



STRUCTURAL REVIEW OF BC TIMBER SALES

**DISCUSSION PAPER on the KEY CHARACTERISTICS of an
EFFECTIVE, EFFICIENT BCTS ORGANIZATION**

July 31, 2006

**Prepared by
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Howard Saunders, H & W SAUNDERS ASSOCIATES LTD.**

1. Introduction

The Ministry of Forests and Range (MOFR) has initiated a review to determine if the current organizational structure of BC Timber Sales (BCTS) most effectively addresses its mandate, and to recommend any needed changes.

The focus of this Discussion Paper is on the critical features or characteristics of BCTS as an organization that would affect the attainment of BCTS' mandate. This Discussion Paper reviews several key themes that were discussed at a June 29, 2006 workshop with a wide range of industry stakeholders and with staff from BCTS and the Operations Division of the MOFR. The meeting notes from that workshop are available on the BCTS public website.

The workshop participants provided input into these characteristics, discussed alternative structural models at a high level, and made numerous recommendations regarding how BCTS should conduct its business within any structural model. This broader input will be incorporated into a second Discussion Paper as referenced below.

Public and stakeholder comment on this topic, and on the questions raised in the paper, is encouraged.

2. Terms of Reference for the Structural Review

The complete Terms of Reference for this Structural Review and other background material can be viewed on the BCTS website:

<http://www.for.gov.bc.ca/bcts/about/structuralreview.htm>

This review is co-chaired by Howard Saunders, an external consultant, and Dave Peterson, Assistant Deputy Minister, BCTS.

- It is to use, as a starting point, the current mandate of BCTS, as articulated by its Vision, Mission, and Strategic Goals and Objectives;
- The review is also to assume that the running of BCTS will remain a function of government for the foreseeable future.

The Co-chairs will make recommendations to the Minister of Forests and Range, through the Deputy Minister.

3. Consultation Process

The stakeholder groups represented on the Timber Sales Advisory Council (TSAC) are the primary non-government contacts for this review. As BCTS program participants and ongoing advisors, the TSAC members are already well familiar with the strengths and weaknesses of the present BCTS model, and well positioned to provide input into this review.

Representatives from BCTS, and from the MOFR Operations Division, are engaged in this review alongside the TSAC stakeholders.

Other interested parties are invited to provide written comments.

In addition to the Terms of Reference, regular updates are being posted on the BCTS public website, and include the following products to date:

- The Current Mandate Statements, including Vision, Mission, Strategic Goals and Objectives;
- This Discussion Paper on the Key Characteristics of an Effective, Efficient BCTS Organization; and
- The Summary Notes from the June 29, 2006 Stakeholder Workshop.

Written submissions should be submitted to the address shown below, where they will be collected and forwarded to the co-chairs. Electronic format is preferred.

Comments on this paper are requested by August 15, 2006 if possible, and no later than August 31, 2006.

Email to:

Forests.BCTimberSalesHQOffice@gov.bc.ca

Subject: BCTS Structural Review

Or mail to:

BCTS Structural Review
Attention: Nicole Jee, Office Supervisor
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4. Background:

In 1995, the BC government decided to revise the focus of the existing Small Business Program within the Ministry of Forests, and examined a number of alternative structures that might accomplish that objective.

Between 1995 and today, the mandate of the Small Business Program evolved substantially into the current BC Timber Sales program that was established in 2003. During this period, the structure was modified somewhat, and was examined and reviewed a number of times.

This review will build on the information gathered previously.

In 2006, the BC Competition Council presented to the Premier the reports from its Forest Industry Advisory Committees and made a number of recommendations to the Premier, including one regarding delivery models for BCTS.

- The Wood Products Industry Advisory Committee recommended that government “*carry out a third party independent review of BCTS in collaboration with the recently appointed new CEO (and) consider if a market responsive timber pricing system can be achieved through the BCTS, or a similar organization with a corporatized structure, or recommend if a form of privatization should be considered.*”
- In turn, the Competition Council recommended that government take “*steps to reduce and eventually eliminate its role as operator and seller of timber produced from the Crown timber supply.*”

The alternative structures that have been examined previously fall along a continuum from a program fully integrated within the MOFR organization (the old SBFEP model) to a program fully arms-length from government, delivered by the private sector. The Terms of Reference for this review assume that the running of BCTS will remain a function of government for the foreseeable future, although the question as to whether the BCTS function should be moved out of government in the long term, will be raised and examined.

