diligence/Integrity report carried out by a very reputable consulting group with expertise in forestry. The report was prepared this year for a major Company operating in the petroleum industry and examining options to cover its carbon "debt". Details were provided in strict confidence and no identifying information can be revealed.

The review was very positive in its appraisal of the Forest Products Commission. Direct quotes from the Reports summary include:

"FPC is an outstanding forestry organisation highly capable of establishing, maintaining and monitoring substantial ....plantations for the necessary decades."

(The reporter) "highly recommends the FPC to" (the company).

The report also noted that the FPC was the only potential provider (of carbon credits) to factor climate change into their yield expectations. The factoring in of climate change in forest management in native and plantation forestry is of major importance to environmentalists and industry alike.

Section 4

Whether the *Forest Products Act 2000* and the Commission is the best way of achieving the State's medium and long-term goals.

The forestry industry is in a state of uncertainty. The future with respect to carbon is likely to see an increase in the value attached to trees although this has been delayed. Investment in the timber industry has not been easy to obtain, and will suffer further from the recent corporate collapses. In its modelling the FPC accurately predicted the two companies involved would not obtain the timber targets they had "advertised". Alarmingly, the Commission has significant doubts as to the amount of carbon sequestration likely to result from tree plantings compared to that which commercial operators are suggesting.

If the Government does not stay involved in the timber industry, at least for the present, it risks not having the capacity to address its likely ten million tonne annual emissions costs. This is without even considering the value of the current industry to the state for building, furniture, biomass, salinity management and so on.

In other words, Government has too much to lose by "exiting" the business.

Forestry models

Each Australian State and Territory has a model for forestry that is different from all the others. They differ in terms of the nature of timber harvested, whether it is native or plantation, in the nature of the organisation, the nature of regulation, the degree of Government involvement in the agency, pricing policies and so on. Each structural alternative has its pros and cons. The one thing they do have in common is they have all undergone significant change over the past decade or so.

Current situation

- Forestry Plantations Queensland manages commercial plantations, including native hoop pine plantations.
- Commercial native hardwood forests in Queensland are managed by the Department of Environment and Resource Management.
- Under the South East Queensland Forest Agreement, 1.2 million hectares of native forests are being gradually removed from commercial use between 1999 and 2024.
- In all other Australian jurisdictions, public commercial forestry is overseen by a single Government business enterprise.
- In Victoria, previously public softwood plantations are now privately owned and managed

Table 2: Forest management by jurisdiction

Jurisdiction	Agency	Type	Segment	Description	Financial (2007/08)	Governance
South Australia	ForestrySA (South Australian Forestry Corporation)	Corporation	Plantations	Trees and land Regional industry Research Fire control	$120 million revenue $30 million NPAT $43 million adjusted EBITDA $34 million dividend & TER $3 million CSO - formal schedule – includes fire, reserve management 26% debt / revenue	Five member Board
	PIRSA (Department of Primary Industries and Resources)	Department	Policy	15-17 staff Policy Forest health Extension, regional plantation committees	—	—
	Department of Environment and Heritage	Department	Native forest	No native timber production in South Australia	—	—
Tasmania	Forestry Tasmania	GBE	Native forest and plantations	Trees and land Recreation sites Fire control Non-commercial functions funded from revenue, not CSO	$150 million revenue - $38 million NPAT (loss) $18 million adjusted EBITDA $0 million dividend & TER $0 million CSO 34% debt / revenue	Six member Board
	Forest Practices Authority	Statutory Authority	Regulation		—	—
	National Parks and Wildlife	Department	Parks	Responsible only for Parks, not State forest	—	—
	Policy Unit in Department of Infrastructure, Energy and Resources	Department	Policy	Reports to Minister	—	—

Jurisdiction	Agency	Type	Segment	Description	Financial (2007/08)	Governance
New South Wales	Forests NSW	Public Trading Enterprise within the Department of Primary Industries	Native forest and plantations	Timber and lands Recreation & conservation Environmental services (in and outside NSW) Separate funding for CSOs	\$290 million revenue \$117 million NPAT \$53 million adjusted EBITDA \$0 million dividend & TER \$10 million CSO 58% debt / revenue	No Board – Chief Executive reports to Director General
	Department of Environment and Conservation	Department	Regulation	Park management Harvesting practices	—	—
Queensland	Forestry Plantations Queensland	State-owned enterprise	Plantations only (incl. native hoop pine plantations)	200,000 ha plantations Full powers over land CSOs via schedule Separated from DPI on 1 May 2006	2008 figures not available	Two ministers as shareholders Five member Advisory Board
	Department of Environment and Resource Management	Department	Land management (native forests) Native forest commercial operations (phasing out by 2024) Regulation	Codes of practice Licensing Nature conservation	—	—

Jurisdiction	Agency	Type	Segment	Description	Financial (2007/08)	Governance
Victoria	VicForests	State-owned enterprise	Native forest	Sale of timber Regeneration Development of high value timber and uses Community appreciation of value of native hardwood May deal in land, but does not hold State forest CSOs can be reimbursed	\$125 million revenue \$1 million NPAT \$2 million adjusted EBITDA \$0 million dividend & TER 5% debt / revenue	Four to nine directors (currently six) Accountable to Minister for Agriculture
			Plantations	Have been privatised and sold completely		
	Department of Sustainability and Environment	Department	Public land	All forest values (continues to manage timber in some areas)	—	—
Western Australia	Forest Products Commission	Statutory Authority	Native forest and plantations	Timber sales Unclear land	\$116 million revenue \$6 million NPAT \$10 million adjusted EBITDA \$5 million dividend & TER \$2.4 million CSO 81% debt / revenue	Board of seven Commissioners
	Department of Environment and Conservation	Department	Land management Regulation	Conservation, recreation Fire control Planning	—	—

Note:

- the variability in institutional arrangements between jurisdictions;
- the high debt / revenue ratio of FPC compared with other entities; and
- that in 2008 very little was paid by way of dividends, tax equivalents in any of the State commercial forestry entities.

Research data

Nelson and Nikolakis, of the University of British Colombia (Dec 2008) completed a review of State owned forest agencies in Australia, with particular reference to corporatisation and performance and looked at the question of might there be an optimal form.

The review traces Australian forestry history from the signing of the National Forest Policy Statement in 1992, including the signing of 10 Regional Forest Agreements throughout Australia – designed to provide certainty to the forest products sector in each state.

It then addresses the political, ideological and budgetary forces leading to the transformation of the public forestry sector within the context of National Competition Policy.

The above table outlines the current structures of state agencies, which resulted from the restructuring exercise undertaken in each jurisdiction.

While three States chose an explicit corporate form, the remaining three States opted for a Government Business Enterprise, but with other dissimilarities within. Different approaches were also taken to regulation. The issue of retaining native forest management along with plantations was also managed differently.

The conclusions reached by the authors were interesting, but not altogether informative – other than to suggest that more research is needed before any firm statements can be made about optimal organisational design.

Corporatisation did appear to have an improving effect on performance, but this was not explainable in terms of agencies merely behaving more like corporate bodies.

The study identified a Board of Directors as appearing to be critical to performance.

The study also found that the greater the degree of separation from government, the greater the improvement in performance. The possible reason was expressed as "We hypothesise that this is linked to a greater flexibility and ability to focus on the commercial aspects of carrying out economic activities, including the ability to make strategic decisions around issues that were perhaps too political or where there was not sufficient organisational focus to implement more significant changes (such as timber pricing)."

This conclusion tells only part of the story. One would expect that an agency making purely commercial decisions would be more profitable and efficient given no additional (CSO) responsibilities for which it is not funded, and the further removed from Government, the more likely is it to have a Board of Directors.

The study acknowledges earlier on that other activities of an agency (meeting the triple bottom line) will also have an effect but does not refer to it in its conclusions, other than stating "purely commercial decisions" are more profitable.

Agencies operating further from Government are less likely to need to factor Community Service Obligations into their equation – so of course they will seem more profitable and efficient. This is only natural.

There is nothing wrong with the conclusion that the more commercial entity is more profitable and efficient. However, the context must be taken into account. Government must consider the importance of community service obligations and who should manage them. It would seem sensible that if CSOs involve forestry, it is best to get foresters to manage them.

The question, "What does the Government want from its agency?" is the important one.

If the agency is to have a broader focus than the purely commercial, then the nature of its construction need not (and probably should not) be purely corporate.

Rather, the agency must have the capacity to operate commercially within the context of that broader agenda.

Understanding the above is important in considering the alternatives for managing the WA forestry industry. Basically, there is as yet no answer to the question of what is the ideal structure.

Possible alternative structures

A GTE Structure

A Forestry GTE could assume a number of forms and undertake a variety of tasks. Set out below are two possible scenarios.

The FPC is supposed to operate as a GTE that returns a dividend to government from its operations (which include things no commercial agency would normally do without recompense).

It has been given "ownership" of the trees, at least insofar as the debt associated with them is concerned. It has not been granted "ownership" of land still held by the CC and managed by DEC.

In fact, the trees and the land belong to the state, and could be vested anywhere. The FPC does not need to own either, but could operate as a manager on behalf of Government.

In this model all land used in the Governments timber operations and what is on it could be vested in other than the FPC (but not within DEC) and the associated debt be held by the Department of Treasury and Finance (DTF).

The Government then contracts with the FPC to undertake its timber operations at an agreed commercial price. These operations may include planting, clearing, selling etc as is the case currently. In addition, the FPC could be funded by Government to purchase or lease land for use by Government for its timber initiatives

Also included can be tree planting for salinity, carbon or other purposes, scientific research, industry development and anything that might be a CSO, properly costed and accounted for separately.

These contracts can be contestable, as for any other tender or business arrangement. In turn, the FPC may manage its own HR/Finance functions or purchase them from elsewhere. It would also purchase from DEC such services within the forest as are required – if any, with protection built in for bushfire management, but in a way allowing FPC to directly sub-contract for road works, clearing etc.

The manner in which DEC and FPC interact and their mutual obligations have been issues since the creation of the FPC. DEC argues that it must retain all staff positions currently on the establishment, including those who perform work on the FPC's behalf, in order to have a sufficient workforce to combat fire and so on.

To some extent this is true. However, FPC officers act as fire controllers and play their role in fire management now. If DEC staff (or the equivalent number of them) working on "FPC land" were transferred to the FPC, it is difficult to see why they could not work in a coordinated fashion with DEC staff when needed in times of fire, etc.

This would seem to obviate the need for a forest management contract as complex as currently between DEC and the FPC – or at least reduce the dependency of FPC on DEC. FPC becomes its own master (subject to meeting reasonable environmental standards) and can address what it sees as its own priorities – and at a cost substantially less than they are presently charged by DEC.

Another "service" that could be purchased from the FPC by Government is advice, given that the FPC has the best expertise/information available. However, as the FPC is a commercial entity, there is conflict in it also being a policy advisor to Government.

Given this, there may be an imperative to establish a "policy office" somewhere else in Government. Possibilities include the Department of Premier and Cabinet, a related mainstream department such as Agriculture or Water or under the Minister with responsibilities for GTEs – unless the same decision is taken as in the Legislative review of 2006.

It should be said, however, that whatever form the FPC takes, it is the view of this review that it will need to grow. Therefore, should it be purely commercial, the situation will not be as it was in 2006 at the time recommendations were made following the Legislative Review.

A second GTE option

The above option has the FPC as a commercial manager of forestry matters, but with no property ownership (other than the equipment it needs to do its job).

A second scenario could see the FPC as a land owner, expected to return a dividend to Government as now, with all "CSOs" managed as above. Debt is still an issue but could be held directly by DTF rather than against the FPC.

One of the issues facing the FPC is that of how to assess return on investment. The valuation assigned to forests for future harvesting is volatile and there is uncertainty as to how to value something over a timeframe of many decades. This distorts the return against assets of the Commission.

Assessing the Commissions performance is not assisted by taking the debt and assessed value of the timber into account, given that the "true" value of the timber is unclear.

FPC as a forest "owner"

Presently the FPC waits for a "handout" from the CC/DEC for timber to harvest over the 10 years of the FMP. This amount is gradually being whittled down and as stated elsewhere DEC supervises and manages a long, drawn out approvals and control process.

If one takes an analogy from the fishing industry DEC is involved in the management of marine parks, but is not a day-to-day manager of the rest of the ocean, even though there are environmental standards to be met.

If a similar structure was to be applied to forestry, DEC would take responsibility for reserves and the FPC for state forests. DEC could still have an environmental standards role. Primary responsibility for all land containing plantations or re-growth forests would pass to the FPC. Such an arrangement could provide a management service for DEC in reserves, and further solve a number of problems associated with two agencies operating in adjoining or the same forests.

This is a great deal simpler to manage and does not prevent other activities such as ecotourism happening on what becomes FPC land.

DEC and the Conservation Commission of WA have criticized FPC previously for lapses in environmental management; however, DEC advises that this is not considered a current issue.

The FPC may have taken time to settle in as a new agency, particularly given the rough ride it had in its first few years.

The situation now, however, is that the FPC is nationally accredited as a forest manager and at a higher standard than required by DEC. Given its reliance in part on native forests, it has every motivation it needs to manage these forests sustainably and with all due environmental care. Those areas within FPC controlled forests requiring environmental protection for fauna and flora can be managed by FPC to meet DEC environmental standards.

Categorising re-growth forest as for harvesting (FPC) and old growth and reserve forests for conservation purposes (DEC) also makes the Governments position very clear about the commercial – as well as the environmental – importance of forests.

Alternatives to GTEs

The Legislative Review of the FPC in 2006 recommended that should the FPC remain as a GTE then it should function more like a GTE than the hybrid it is now.

An issue, however, is that a GTE further removed from Government would be less able to focus on the "triple bottom line", even with separately accounted for contracts/CSOs etc. A policy body elsewhere splits the advice available to Government on forestry – but also on how to coordinate the triple bottom line outcomes.

A Separate GTE might also cause complexities in the vesting of state property.

There are a number of disadvantages in a GTE format that can actually impede achievement of its multiple objectives. The "commercial imperative" does not sit well alongside the other obligations whilst it remains the major focus and generates criticism from interest groups.

A Forestry Department or Statutory Authority that is also a Department

A Forestry Department would have the capacity to integrate the three elements of the bottom line, but would need to find a way to manage its commercial responsibilities.

To raise a possible return to a "forestry department" probably seems counter-productive, given the readiness with which Governments have welcomed privatisation and corporatisation (GTEs). However, the nature of the organisation required depends very much on the job one wants it to do. There have been failures in corporatisation that reflect a miss-match between what is required and the decision to corporatise as a way of achieving it.

The FPC undertakes many community services functions on behalf of Government. Should the agency be removed further from Government by becoming a "full" GTE (see the Nelson/ Nikolakis paper above) then some vehicle will need to be found in order to meet these obligations or the corporate entity, or some other, will need to be paid to undertake them on Governments behalf. A Government Department, funded from consolidated revenue, can be tasked specifically to undertake CSOs under direct control. It can advise Government on policy matters without any corporate vested interest; this advice will come from an expert entity, rather than a "policy office" which may well be necessary if the FPC is to become fully commercial.

(Note, however, that the issue of the FPC being a lead agency as well as a commercial operator was addressed in the 2006 statutory review of the FPC. There, it was decided to retain the lead agency role within the FPC – the agency was fairly small, skills/expertise could be enhanced in the FPC and direct appropriation would reduce the real or perceived risk of commercial conflict of interest.)

A Forestry Department's primary function, acting as one of the Governments natural resource management agencies, would be to manage the natural resources of the State from a holistic perspective (one of the problems of any agency with a single brief, is that the agency can lose perspective of the whole).

It will be in a position to advise the State as to how forestry can be used to solve a range of problems – and implement the effect of this advice. (This does not mean that one should combine all agencies which have a role in solving the same problem – but this issue will be addressed later.).

The creation of a Department does not need to mean the loss of commercial capacity. For example, the New South Wales Government created a commercial entity (Forests NSW) within its Department of Primary Industry, with responsibility for forests and plantations, lands management and separate funding for CSO's. Environmental services are provided through the entity as are recreation and conservation,

Leaving aside debate as to whether WA would be best served by a Department of Primary Industry or Natural Resource Management, the situation in NSW can be seen as somewhat analogous to a Department of Forestry with a marketing GTE within it – with a board if required.

This agency would be required to act ONLY as the marketing/contracting arm of the Department. Should the State (e.g., Verve/Synergy) wish to meet its Carbon responsibilities through the Department then contract details would be negotiated through the Marketing organisation, with the returns going back to the State, for use perhaps in meeting its other environmental responsibilities.

The Department of Forestry would also provide the opportunity to move duplicate elements of forest management out of the DEC (where it would still "regulate" activities within forests being maintained for reserves as now).

It is likely the "Green" movement would prefer to see forests maintained by a "Department of Forestry" with no direct commercial benefit, than a "Commission" expected to make a profit.

A Department

The model above defines a Forestry Department, the major roles of which relate to environmental management, lead agency responsibilities, policy advisory, industry developer, forest management and so on. It just happens also to provide Government with a significant financial return from some of these activities.

A balanced view of forestry means achieving the "triple bottom line" of positive environmental, economic and social/community outcomes. Naturally, there are competing objectives; sometimes, the meeting of one agenda will have downsides for another. It is all about balance.

Unfortunately, commentators always seem to adopt an extreme position, which is not helpful and casts more shade than light on the debate.

Economic sanity does not need to mean environmental madness and vice versa. That one agency needs to address the three cornerstones of the triple bottom line, and that this is not easy, does not mean these responsibilities should be split - to the contrary.

However, perception needs to be addressed also. History shows that if an agency has an environmental focus, then any direct or indirect funding it receives from "commercial" operations will be viewed with suspicion.

Under these conditions, it may be necessary to separate the "income" side of forestry from the operational side.

The original intent of the FPC was to do only this – to set up a small agency with responsibility for marketing forest products available through the work of the then CALM. This would have meant establishing a Statutory Authority of less than 30 people.

This would excise the "commercial" from the FPC but is not a recommendation for putting the rest of the FPC back into the Department of Environment and Conservation. The focus of that agency is very much the environmental cornerstone of the triple bottom line, and so it is not ideally placed to exercise the "balance" referred to above.

The separate marketing authority within a Departmental structure is not recommended for reasons spelled out in the following paragraphs, but is an option.

A Statutory Authority

The discussion above relates to the coordinating benefits of a Departmental Structure, but also illustrates a significant difficulty, that being the capacity of a Department to operate as a commercial entity (probably requiring a GTE within, or similar).

Another issue exists in that a Department cannot have a Board of Governance and therefore would have to resort to something like an advisory committee to reflect the interests of stakeholders.