5. Structural Review Process

At issue is the question of whether a different type of structure for BCTS would better address the elements of its mandate. The objective is not change for change’s sake, but to determine if there is a “business case” for change. That is, if change will allow BCTS to better fulfill its mandate. Accordingly, the possibilities for change range from an entirely new structure, through to improving the efficiency and effectiveness of BCTS within its current structure.

Feedback from stakeholders has identified that there is not a universal understanding of the term “BCTS structure”, in the context of what this structural review will be examining. The fundamental purpose of this review is to answer the question: *What is the best TYPE of organizational structure for BCTS, given its mandate?* As a result of the review, recommendations will be made as to whether BCTS should remain a division within the MOFR, a special operating agency, a Crown Corporation, a private company, etc. In the context of this review, “structural review” is synonymous with examining the governance model for BCTS, or examining alternative service delivery models for BCTS. On the other hand, this review will not include an examination of the detailed internal workings and relationships of BCTS, or make recommendations on issues such as office configurations, whether BCTS should have a Regional presence in addition to its Headquarters and its Business Offices, the desired degree of consistency between offices, etc. These latter issues have been, and will continue to be, addressed through periodic internal organizational reviews of BCTS.

As noted earlier, the procedures for this structural review are detailed in the Terms of Reference. This review starts from the documented mandate of the existing BCTS program, and then identifies the critical organizational features or characteristics that could affect the attainment of that mandate. This Discussion Paper represents the initial findings of the co-chairs on this topic, and is intended to solicit further input on these characteristics.

Once the key characteristics have been identified, the current and alternative structures will be evaluated in light of those features and of the implications of moving to any alternative. The co-chairs will then recommend any changes or improvements needed to the BCTS structural model, or recommend improvements needed within the current structure. These recommendations will be put into a second Discussion Paper which will be posted on the website and will be taken back to the stakeholders’ group for discussion in a workshop planned for September, 2006.

By September 30, 2006, after reviewing the input from interested parties and the feedback from the workshop, the co-chairs will make final recommendations to the Minister.

6. Themes and Characteristics

Several themes were identified initially by the co-chairs and the following questions around each theme were posed to the workshop participants.

Initial Themes

- i. Clear Goals and Objectives (clarity and completeness of mandate)
 - Do the current goals and objectives need to be clarified or strengthened?
 - What else, if anything, should be added to the current goals or objectives?

- ii. Timber Sales Program that Supports Market Pricing System
 - What needs to be included to be ensure use for Market Pricing System?

- What latitude should BCTS have (not have) in designing their sales program?
- iii. Costing Program Applicable to Market Pricing System
 - How can BCTS have a relevant cost structure comparable to licensees?
 - How might BCTS' cost structure differ from that of a licensee?
- iv. Effective and High Performing Organizational Structure
 - How can BCTS improve their internal structure?
 - How can the organization be competitive and efficient?
- v. Business Acumen
 - How important is business acumen among BCTS staff?
 - Can business acumen be fostered in the setting of a government agency?
 - What sort of organizational structure would be necessary to foster business acumen?

The workshop discussion proposed three additional themes. Upon further consideration, the co-chairs concluded that these eight potential themes could be amalgamated into the following four, with their associated more-detailed characteristics.

Questions are raised in this paper around many of these draft characteristics. While this Discussion Paper is intentionally focused on these characteristics, in the interest of setting the stage for the next phase of this review the co-chairs often raise the question of whether a characteristic is linked particularly to the choice of structures.

Theme 1: Clear Goals and Objectives

BCTS currently addresses 4 Strategic Goals that are documented in the publicly-available BCTS Service Plan. Each Goal is noted in italics below.