The above model would have a Board only on the commercial side, which would probably produce accusations of bias from those whose input was less part of the formal system.

If the "GTE" was to be a separate entity completely, it would create other problems in obtaining the triple bottom line and would require two agencies rather than one.

However, there is one structure that would overcome these difficulties.

There are examples of Statutory Authorities such as Landgate and the Disability Services Commission (DSC) that in fact work as both a Statutory Authority and a Government Department.

Should the FPC be recast as both a Statutory Authority and a Department, it would have the advantages of the departmental structure but without the disadvantages.

First, it is well placed to provide a balanced focus on the "triple bottom line" and to provide Government with the most expert advice on forestry and how it can be used broadly in the best interests of the state.

As a Statutory Authority it can acquire property, trade, sue and be sued, etc. It can earn and either receive a net appropriation or otherwise return its income (profit) to the state.

As a statutory authority it will have a Board which can be selected on the basis of skills and knowledge of each element of the triple bottom line. This would demonstrate to interest groups that information they believe to be important would be available to the Board and agency.

Should the FPC continue to operate in native forests, and have the responsibility to draft its own forest management plan, then a Board with skills and experience across issues that are important to interest groups is likely to be more acceptable. Note, skills and experience are recommended – not the representation of interest groups per se.

All CSOs/Budgets/funds expended etc will be open to parliamentary scrutiny through the process of Estimates Debates (not presently the case).

A Statutory Authority can also operate as a Department for the purposes of the Public Sector Management Act (see Landgate, DSC). Presently the FPC cannot pay its staff commercial incentives nor does it offer them the security of the Public Sector.

An organisation with the above attributes also appears to meet the attributes of agencies sought by the Economic Audit Committee.

The issue of being a commercial operator, but also giving policy advice to Government is not so relevant if the agencies role is seen as being to balance the triple bottom line of the economic, social and environmental. This was certainly the view of the Legislative Review of 2006.

However, the "commercial" sector within is visualised as a section, or "sub-department", of the FPC, free to operate commercially but constrained (or encouraged) by a Board and Corporate Executive with a broader view. With all income being returned to Treasury and with the agency being funded through consolidated revenue, there is markedly less likelihood of the agency operating as a pure GTE – even though it would compete at commercial rates in the market place and in keeping with National Competition Policy.

The changes for staff inherent in the agency becoming a Department under the Public Sector Management Act are career security. However, should staff wish to remain on the same employment conditions as presently, then there is no impediment to them doing so. All new employees would be employed under the PSMA .

Recommendation:

It is recommended the Forest Products Commission be recast as a statutory authority for its operations and as a Department under the Public Sector Management Act.

It is recommended the agency be re-badged to reflect its forestry obligations under the "triple bottom line" of economic, environmental and social responsibility.

The "Agriculture Option"

Whilst the above option is recommended, some consideration of a broader departmental model is offered.

The Department of Agriculture and Food (DAFWA) has previously argued that synergies between its functions and those of the FPC (eg farm forestry, mutual interest in the land, salinity management and others) provide sufficient reason for incorporating forestry within DAFWA.

In its legislative review submission of 2006 the Department argued for a departmental structure for the FPC (within Agriculture) citing concerns that a commercial entity (the FPC) had lead agency status and involvement in plantations and farm forestry.

Their present submission draws attention to concerns that the FPC has been unable to complete its plantation and farm forestry strategy as it remains unfunded, the fact that the amendments to the legislation have not been enacted, state agreement acts having a negative impact on bringing in additional plantation developers and the like. DAFWA is critical also of the FPCs view of the value of tree plantings less than about three quarters of any land having a worthwhile effect on salinity.

DAFWA also raises issues that would need to be addressed such as debt management, HR issues, difficulties between DEC and the FPC, state agreements and plantation management before any move to departmental status should occur.

The latter issues should be addressed in any event, no matter the organisational structure to be pursued.

In its summing up, the DAFWA submission states "The Department believes farm forestry advisory services are required to support land owners. This could be achieved by equipping a department with the relevant expertise from FPC, and possibly forestry and revegetation expertise from DEC. If responsibility for woody perennial vegetation on private land is consolidated within one Department, it is logical the relevant public sector expertise also be based and maintained in that Department.

There is something to this argument; the question is, however, whether DAFWA would be the preferred vehicle for that.

Experience elsewhere suggests that merging agencies with some synergies, but also with different contributions to make, can have major unintended and adverse consequences.

Further, it is well known in organisational literature that once agencies reach a certain size administrative costs become disproportionately high and communication channels over-extended to the point of becoming dysfunctional.

If DAFWAs expansion came via the inclusion of a new "Division of Forestry", the aforementioned concerns may very well materialise. There is also a real risk that forestry would suffer if it was not the primary focus of the agency. It is fine to argue that with a broadened brief, the agency would simply adjust to its new mandate, but in practise this seldom occurs, at least for some considerable time.

As much as anything, the FPC can be seen as one of a number of natural resource managers or environmental contributors. As such, a case could also be made for merging the FPC with another natural resource or environmental manager but with the same issues arising.

In reality, the state has many responsibilities that cross the boundaries of a number of departments. The best way to bring the agencies together is not to combine them unless synergy is very strong or they are too small to be individually viable. There is no one combination of agencies that will solve the myriad complex problems of Government.

It is better to divide Government into key policy areas and bring the relevant agencies together to jointly address each issue of mutual interest, for example, in a natural resource management group for that purpose, as is the case now. That is, bring different agencies together in different configurations to solve particular problems where each has a particular contribution to make.

During consultation a question was asked as to what would need to be "left out" if the FPC moved to DAFWA or some other Departmental arrangement?

As seen above in the "Forestry Department" option, nothing needs to be "left out" if one adopts the NSW approach to managing native forests within the Department for Primary Industry. In fact, that model incorporates both the commercial and environmental elements.

Should the Government opt for a GTE model, then the Department of Agriculture and Food is a contender to assume policy responsibilities. However, for reasons spelled out above, that solution is not recommended.

Section 5: Financial review

A comprehensive independent review of FPC's operations and financial forecasts, including a review of insurance practices in order to rigorously assess FPC's sustainability.

1. FPC's financial business model

The *Forest Products Act 2000* established FPC as a Government Trading Enterprise responsible for generating revenues and making profit. It generates its income from the sale of forest products and from the provision of forestry and related services.

FPC has two business streams, a harvest business and a new plantation business. The harvest business is the traditional log timber supply business supplying native and plantation grown timbers into South West sawmills. The New Plantations business is the business of establishing new plantations to provide the future timber resource of the State together with the environmental benefits of carbon and salinity control.

The sale of timber to sawmills provides the revenues to support the harvest business whereas the revenues for the New Plantations business have come from Government environmental programs to address water quality and salinity and more recently from fee-for-service projects with carbon investors.

Sales revenues need to not only recover the direct cost of harvest and delivery and other operating costs but also need to provide sufficient 'margin' to re-establish and manage the resource for future harvest. Sales revenues also need to provide sufficient margin to service FPC's long term debt.

FPC pays income tax equivalents under the National Taxation Equivalent Regime (NTER) along with all other government taxes, duties, rates and charges.

In addition to paying all tax equivalents, FPC meets all other competitive neutrality requirements of National Competition Policy. Competitive neutrality ensures that FPC, by way of its Government ownership, does not enjoy a competitive advantage over competing businesses. Conversely FPC is required to comply with all State Government policies.

FPC's capital expenditure needs are funded from retained revenues. FPC's non forestry capital needs are primarily minor plant and equipment, IT systems and other periodic infrastructure needs. Given these needs are relatively minor, such investments can be funded from profits, however any major new investment in plantations, land or buildings need to be funded by additional debt.

The FPC also pays a dividend to the State from its annual profits. FPC dividend policy provides for 50% of Net Profit after Tax (NPAT) prior to natural resource asset valuation to be paid as a dividend.

2. FPC's long term financial strategy

FPC's long term financial strategy is to develop plantations which will supply the State's future demand for timber as well as environmental values. Given the nature of investment markets, the investment strategy is based on renewable energy and carbon markets to fund the future expansion of the State's plantation timber resources together with providing a more diverse revenue stream.

During the past seven years, the FPC's plantation expansion program (Strategic Tree Farming (STF) project) has been funded by borrowings and more recently (since 2004) by the Commonwealth and State Government through the National Action Plan for Water Quality and Salinity.

Government funded natural resource management programs similar to the STF project are unlikely in the medium term, certainly at the scale of the $64 million STF project. Current State government approved funds for natural resource management projects would suggest that future FPC's natural resource management projects are likely to be small scale projects focussed on high value water catchment areas.

FPC's existing and new timber plantations will need to play a significant role in the emerging renewable energy and carbon markets. Current unused resource from FPC's plantation and native forest harvest operations will be a key feedstock to new and existing bio-energy power stations. FPC's capacity to establish the plantations will be crucial to the State to create the carbon permits required by both the private and public sector under the CPRS.

FPC's strategy has been to position itself as the provider of these services and in doing so becoming less reliant on Government environmental programs as a source of funds for plantation expansion.

FPC's technical ability and organisational capacity to meet the current demand for forestry carbon permits is keenly sought after by carbon emitters. Demand for forestry based carbon permits far exceeds existing capacity as forestry remains the most viable carbon offset option available to carbon emitters. In the absence of forestry permits emitters will be left with little option but to buy permits at the proposed CPRS carbon permit auction.

The renewable energy and carbon markets present a real opportunity for the FPC to assist carbon emitters and energy suppliers meet the legislated targets on renewable energy and carbon emissions. The WA State Government's electricity producers (Verve Energy and Horizon Power) will have a major task in achieving these targets.

FPC financial strategy has also been to maintain and improve the profitability of its traditional harvest business. This strategy is designed to not only deliver consistent financial returns to the State but also to improve financial margins necessary to continue to re invest in ongoing forest management.

3. FPC's financial position

FPC has historically returned a relatively small annual profit consistent with other Australia forest agencies. Annual FPC revenues have remained relatively consistent year on year after the initial decline following the introduction of Protecting Old Growth Forest policy.

However the 2008/09 financial year has been a difficult year for the FPC. A number of major events, specifically:

- the Varanus Island gas explosion (which saw the pine timber industry effectively close down for 6 weeks);

- the Yanchep and Bridgetown wild fires in January 2009; and
- the broad economic downturn,

all combined to seriously impact on FPC's financial performance.

To assist the FPC to deal with this financial impact the Economic and Expenditure Review Committee (EERC) agreed to an initial $15 million equity injection with a further $10 m conditional on a review into FPC's operations and its financial sustainability.

While the difficult 2008/09 financial year was the result of several one off events, being the January wildfires and the Varanus Island gas explosion, the broad economic downturn will continue to manifest itself in the short term through reduced customer demand. As a result of economic circumstances three major sawmills have closed (most likely permanently) and several others have reduced their forward orders reflecting the continued difficult economic conditions.

In response to these conditions, the FPC has taken steps to find replacement markets for surplus timber resource and to reduce expenditure. However FPC's ability to achieve this in the short term is difficult due to the relatively high fixed cost nature of forestry and the time to develop replacement customers.

FPC's financial forecasts are further impacted by the continued uncertainty surrounding the implementation of the Carbon Pollution Reduction Scheme.

FPC has just completed a 8,500 hectare new plantation planting program in 2008/09 including a 5,000 hectare carbon planting program for Synergy and the final 3,500 hectare planting for the Commonwealth and State government funded Strategic Tree Farming (STF) project.

While demand for FPC plantation services is strong, without exception potential customers are looking for CPRS regulatory certainty before committing to a carbon planting program with FPC. If the CPRS legislation does not pass before October 2009 it is almost certain that FPC will have no planting program for the 2010 year.

This uncertainty has left the FPC in a difficult position, the need to maintain capacity to establish carbon plantings with the strong possibility of FPC not having a funded planting program for 2010.

The FPC does not have the financial capacity to establish new plantations in 2010 in its own right in preparation for a 2011 program.

4. The carbon market

Western Australia will have large carbon liabilities arising from the CPRS. These obligations will arise in both the public sector, primarily in power generation, and the private sector through existing and proposed resource development projects.

Carbon emitters such as these have limited options to secure carbon permits other than through the Emissions Trading Scheme (ETS) proposed under the CPRS. The ETS creates the mechanism through which carbon emitters acquire and surrender carbon permits. Carbon emitters are looking to diversify their new carbon liabilities through a portfolio of measures including acquiring carbon permits through plantation based carbon sequestration.

Carbon sequestration through the establishment of new plantations represents a unique opportunity for the FPC and for the State. The creation of carbon permits through bio sequestration not only assists with meeting carbon reduction targets but also assists in creating new timber resources for the State, ongoing salinity control and regional development.

Without the carbon permits created through offsets, carbon emitters will need to acquire all their required permits from the Commonwealth through the carbon permit auction. "Growing" carbon permits in Western Australia through the establishment of new plantations rather than "purchasing" carbon permits from the Commonwealth delivers direct financial, timber, salinity and regional development benefits to the Western Australian economy.

FPC's carbon business model is clearly focussed on an integrated model where carbon plantings are integrated with agriculture and the plantings are established with a harvest timber product outcome, not just plant and forget. That is, secondary benefits are derived.

The FPC is the only Government agency with the technical capability and organisational capacity to undertake this work. Until there is a viable private sector capability to provide this service, the Government must maintain the capacity to do so. In fact, as has been stated earlier, public company executives believe the market will be so large that all potential players will be needed.

5. FPC harvest business

The FPC's financial projections for its harvest business suggest that customer demand will remain at 90% for the next year or two. The loss of three saw mills and the general reduction in FPC customer demand suggests it will take some time before revenue returns to pre 2009 levels.

The FPC harvest business supplies the majority of its products to sawmill customers supplying the Western Australian construction sector, primarily for residential housing. The WA housing sector remains subdued though recent indications are that the economic downturn is unlikely to be as deep or protracted as originally thought. While FPC sales contracts generally do not provide 'take or pay' provisions where the customer is required to take a minimum quantity the long term sales contracts do guarantee the resource to the customer therefore restricting any ability to find alternative markets for this 'surplus' resource in periods of reduced customer demand.

While revenues are variable, major elements of FPC's cost structure are fixed. Forest management expenses, employee expenses and payments through to the Department of Environment and Conservation (DEC) are essentially fixed regardless of revenue.

The FPC harvest business requires ongoing investment in forest management expenses maintaining the resource for future harvest. This investment is an annual investment to provide the resource for future harvest. The cost is incurred regardless of revenue and while it can be delayed a year or two it must ultimately be incurred to maintain the integrity of the future resource and to deliver the State's commitments under the various timber supply State Agreement Acts.

FPC financial projections

The FPC has developed its 5 year financial projections assuming that reduced timber sales will continue in the short term until returning to pre 2009 levels in 2012/13. Its projections are also based on the CPRS commencing in 2011 with FPC establishing 10,000 ha of new plantations in 2011 increasing to 15,000 ha in 2012 and each year beyond. The forecasts are also developed assuming an expenditure reduction program and ongoing postponement of forest management programs until sale revenues increase.

Under this scenario FPC will make a loss in 2010/11 and 2011/12 before returning to profitability in 2012/13.

Should the CPRS not eventuate and demand for forestry based carbon permits disappear FPC would need to contract to a timber harvest business only. FPC would then need to further downsize all elements of its business to the level the timber sales revenues can support. Under this scenario FPC becomes a much smaller business.

It is problematic if the FPC is financially viable in the long term under this scenario as the degree of cost cutting required to maintain a cash operating surplus is likely to be not sustainable. Unless financial impediments to FPC are resolved FPC will need continued government support.

Specifically the annual payments to DEC including fire suppression costs need to be reviewed to ensure that payments made are consistent with what FPC's sales revenues can support.

6. Strategic Options for Government

An FPC with a strong new plantations business providing carbon plantation establishment services to the new carbon economy will ensure FPC's financial sustainability. The State will maintain a strong carbon offset capability not only delivering the carbon values but also the timber, salinity and regional development benefits that the FPC carbon model provides.

Under this model FPC returns to profitability after 2010 thereby providing a regular dividend stream to the State. The FPC as a harvest only business will require ongoing financial support either through resolving some of FPC's financial impediments to success or through direct financial assistance.

The FPC as harvest only business means the State loses it capacity to establish new plantations under the carbon banner. Future timber resources for the State will need to come via imported timbers in some cases sourced via unsustainable forest practices. Future opportunity to invest in plantation and associated infrastructure in regional WA is also lost

However, in the meantime, without direct financial assistance from Government, FPC will need to downsize its business, severely impacting on its capacity to provide this benefit in the long term.

This downsizing will involve reducing capacity in FPC's regional offices including the likely closure of some regional offices, downsizing the Manjimup Nursery (if not selling it) and negotiating severance with the 40 – 50 employees effected.

The cost of this is likely to be in the order of $10 million including $3m to $4m in severance costs plus $5m to $6m in deferred forest management expenditure.

This $10m would be far better invested in maintaining FPCs new plantation capacity. This $10m would be combined with a $15m contribution from Synergy to undertake a 5,000 hectare planting program similar to the 2009 program.

This would result in a carbon asset being developed for the State, FPC's capacity maintained and regional employment retained.

The biggest benefit, however, remains the ability of the State to retain through the FPC the capacity to assist the large public and private carbon emitters in managing their CPRS carbon liabilities.

Providing the FPC with this "once off" injection carries little or no risk as Government will need the $10m for carbon off-set in the future, and Synergy are likely to need to purchase the "$10m worth of plantation in any event. That is, there in no net cost.

Not providing the $10m, however, is likely to lead to major repercussions. The FPC will need to "re-boot" the capacity to develop plantations for carbon sequestration and bio-mass, certainly deferring its capacity to respond, if not causing much greater long term damage.

Financial modeling by FPC demonstrates that a retained capacity will generate significant future income for the state, along with significant environmental and social benefit.

Note, the sub-section immediately following addresses other impediments to the FPC's financial model. It can be seen readily that the FPC would be making a significant profit should these additional burdens not have been put on it. In a sense, FPC is being "punished" by circumstances for which it is not responsible.

Recommendation:

It is recommended that FPC be advanced $10m to maintain operational capacity in the lead up to the 2011 carbon planting.

7. Other impediments to FPC's financial model

It is in the context of reduced FPC revenues that FPC has sought to revisit some long standing anomalies of its financial relationship with Government and with the Department of Environment and Conservation.