Characteristics:

A. Goals should be clearly understandable to all

- a) Goal 1 "*Provide a credible reference point for costs and pricing of timber harvest from public land in BC*"
Given the fundamental role of BCTS to provide data for the Market Pricing System, that will in turn determine the stumpage for the remaining crown timber, clearly this is the primary Goal and the other Goals must be consistent with it.
- b) Goal 2 "*Optimize net revenue to the province, within the parameters dictated by our benchmarking mandate and safe and sound forest management practices*"
While there appears to be support for the intent of this Goal, its wording may require considerable revision to clarify the expression "*optimize net revenue*" as workshop participants had

varying interpretations of it. For example, should "net revenue" be only that generated by BCTS or should it include government revenue from other sources? Should BCTS strive to maximize the value generated by each individual Timber Sale, but not necessarily by the sales program as a whole?

Is a goal like this a critical requirement to ensure that BCTS acts so that its competitive timber auctions generate fair market value for the public timber resource?

It was observed that the benchmarking mandate of BCTS may limit its ability to pursue creative options, such as lump sum timber sales, that could reduce costs and increase net revenue.

c) Goal 3 "*Provide opportunities for customers to purchase timber in an open and competitive market*"

The wording of this Goal may also require considerable revision to ensure its meaning is clear.

This wording appears to limit BCTS to providing opportunities only within the context of an open and competitive market, although currently BCTS administers a portion of the sales for Category 2 registrants only, where competition is limited to only a certain category of bidders.

In addition, the phrase "*provide opportunities for customers*", could be interpreted to direct BCTS to ensure it meets the needs of all potential customers, which could create conflicts with achieving Goal 1.

These thoughts raise the question of BCTS' role in such "social forestry" programs and the need for clear direction regarding the relationship of BCTS to the other broader objectives and responsibilities of the MOFR. (see below)

d) Goal 4 "*BC Timber Sales is a high performing organization with skilled, motivated and proud people*"

There is widespread support for this Goal and it does not appear to require clarification.

While there is a recognized need for clarity of goals, it is not obvious whether these concerns hold implications for the appropriate organizational structure for BCTS. Does the BCTS structure affect these issues?

B. Clear distinction between the mandate and responsibilities of BCTS and of the MOFR

There was not a consensus amongst the workshop participants on this topic, particularly on whether BCTS should or should not incorporate the MOFR objectives around the Value-Added industry as reflected in the current Category 2 “protected pool”. Other issues to consider here include:

- a) Is there a need for a clear separation (physical and structural) between BCTS and the MOFR Operations Division?
- b) How to clarify the roles of BCTS staff versus Operations Division’s Compliance & Enforcement staff regarding supervising/overseeing timber sales licences?
- c) How to ensure that BCTS is seen to be operating independently i.e., the MOFR treats BCTS the same as a licensee as far as plan approvals, etc?
- d) Is there a trade-off between the symbiosis with government and the independence of BCTS?

If separation is important, what degree of separation is required: distinct mandates; distinct identities (vehicles and logos); physical office separation; different organizations; etc? Can the desired degree of separation and independence be achieved by anything short of complete privatization, i.e., becoming nearly the same as any other private sector licensee?

C. Consistent interpretation and transparent application of objectives

There was general acceptance for the following principles:

- a) BCTS must ensure that policies and procedures reflect the intent of the goals and objectives and are understood by staff, and should test for staff awareness.
- b) BCTS must ensure that goals/objectives/policies/procedures are applied transparently and consistently across regions and among customers.
- c) BCTS must ensure that performance measures are derived that directly relate to the Strategic Goals, and are used to monitor and direct BCTS activities.

How could an alternative structure make BCTS more successful in addressing these issues?

Theme 2: A Timber Sales Program that Supports the Market Pricing System

The Market Pricing System (MPS) is used to set the upset price¹ for competitively bid timber and to set the price for timber harvested under long term tenures. The system uses equations determined from sales data collected by BCTS from competitively bid sales. Sales made to Category 2 participants (the “protected pool”) are not considered competitively bid due to the restriction on who can bid, and are excluded in deriving the equations.

The MPS system is administered by MOFR’s Revenue Branch, with the assistance of Economics and Trade Branch who conduct the required statistical analyses and tests. While the issues like data robustness, transparency, data quality, and sale administration are the responsibility of BCTS, other issues that relate to the statistical requirements or the administration of MPS are the responsibility of these other branches.

Workshop participants identified the following characteristics as necessary to support the Market Pricing System.