FPC debt structure - $6m/a

On establishment FPC assumed the assets and liabilities of the forest products business units of CALM. Included within that was long term WATC debt of $75 million. Subsequently that debt has grown to $91 million a net increase of $16 million. This increase in debt has been used primarily as the State's matching contribution with the Commonwealth government for the National Action Plan for Salinity and Water Quality (NAP) program under which the STF sits. The cost of servicing this new debt has been met by direct government financial assistance; however the underlying long term debt inherited from CALM remains.

FPC/DEC works agreement - $8m/a

The financial relationship between FPC and the DEC has been the source of much consternation between the two agencies for some time. At the establishment of FPC, arrangements were made for FPC to 'contract in' some core business services from the then CALM. The basis for these arrangements was to avoid duplication between the two agencies and for FPC to access the existing capacity within CALM on a 'fee for service' basis. It was also designed as a means for CALM's fire fighting workforce to undertake FPC plantation works when not required for fire duties.

Both FPC and DEC have been unhappy for many years with these arrangements. FPC has been unhappy with the lack of control, the quality and the value for money of the works done while DEC believe more funds should be made available, particularly for plantation fire protection.

Major concerns of the FPC with the current arrangements revolve around FPC's inability to control a significant amount of expenditure. Payments to DEC represent 25% of FPC's "controllable" expenditure. However, in effect it has no control over that expenditure, to use normal commercial means to improve service delivery, to ensure value for money outcomes or to manage expenditure to available revenues. Basically DEC gives DTF its "costings" and the FPC is debited that amount.

DEC fire suppression costs - $2-5m/a

FPC is required to pay DEC for all costs incurred by DEC in suppressing wildfire in or threatening the State's plantations. The basis for levying this cost to FPC is that DEC fire suppression actions are protecting the FPC's asset. Based on working arrangements established when FPC moved from CALM, costs incurred by DEC in suppressing wildfire in State Forest, where the primary asset being protected is an FPC plantation are levied against the FPC.

Unlike other State forestry agencies FPC has no fire fighting capacity; all fire suppression capability is retained by DEC. The origins of this arrangement stem back to the establishment of FPC away from CALM in 2000 where the decision was taken to retain the State's fire fighting capacity within CALM.

This cost of wild fire suppression has increased significantly over recent years as the intensity, number and cost of fires has increased. Ultimately some part of government has to pay the cost of wildfire suppression. It is noted that no other government agency, private company or private landowner is required to contribute to the costs of DEC's fire suppression activities in a similar way to FPC.

FMP contribution - $0.9 m/a

FPC pays $0.900 million to DEC each year as a contribution to DEC's costs in administering the Forest Management Plan. FPC contends that the FMP imposes a disproportionate cost on forestry operations that must be borne by industry and therefore suggests that the degree of regulation and oversight be reviewed with the objective of reducing this impost on industry.

Human Resources and Financial Services - $ 1m/a

FPC purchase Human Resource and Financial transactional services from DEC under an annually reviewed Service Level Agreement. The cost of these services amounts to approximately $1 million per annum. Given the size of the FPC in terms of its establishment and accounting requirements, this seems excessive. Understandably, FPC would prefer to bring that service in house or seek competitive tenders for the work.

FPC has been reluctant to undertake either of these options as it has been scheduled to utilise the Office of Shared Services (OSS) for some time. To avoid the costly exercise of transitioning to an alternative arrangement when the OSS role is imminent this option has not been pursued. However FPC's transition to the OSS continues to be delayed and it would seem reasonable for the FPC to assume responsibility for its own services. Advice is that DEC would be comfortable with this.

Non Commercial Activities - $4m/a

FPC undertakes a range of activities and functions to deliver on government policy, to develop and support industry and to comply with government regulations. Many of these activities provide no direct financial return to the FPC though provide a range of forest industry and regional benefits.

Whilst FPC identifies these activities in its annual Statement of Corporate Intent the cost of undertaking these is born by the agency at the expense of profit and dividend.

Peel A

The Peel 'A' pine plantation in Baldivis has been clear-felled over the last few years, the land being required for urban development. A 1996 cabinet decision resolved that proceeds from the sale of this plantation land were to be used to retire CALM debt associated with the then CALM maritime pine project.

On establishment FPC inherited much of this debt from CALM with the expectation that the proceeds from the sale from the Peel A plantation would accrue to FPC to retire the inherited debt.

The plantation has been removed and Landcorp are now developing the land. Monies have been flowing from Landcorp to central Government; FPC has received none of this income.

FPC understands Landcorp have made payments to government of approximately $24 million to date.

FPC is of the view that these monies should be used by FPC to retire part of its debt.

Mine clearing compensation - $5m/a

Alcoa and Worsley, as well as other mining companies, make payments each year to the State (via DEC) as compensation for the impact of their operations on State forest. The payment of this compensation is a requirement under the various State Agreement Acts which support these mining operations.

FPC is of the opinion that it should at least receive a portion if not all these payments on the basis that the payments were originally set up to compensate for loss of future earnings from timber production in addition to the loss of other forest values.

As the timber production issue impacts directly on FPC's business then it would seem logical that FPC or Industry benefit from the compensation. FPCs case would appear strong.

Implications of these "other impediment"

The above "other impediments" are not insignificant as seen in the summary below:

a)	FPC Debt Structure	$6m pa
b)	FPC/DEC Works Agreement	$8m pa
c)	DEC Fire Suppression Costs	$2m to $5m pa
d)	FMP Contribution	$.9m pa
e)	Human Resources and Financial Support	$1m pa
f)	Non Commercial Activities	$4m pa
g)	Mine Clearing Compensation	$5m pa
h)	Non receipt of income from the sale of Peel A	$24m

a) This is an impost resulting from the long term nature of timber investment, but resulting mostly from events occurring before the FPC existed. It is arguable the FPC will obtain no benefit from some of this investment.

b) This is a matter over which FPC has no control, but does pay a 40% loading it would not pay commercially.

c) There is a question here as to what FPC is charged for. It is understood FPC pays the total cost of a fire (for fighting fires in state forest or the potential threat if they are not actually in the state forest; ie DEC reserve).

   Given DEC receive salaries for staff employed whether fighting fires or not, charging the full cost of the fire fighting is not justified.

d) See comments above, FPC believe they are paying too big a share.

e) $1m is excessive

f) These are non-recompensed CSOs that Government would need to purchase elsewhere if the FPC did not conduct them.

g) These represent a loss of potential income, which on the face of it, should have gone to the FPC.

h) These represent a loss of potential income, which on the face of it, should have gone to the FPC.

Not all of the above could be expected to flow to the FPC. However, it is clear the FPC is doing far better than would be shown simply by looking at the "bottom line".

Ongoing responsibilities

In addition to the above, the FPC undertakes a considerable amount of clearing, road building and maintenance among other needs relating to harvest operations, some of which would need to continue were the FPC to quit its native forest operations.

Should the FPC cease its operations in native forest or be required to downsize its activities to any significant extent it is important to note that many of the costs would continue, such as debt, fire suppression, a proportion of the activities carried out in the works agreement and some of the FMP.

Given the FPC is now expected to meet its own costs, the State would need to find an estimated additional $10-15million plus, annually, should it cease to exist.

Recommendation:

It is recommended that DTF examine the above impediments to the financial performance of the FPC and adjust them accordingly.

Recommendation:

It is recommended the FPC Human Resources and Financial Support Services currently conducted by DEC be passed to the FPC with the financial resources currently paid to DEC for this purpose.

Section 6: The appropriate degree and means of overseeing harvest operations on public lands

Presently, although consulted, the FPC has little or no say in the amount of timber it is allotted in the 10 year Forest Management Plan. DEC prepares a forest management plan for the CC, rolling indicative three year harvest plan, participates in development of an annual harvest plan, prepares manuals, guidelines to set environmental standards, vets operations, grants access, monitors the harvesting operations, requires changes from time to time and reviews the management system.

In its submission DEC is of the view that its statutory function to manage State forest, (CALM Act section 33(1)(a)(i)) to do so in accordance with the FMP (CALM Act section 33(3)(a)) and the requirement in the *Forest Products Act 2000* for the FPC to enter into an arrangement with the Executive Director of CALM in relation to access of the contractors to the land for harvesting (section 57(2)(a)), provide the legal basis for DEC's actions with respect to monitoring and granting of access.

FPC is required to undertake detailed planning in preparation for logging in any coupe and is required to submit the proposal to DEC for approval. This involves several checklists and coupe level planning documents, a two stage approval process during the wetter part of the year, safety checks by DEC, monitoring and so on

When the Regional Forest Agreement was signed in 1999, the intent was to balance environmental, social and economic values in forestry. However, 2001 saw the decision to cease logging old growth forest. The DEC submission to the current review points out that since this time there has been far less in the way of community/political issues in forests and the comment is made:

"However, close attention and careful management have had to be applied to ensure that the issue has not again (or yet) emerged as one of significant public controversy".

DEC was highly critical of the FPC in its submission to the 2006 Statutory Review, particularly with respect to what it saw as not meeting the environmental standards set in the FMP and not recognising CALM's role in meeting those standards. (DEC also state that the FPC does not invest sufficiently to ensure ecologically sustainable forest management, citing as the most likely reason the FPC's role as a commercial entity required to accrue profits).

DEC comments in the present review acknowledge improvement in both these areas, but state "However, the fundamental institutional settings that lead to these issues remain, as identified in the report on the mid-term audit of the FMP".

The DEC submission goes on to state that forest conservation groups continue to monitor the FPC's forest activities and so the highest standards should therefore prevail in order to prevent further political debate.