Characteristics:

A. Robust sales data

Stakeholders agreed on certain characteristics that are relevant to BCTS' mandate:

- a) Ensure credibility of auction data vis-à-vis tests of an open and competitive market.
- b) Ensure variety of sale sizes and other sale characteristics
- c) Ensure sales cover the range of timber types/profile and harvest systems
- d) Ensure a system that encourages many bidders and a wide spectrum of buyers and sellers, while establishing qualification criteria so that qualified bidders are competent and responsible enough to bid reasonably on, and harvest, Crown timber without jeopardizing the resource, BCTS' net revenues, or the safety of workers and the public.
- e) Ensure that the timing of sales over the course of the year or over a market cycle meets client needs and optimizes net revenue.

To qualify as "robust", the important issue is that the timber sales volume should be close to 20% of the annual harvest (the objective that government has set for ensuring credible reference points), and should cover the range of conditions experienced by the major licensees. This implies some stability of annual harvests, but strict adherence to the AAC target and a total lack of responsiveness to market cycles would likely be unsatisfactory both to clients and as a credible reference point.

It is not clear that one structure would be superior to another in terms of

¹ The upset price is the price below which bids will not be accepted. An upset equal to 70% of the expected winning bid predicted by the equation has generally been used, but lower upsets may be used if there is reason to expect that the timber would not sell at 70% or more of the predicted winning bid.

bidder qualification and enforcement, apart from the possibility of political intervention on behalf of unqualified bidders, at one extreme and the possibility of more arbitrary decisions if the program were administered by a private company, e.g., as a private landowner might. As long as the timber is a public resource, proper administration of clear and fairly enforced policies and guidelines would be required to give the public fair access to the opportunity, so that the type of organizational structure might make little or no difference.

B. Transparency

Stakeholders agreed that it is critical that the data generation and collection processes be fully transparent. Considerations include:

- a) Ensure all parties, including BCTS staff, are informed on what data is used in the Market Pricing System, and how it is used.
- b) Ensure that sale procedures and reporting systems are open and understandable.

C. Data quality

Stakeholders provided the following advice. While these really are recommendations around BCTS procedures, they were included here as they are considered critical components of the data generation process.

- a) Analyze sales data to identify market and bidding manipulation and deal with it appropriately and quickly.
- b) Ensure that all of the required data for the sale are properly and accurately recorded and that none of the items are missing.

Workshop participants also provided strong advice back to the other MOFR branches who are users of the BCTS data, including recommending that data points not be used in updating the expected winning bid equation until all parameters have been met, e.g., stumpage and waste billings have been paid, and the sale fully logged within its term. Much of this discussion does not relate directly to BCTS' mandate or structure, although it does point out the critical linkage between BCTS activities and those of the other branches of the MOFR.

Theme 3: Costing Program Applicable to Market Pricing System

It is intended that BCTS program costs will be used instead of licensee costs in the MPS system in adjusting for the costs borne by major tenure holders on their licences but borne by BCTS instead of the bidder in the BCTS sales program. The issues are in knowing if BCTS costs are analogous to those licensees bear and in ensuring that reporting systems are comparable so that when it is

necessary to use licensee costs, both the MOFR and industry are confident that there is no overlapping or duplication of costs in the relevant categories.

Characteristics:

A. Transparency and symmetry

- a) Strive to achieve BCTS symmetry of obligations and comparability of costs with major licensees' responsibilities regarding stewardship, safety, certification, etc.
- b) A stable land base for operations may be an essential element in achieving symmetry with licensee costs and obligations
- c) Ensure transparency between industry and BCTS cost categories and reporting so that costs can be compared e.g. road costs tied to specific sales; reporting at same scales, overhead etc.
- d) Ensure equitable application of rules by the MOFR (between BCTS and major licensees)

B. Contracting

- a) Some licensees are required by Bill 13 to enter into long term contracts with contract loggers on a portion of their harvest. Licensees argue that this results in higher costs than where the requirement does not exist, and that such costs need to be recognized as tenure obligation adjustments that are not incurred by BCTS bidders. There is little agreement on the existence or the magnitude of such differences, but the issue raises questions about symmetry.
- b) Contracting practices must be comparable to industry, i.e., there is a perception that BCTS must accept the lowest bid for contracts such as road building and silviculture even if this may not produce the best value for money, whereas licensees are liable for contractor failures and may decide not to accept low bids. There is a need to ensure understanding of differences and impacts of government policy-based restrictions around contracting practices, if BCTS costs will eventually be used instead of licensee costs for the tenure obligation adjustments.