Community expectations are important; however, one wonders to what extent DEC's close control and monitoring is driven by this concern rather than a real need to be so "vigilant".

In its submission DEC goes to some lengths to explain its management of FPC's involvement in state forests and whilst stating that the performance of the FPC has improved, nevertheless points to areas where the agency would like to see more improvement. The mid term FMP also has the CC being critical of the FPC and DEC.

An FPC Perspective: DEC explains its need to be in close control to meet its legislated role and manage the political/community situation. The FPC, however, is of the view that the way in which DEC undertakes its role is needlessly intrusive, costly for both agencies and causes FPC unnecessary difficulty in meeting their agenda.

FPC argues for a simplified approvals/monitoring process.

An examination of the documents/checklists and approvals processes does reveal what appears to be a needlessly complex system.

DEC has the material and capacity to draft (in co-operation with FPC) a set of guidelines for the harvesting of forest which will cover nearly all situations.

It is surprising that approvals are not simply a one-step processes where FPC is allotted its list of coupes that are available over, say, a five year period (in advance) and required to undertake the work in a prescribed fashion in accordance with set standards. The DEC then monitors progress as an auditor.

It may be that DEC management needs those staff who are involved in approvals and monitoring to be available to fight bushfires in the summer months. It may be that DEC is overly concerned that it must handle the perceived community/political risk. Whatever the situation there is no doubt DECs management of FPC can be radically simplified.

On touring the State's forests, the comment made by several people was "if you shake a tree a couple of DEC officers are likely to fall out." Whilst certainly facetious, the comment may be justified.

Section 7: The Forest Products Commissions Role as both a Commercial and Non Commercial Entity

1. Potential synergies and conflicts between the FPC's commercial and non-commercial activities, and the extent to which this affects its overall performance;

This topic has been addressed in part elsewhere in the report in the context of forestry requiring a "balance" in order to meet the desired triple bottom line. There are many synergies within forestry operations and between commercial and non-commercial activity.

In fact, as also expressed earlier, one needs to look at the industry as a whole in order to obtain the best view of its parts. For example, the value of timber should not only be assessed on the basis of any one use. One tree can provide timber for quality furniture, material for fabricating composite timber, biomass for burning and so on.

Additionally, while a tree is growing it will have sequestered carbon and continue to do so while it remains as furniture or is used for bio-char; it may have had a role in salinity or erosion control and provided a habitat for birds/animals. It will have provided jobs in the process.

Each use is important in assessing the value of timber.

Each, more to the point, requires the same set of forestry skills to manage and the management of each really cannot ideally occur independently of the others, if one is to maximize what the industry can achieve.

That is, one could view the sale of timber products as the result of environmental activity or environmental management as a bye-product of commercial activity. To some extent each is true.

The consequences of not looking at the whole can be demonstrated by example:

If trees are grown for carbon sequestration, but not harvested, they provide no local industry other than keeping them alive. If they are harvested they can be exploited to replace aluminium as building material, bio-mass to replace coal and so on. They provide for both industry and community development.

If trees are grown only for sequestration, large blocks in higher rainfall regions will probably be preferred. This will probably not assist in erosion control or salinity management.

If re-growth forest ceases to be harvested, a large acreage will be removed for the environmental purposes that stopping the logging is meant to protect. Trees left in the ground can sequester carbon only once until they die and new trees grow. Harvesting enables carbon to be sequestered multiple times on the same patch of ground, thereby acting more to reduce global warming than any tree merely left to grow old. It is the growing tree that sequesters, so harvesting increases the total amount that can be sequestered.

As can be seen there are many synergies within forestry, and between elements that are both commercial and non-commercial.

The point is not to separate these elements out such that there is no possible conflict. The goal should be to maximise the "triple bottom line" whilst acknowledging the potential for conflict – and to establish processes that minimise the risks inherent in that potential conflict – without causing unintended harmful consequences.

2. Impediments to FPC operating as a commercial entity

The need for the FPC to operate as an environmental manager, whilst being established as a commercial entity is one of the impediments it faces, particularly as by and large these non-commercial activities have not been recognized in a budgetary sense.

A timber industry spokesman complained that he didn't know if the FPC was a timber producer or environmentalist. What was the Commissions priority?

The answer is that it is both, but established in such a way as to limit its effectiveness as either. The solution is most likely to be found if the nexus between FPC contracts and the FMP is broken.

There is no reason, left to its own devices, that the Forest Products Commission cannot maximise its triple bottom line result.

Its current impediments are largely financial and are not the result of anything the Commission has done. These are spelled out in the Finance Section along with possible scenarios to address them.

In short, however, unrecognised community service obligations and lack of clearly spelled out functions that recognize this role are two major impediments.

FPC payments to DEC are another impediment. A commercial organisation would not enter into any contracts such as FPC has with DEC – certainly not at the price. It is similarly considered that a commercial operator would not tolerate the nature of approval processes and monitoring the FPC faces

The 10 year FMP itself places the FPC in difficulty with no investment likely towards the end of the plan. The 3 year/1 year "interim" plans do not give the FPC sufficient lead time or flexibility in sequencing their activities. The fact that the approval process requires sequential approvals and that DEC regional managers can and do make decisions requiring further FPC action is cumbersome and time consuming.

In Victoria, the Forest Management Plan is a rolling15 year affair, divided into 5 year stages such that when one stage commences, the next 5 year stage is drafted thereby solving the problems caused by the 10 and 3 year WA scenario.

Recommendation:

It is recommended that any Future Forest Management Plans operate over 15 years, in three 5 year segments, with the FPC being given flexibility to harvest across each 5 year segment.

It is recommended that contracts of sale not be limited by the length of the Forest Management Plan.

3. The appropriate commercial powers - e.g. to enter into joint ventures - needed to deliver the State's commercial forestry and forest industry objectives:

The appropriate commercial powers for the FPC depend somewhat on the nature of the agency it is to become. Should the agency revert to a Departmental model, then issues such as its capacity to borrow will be largely Treasury driven.

However, there are precedents for agencies that are both a Statutory Authority and a Department with commercial capacity.

Should the agency become fully corporatised, then it should have the same commercial powers as other Government GTEs.

However, it must be emphasized that whatever structure finally emerges, the agency must have all of the commercial powers it needs to operate on a level playing field. It is in the best interests of both industry (National Competition Policy) and the agency (fair commercial return) that this be the case.

Given the difficulty attracting investment and the respect with which the FPC appears to be viewed, there are clearly likely to be opportunities for joint ventures. One issue not raised earlier relates to the boundaries within which the FPC operates. Taking a broader view of its role in environmental management, and its expertise, it is also recommended the FPC be given the authority to operate at a national (and potentially international) level.

4. The potential role of the FPC in leading the development of renewable energy from woody crops and the generation of competitively priced emissions units from reforestation while generating other economic, social and environmental benefits.

As spelled out in the independent review conducted of the FPC for due diligence purposes, at least one major corporate assessor of such things holds the view that the FPC meets the highest standards to generate competitive priced emissions units. In fact, the Company for which the report was prepared also finds the FPC a preferred provider precisely because of the "secondary" benefits to society and the environment whilst meeting the companies economic goals.

The WA Government-owned "Synergy" Corporation holds the FPC in similar high regard and is pursuing the possibility of the FPC extending its plantings to address their carbon debt and is also looking at options for other purposes.

A Company which for commercial reasons cannot be named here has also commenced discussions with FPC regarding the potential for them to grow biomass for fuel purposes.

During the conduct of this review opinion as to the competence of the FPC was almost uniformly that the agency was well managed, with a strong research and development capacity.

This is amply demonstrated in the Commissions research into which trees/woody crops are best suited to differing rainfall patterns and soil types, what silvicultural techniques are required and so on. Their research is of benefit to industry and to the State.

A very recent success of the FPC has been the agency's research into sandalwood. Working with the Universities of Western Australia and British Columbia, the FPC has discovered the gene responsible for the production of sandalwood oil. This discovery has major implications for the future of the sandalwood industry, which was in fact pioneered in Western Australia by the State Government through the FPC's predecessor.

To measure the effect of different plantation practices takes seven years with tropical and fifteen with native sandalwood. Having isolated the gene, measurement can now take place within months of planting.

The importance of this type of research carried out by the FPC, on whatever aspect of forestry, is major for industry and a measure of the organisations competence.

5. The FPC's obligations under the State's Forest Management Plan 2004 - 2013 and that Plan's likely successor:

The FMP is prepared by DEC and approved by the CC. Although the FPC is "consulted" in the process, in reality it has no real say in the decision. The CC has, since the current FMP, added extensively to reserves and is seeking the reserving of a further 209,000 hectares. Additionally, 63,000 hectares have been set aside for habitat zones, serving to further reduce the area available for harvesting, rendering the process of harvesting more difficult and costly.

As described earlier, the FMP requires the FPC to go through a tortuous approvals process and they are subjected to exceedingly close and intrusive scrutiny.

The FMP also contains a thirty per cent allowance for global warming and die-back. That is, the available harvest per annum is reduced a further thirty per cent as a "precautionary" measure.

The CC and single interest groups then claim that sustainable harvesting is becoming non-viable. The CC appears to act very much like one of the groups lobbying to cease all native forest logging.

Under these conditions, it may well be that the CC decides that there will be no timber available for logging under the next FMP.

As discussed earlier, however, the FPC has the capacity to operate a working forest in a sustainable and environmentally responsible manner. There are sound environmental, social and economic reasons why it should be commissioned to do this.

6. The interrelationship between the functions of the FPC and other agencies and the degree to which these are coordinated;

See the discussion under "the Agriculture option". The FPC is an agency that operates in several dimensions, operating to meet the triple bottom line economically, environmentally and socially. It has elements of both a GTE and an environmental manager. It has these in common with other agencies, but does not fit neatly within any of them.

Ultimately, the State Government decides those areas of policy which are sufficiently important to establish a forum for coordination of Government action. The Forest Products Commission has a role across, for example, salinity, global warming, regional development, industry development and so on. It is a matter for Government to consider the FPC, along with other agencies, when identifying policy considerations and which agencies have a role to play.

7. Existing public sector investment in plantations and farm forestry, and the extent to which the State's interests are served by maintaining a commercial agency to manage and profit from those interests;

See Section 5, Finance Review.

8. Emerging national legislation on renewable energy and carbon sequestration;

See Introduction and Sections 1 & 2.

9. The potential for private sector investment in plantations and farm forestry;

See Section 2.

Legislation

The Legislative Review of 2006 resulted in the drafting of the Forest Products Amendment Bill 2008 for presentation to Parliament. As it transpired, a State election was called before a Bill could be presented to Parliament.

The 2006 Review addressed many of the concerns that also arose in the present review and these were reflected in the Bill.

It is therefore proposed to comment on the 2008 Bill only and specifically on those elements where further discussion or change is recommended.

Depending on the degree to which recommendations of this report are accepted, there will need to be a more complete rewrite of the legislation; however, the following suggestions are offered:

Part 1 - Preliminary

"chief executive officer' to hold the title "Director General" in keeping with public sector norms.

"management plan" will refer to the plan developed by the Forest Products Commission

"non-commercial functions" means functions related to "forestry" (not "forest products")

"profit" - delete and use the terminology "financial return"

Part 2 – Forest Products Commission

Section 5 – A name change is suggested more in keeping with the Commissions "triple bottom line" agenda. Examples might include such titles as "Forestry WA" or "Western Forestry". The term "forest products" suggests a primarily commercial agenda.

Section 6 - Commissioners – also include a member with knowledge of environmental management more broadly and a Member with a Regional development perspective.

The Chairman reports to the Minister for Forestry (as will the Director General).

Section 10 – Functions of the Commission. Replace "Dual objectives of the Commission" with "Objectives of the (agency)". Redraft to broadly deal with the "triple bottom line".

An example might be "to utilise forestry and forestry resources to provide environmental, social and economic benefit for the State".

Section 11A – Functions. Include an environmental management function specifically referring to carbon, land degradation, salinity and "such other…as are necessary".

Section 11B – Other Functions. These will need amendment with respect to the management plan, CALM Act, any memorandum of understanding as a result of vesting land in the FPC.

Division 2 – Strategic Development Plan

Section 31 – Matters to be included in Statement of Corporate Intent. Subsection (j) to (l) refers to "the nature and extent of non-commercial functions that are to be performed" and to costs and compensation. It reads as a "tack on". It is suggested the goals of the agency be couched in terms of the three elements of the triple bottom line and that each be addressed separately as sections of the statement of corporate intent.

Part 5 – Staff

Section 39 – Other Staff. Staff to be employed under the Public Sector management Act and as permitted by that Act.

Part 6 – Financial provisions. To reflect that the Commission is funded through the consolidated fund.

Part 8 – Contracts for the management, harvesting or sale of forest products. Amendment will be required to reflect the greater autonomy of the FPC to manage its own operations – albeit there will be requirements to conform to the requirements of sound ecological management.

Other matters

When Governments (or organizations generally) attempt to "correct" anything or cater for a change in circumstances, it is rare for them to consider the matter in the context of "a clean sheet". What happens, therefore, is that the problem is resolved by "adding" something, such as a new agency, or a function to a new agency or a new regulation and so on.

After a time, it emerges that the system has become cumbersome or cluttered. There is presently a Government review of approvals processes and an economic audit that owe their genesis in part to this.

Within the environmental management area this seems to have occurred with regulatory mechanisms, land management and approvals processes.

The question is asked, "Why is it necessary to have a Conservation Commission of WA, an Environmental Protection Authority, a Marine Parks and Reserves Authority and a Department of Environment and Conservation which contain elements of previously existing agencies cobbled together into a new form?"

Some consolidation of these activities, for example by the creation of a new Environmental Protection Authority to include the previous functions of the EPA, MPRA and CC, should lead to improved efficiency.

An opportunity exists also to look at the internal workings of DEC in order to evaluate the management of functions it has had over a long period or recently acquired. This would fit in with the recently announced Economic Audit Committee, particularly term of reference 3 (An examination of the current structure of government agencies to determine whether changes are warranted to better support the efficient and effective delivery of government services) and 4 (An evaluation of the effectiveness of existing performance metrics and options for greater transparency and accountability through improved public reporting).

In terms of land management the relationship between DEC and the FPC as to who does what and who pays, which was discussed earlier in this report, has been needlessly complex, is inefficient, places the FPC at a commercial and operational disadvantage and renders the DEC not appropriately accountable.

Approvals processes are inefficient, convoluted, sequential rather than simultaneous and could be greatly simplified.

The Forest Products Commission is well able to manage these things to a set of standards, without requiring "over the shoulder" supervision, which would free up resources for DEC to use on environmental management.

Appendix 1

Terms of Reference

The Forest Products Commission (FPC) was established in 2000 as a Statutory Authority to manage Western Australia's commercial forestry activities, and is the State Governments lead agency for forestry and forest products. FPC undertakes a combined role of commercial manager of the State plantation and forestry resource, as well as providing policy development and other Government support activities. FPC manages the seeding, harvesting, maintenance and marketing of WA's state owned timber plantations, and is a competitor in certain sectors of the forestry and plantation industry, a monopoly provider in native hardwoods, and has a practical monopoly in softwood plantation in WA.

Government involvement (regulation, policy and industry support) in any industry should be aimed at providing leadership in achieving social, economic and environmental benefits through careful planning, regulation, research and development, coordination, monitoring, and evaluation and reporting.

The Review should address:

- the role of the State in timber and forest products;
- the need for the State to be a supplier of forest products (wood included) to industry;
- the State's appropriate interest and responsibilities in plantation and farm forestry;
- the State's role in encouraging and regulating private sector investment in commercial tree crops, for the accrual of social, environmental and economic benefits;
- the appropriate policy, regulatory and institutional arrangements to support sustainable and developing forest products industries;
- the State's national and international obligations with regard to forests and plantations;
- the need for the *Forest Products Act 2000* and any recommended amendments to the Act.

Key issues to examine and report on will be:

- the success of FPC in implementing the objectives of the *Forest Products Act 2000*;
- whether the *Forest Products Act 2000* and the Commission is the best way of achieving the State's medium and long-term goals;
- a comprehensive independent review of FPC's operations and financial forecasts, including a review of insurance practices in order to rigorously assess FPC's sustainability ;*
- the appropriate degree and means of overseeing harvest operations on public lands;
- potential synergies and conflicts between the FPC's commercial and non-commercial activities, and the extent to which this affects its overall performance;
- impediments to FPC operating as a commercial entity;

- the appropriate commercial powers - e.g. to enter into joint ventures - needed to deliver the State's commercial forestry and forest industry objectives;

- the potential role of the FPC in leading the development of renewable energy from woody crops and the generation of competitively priced emissions units from reforestation while generating other economic, social and environmental benefits.

In preparing recommendations to Government, the reviewing body should have regard to:

- previous reviews of the FPC, including the Department of Treasury and Finance's functional review and the previous government's statutory review of the *Forest Products Act 2000*;

- the Government's contractual obligations under State Agreement Acts tosupply plantation and native timber, covering the basis for these SAAs, what they are intended to achieve, and options for Government in delivering on these obligations;

- the FPC's obligations under the State's Forest Management Plan 2004 - 2013 and that Plan's likely successor.

- the interrelationship between the functions of the FPC and other agencies and the degree to which these are coordinated;

- existing public sector investment in plantations and farm forestry, and the extent to which the State's interests are served by maintaining a commercial agency to manage and profit from those interests;

- emerging national legislation on renewable energy and carbon sequestration;

- the potential for private sector investment in plantations and farm forestry; any matters which after the approval of the Minister are included in the review.

* This financial review was agreed in March 2009 at the time FPC received additional funding of $15million for 2008/2009 to assist in dealing with the immediate cash flow implications of (fire) damage to State-owned pine plantations and the impact of the Varanus Island explosion on log sales. This review is required before the Government will consider further funding requests as a result of the same events (fire and gas shortages). The information required will be provided by FPC's Executive Manager of Corporate Services and the review carried out by Mr. Lowe and the Executive Manager of Corporate Services at a level and precision agreed with the Department of treasury and Finance who will adopt an audit role.

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Appendix 2

Recommendations of the Statutory Review of the *Forest Pro...*

The Terms of Reference of the current review require that recommendations of the Legislative Review of 2006 be considered. The recommendations are reproduced below, each with a comment as to its continuing applicability in the context of recommendations of the current review.

Recommendation 1:

That the FPC retains responsibility for non-commercial activities and includes a full description of these in its annual Statement of Corporate Intent, identifying their cost, funding source and impact on the financial performance of the organisation.

(Comment: Agreed, but some funds will come from Consolidated Funds)

Recommendation 2:

That the FPC provide lead agency functions for the forest products industry on behalf of Government.

(Comment: Agreed)

Recommendation 3:

That the FPC continue to focus on improving profit performance, Return on Capital Employed and Return on Assets, at closer to commercial rates and establish a formal gearing policy to help guide future debt management and optimisation decisions.

(Comment: Agreed that commercial rates should be pursued and that National Competition Policy should apply; however, in balancing the three elements of the triple bottom line, the agency will be required to focus not only on profit performance)

Recommendation 4:

That the FPC closely monitor employee costs to achieve appropriate benchmarks to be set by its Board.

(Comment: Agreed)

Recommendation 5:

That the Minister consider commissioning a review of resource allocation and the internal structure of the FPC.

(Comment: Completed)

Recommendation 6:

Any further State Agreements or State Agreement Acts, and related contracts. For supply of forest products must achieve and maintain commercial rates of return.

(Comment: Agreed)

Recommendation 7:

That the Minister should consider the preparation of an industry plan for the native forest timber industry in Western Australia.

(Comment: Agreed)

Recommendation 8:

That the functions undertaken by the FPC be retained, as a separate statutory authority.

(Comment: Agreed)

Recommendation 9:

That the Board of Commissioners be retained, its appointment criteria broadened, with an additional requirement that at least one member has expertise in finance and at least one has expertise in forestry/sustainable silviculture.

(Comment: Agreed; however, it is also recommended the Board include an environmental scientist or someone with like experience and someone with experience in community/ industry development)

Recommendation 10:

That all new Board members undertake a two-stage formal induction program.

(Comment: At the discretion) of the Board

Recommendation 11:

That the FPC be made an SES organisation, to allow the Minister for Public Sector management to employ the general manager.

(Comment: It is recommended the FPC become a Department under the Public Sector Management Act)

Recommendation 12:

That the FPC and DEC establish, in consultation with the Conservation Commission, a joint system for dealing with non-compliance in ESFM standards, and objective measures of an environmental performance for forest operations.

(Comment: It is recommended working forest be vested in the Forest products Commission and that the FMP be developed by the FPC and implemented under the appropriate environmental conditions – to be negotiated by the FPC and DEC, with the Conservation Commission, or whoever should be the Government source of advice, for opinion)

Recommendation 13:

That the MOU between the DEC and the FPC be amended to provide more effective dispute resolution procedures, and a means for transparency recording the delivery of works and services by the DEC to the FPC. Eventually payments for work undertaken by DEC should reflect the work actually performed.

(Comment: Agreed should the situation regarding vesting of land and DEC undertaking work for the FMP be retained. However, it is recommended the FPC be responsible for its own forest management, with coordination where it is necessary – eg fire management)

Recommendation 14:

That the Minister require the development of a cooperative interagency strategy to manage the competing requirements of the DEC and the FPC in regards to harvest supervision and fire suppression responsibilities.

(Comment: Agreed, see above)

Recommendation 15:

That the Minister. In cooperation with the Minister for the Environment, support initiatives by the FPC and DEC to clarify their respective roles and interactions.

(Comment: Agreed)

Recommendation 16:

That the MOU between the DEC and FPC be amended to specify that access to land be subject to working arrangements which allow the FPC to have input into any proposed land use changes.

(Comment: Agreed should access arrangements be necessary, see above)

Recommendation 17:

That the *Forest Products Act 2000* be amended so that the concurrence of the Minister for Forestry is required before changes reducing the land available can go ahead.

(Comment: Agreed should the land not be vested in the FPC)

Recommendation 18:

That the *Forest Products Act 2000* be amended to confirm that the FPC can buy and sell freehold land, with appropriate checks and balances.

(Comment: Agreed)

Recommendation 19:

That the DEC transfer to the FPC the fee simple land identified in the Marketable Land Review dated 22 November 2001.

(Comment: Agreed)

Recommendation 20:

That the Minister considers legislative changes and subsequent vesting in the FPC of reserves intended for the production of forest products.

(Comment: Agreed)

Recommendation 21:

That miscellaneous and consequential amendments as detailed in Chapter 9 should proceed.

(Comment: Agreed as are still appropriate)

Recommendation 22:

That accepted recommendations in this report be implemented as soon as possible and a progress report provided to the Minister by 1 February 2008.

(Comment: Agreed the recommendations of the current review be implemented and reported on by 1 February 2010).

Appendix 3

Recommendations of the Functional Review of the Forest Products Commission October 2005

The Terms of Reference of the present review require that recommendations of the functional Review of the Forest Products Commission 2005 be considered These are reproduced below with comments.

Recommendation 1:

If the FPC is to operate as a GTE then its commercial performance must become its overriding objective

(Comment: A GTE is not recommended)

Recommendation 2:

Where the FPC undertakes "core" commercial activities but the business case for these is in part driven by social and environmental factors then the financial impact of the non-commercial components needs to be clearly identified, costed and reported.

(Comment: All activities should be reported on as they relate to the strategic/Operational plan of the agency)

Recommendation 3:

All of the FPC's non-commercial functions of CSOs, whether implicit or explicit must be identified, costed and their source of funding disclosed.

(Comment: Agreed)

Recommendation 4:

The cost of non-commercial "environmental based" plantings on agricultural land by the FPC should, for accountability and transparency purposes, be reflected against an appropriate outcome/output structure that allows for the assessment of the extent of achievement of the Government's policy priorities. For example, the Department of Agriculture (or for that matter another line agency) should contract with the FPC on a fee for service basis to plant and manage plantations established on environmental grounds.

(Comment: Agreed, however, given the recommended changes, fund would probably be directly appropriated to the FPC)

Recommendation 5:

The FPC's role in the development of Government policy should be moved from the FPC to a line agency, for example, the Department of Agriculture, to ensure that the FPC is not advantaged or disadvantaged in the pursuit of commercial activities. Similarly, responsibilities for industry development should reside with the Minister for State Development.

(Comment: This is not agreed, given the re-definition of the role of the FPC)

Recommendation 6:

Overall ministerial responsibility for the FPC, once social, environmental and industry development policy issues have been excised from the FPC, should be moved to the Minister for Government Enterprises.

(Comment: No longer relevant)

Recommendation 7:

Where government policy impacts on the FPC's commercial performance, the impact on the FPC should be clearly identified, quantified and where the FPC is not compensated for these policy impacts then clear acknowledgement needs to be made regarding the extent the decisions have on the FPC's operating result.

(Comment: Agreed)

Recommendation 8:

A concerted effort be made by all parties to ensure thatr prescribed planning and reporting deadlines are met. In this regard the FPC must involve the DTF at the earliest possible stage when formulating its SDP and SCI.

(Comment: Agreed)

Recommendation 9:

The DTF needs to be more forthright and upfront in negotiating the necessary financial and performance information it requires to manage the "owner's involvement" in the FPC.

(Comment: Agreed)

Recommendation 10:

Consideration needs to be given to the composition of the Commission with the view of strengthening the mix of the Commissions's expertise and understanding of the accountability framework under which government GTE's operate. A DTF officer would perhaps be a useful appointment to the Commission (the Board).

(Comment: Not agreed, given the recommended changes)

Recommendation 11:

Consideration be given to having the FPC's SDP and SCI locked away and approved by all parties concurrently with the budget information.

(Comment: "All" parties will carry a different meaning should the recommendations of this review be accepted)

Recommendation 12:

The FPC and CALM to work harder at reaching agreement on each others respective responsibilities and any fee for service arrangements. The responsible CEOs must be compelled to make the relationship an effective one with Resource and Performance Agreements entered into with respective Ministers used to require the CEOs to amicably resolve their business relationships.

(Comment: Agreed, but the nature of any Agreement will be quite different and hopefully less vexacious)

Recommendation 13:

Where agreement cannot be reached the matter be referred to the Treasurer to seek independent expert advice on the matter and any costs associated with the expert advice to be borne by either the FPC oir CALM as determined by the arbitrator.

(Comment: No longer likely to be necessary)

Recommendation 14:

Where the FPC work is required to be undertaken by CALM, in accordance with an agreed work plan, but is not performed by CALM due to some unforeseen circumstances (ie fire fighting responsibilities diverting resources away from the FPC work plan) then CALM should, given that the FPC is and should not be obliged to pay for work not performed, look to prioritise its own existing resource allocations to accommodate the revenue shortfall.

(Comment: No longer relevant)

Recommendation 15:

Consistent with the requirements of section 71 of the *Forest Products Act 2000* a comprehensive review of the *Forest Products Act 2000* be undertaken by the Minister for Agriculture, Forestry and Fisheries in close consultation with the Department of Treasury and Finance with the review being undertaken as soon as possible.

(No longer relevant)

Submissions and consultation to the review of the Forest Products Commission 2009

Written submissions

The Forest Products Commission

Board, Forest Products Commission

Department of Agriculture and Food

Department of the Environment and Conservation

Conservation Commission of Western Australia

Department for Planning and Infrastructure

Synergy

Consultation

Department of the Premier and Cabinet

Department of Treasury and Finance

Department of Water

Water Corporation of WA

The Wilderness Society of WA Inc.

The Conservation Council of WA Inc.

The Forest Alliance of WA

VicForests

Gunns Limited

Whittakers Timber Products

Petroleum industry company

Nannup Timber Production

Great Southern Timber Corporation

Wesbeam

Western Poles Co

Wespine Industries P/L

Forest Industry Federation of WA