C. Overhead

- a) Ensure overhead cost categories are clearly defined so that BCTS costs can be accurately compared to industry.
- b) Clarify how human resource management practices in government affect overhead costs, so that the merits of different structural alternatives for BCTS may be assessed.
- c) Whereas licensees incur overhead costs in the tracking and payment of stumpage expenses, BCTS may incur overhead costs in supporting the stumpage revenue collection function. BCTS needs to ensure that any revenue collection costs are identified separately, and industry overhead surveys must identify those

costs which are not borne by BCTS.

Given the significant difference between the mandate of BCTS and that of a forest industry company, it is difficult to see that the overhead structures will ever be symmetrical or directly comparable. It is questionable whether BCTS' overhead costs could ever be considered to approximate the average overhead costs of the licensees. Should BCTS' overhead just be considered one piece of input into the overhead cost considerations within MPS?

Some of the foregoing items and issues raised by stakeholders deal mainly with what needs to be done instead of how (they are operating issues rather than issues that bear on structure). The other characteristics speak to two issues: BCTS' involvement as a business entity operating in public view on a public resource, and the separation of BCTS from the rest of the MOFR so that they can operate more like a licensee e.g., having a stable land base (chart area) on which to plan operations and accept stewardship obligations, similar to licensees.

How far along the spectrum of structural change does BCTS need to move, if at all, to address these issues?

Theme 4: Effective and High Performing Organizational Structure

Stakeholders had considerable interest in ensuring that BCTS reflected the key characteristics of an effective and high performing organization.

Characteristics:

A. Appropriate, effective staffing

Stakeholders were unanimous that BCTS staffing procedures were critical to the success of the organization. Issues to consider include:

- a) Ensure business units and personnel have the right level of experience and expertise
- b) Ensure diversity of expertise, i.e., accountants, foresters, MBAs.
- c) Ensure personnel practices are competitive and flexible, i.e., don't limit to in-service competitions; provide competitive compensation and flexible hours of work, and reward high performance and correct under-performance.

Can the desired degree of expertise and initiative, and the needed operational flexibility be effectively attained within a government

department? If not, why not, and how far from that does the structure have to move to achieve the desired characteristics?

B. Appropriate support services and processes

Stakeholders were unanimous that internal BCTS procedures, processes, systems and support services were critical to the success of the organization. Given the lack of stakeholder knowledge on the details of how BCTS is organized and run, it was difficult for them to provide specific advice. Input on this topic will need to be gathered from BCTS/MOFR staff.

Can the desired efficiencies and the needed operational flexibility be attained within a government department? If not, why not, and how far from that does the structure have to move to achieve the desired characteristics?

C. Business acumen

Stakeholders were unanimous that it was critical that BCTS as a whole, and BCTS staff as individuals, posed a high degree of business acumen. This is not often thought of as a requirement of government departments. Issues raised include:

- a) The organization needs to understand its market and what drives it, and be responsive to market opportunities.
- b) Sales offered should be selected and packaged to address market needs, recognizing that the mandate and symmetry with licensee obligations oblige BCTS to log the timber profile
- c) There must be a business case behind BCTS' activities to ensure the organization is cost conscious, cost effective, competitive, and understanding of cause and effect. The business case may be that the timber sales make sense from both BCTS and registrant point of view, or that the activities are necessary to support the timber pricing mandate and the obligation to log the timber profile on the timber harvesting land base. That is, BCTS cannot offer only timber which is in high demand and ignore less desirable components of the timber profile that contribute to the AAC.

Can business acumen be maintained within a government organization, or is some degree of separation from government departments required? If not, why not, and how far from that does the structure have to move to achieve the desired characteristics?

D. Regular communication with its customers and other

An effective communications program would include frequent, timely and two way communication with stakeholder groups; clearly identified contact personnel and designated communicators; and, identification of the various stakeholder groups whose need must be addressed (customers,

stakeholders

other forest industry participants, BC politicians and public, US trade interests, etc.)

Is the type of organization of any particular significance in the attainment of these characteristics, or are these primarily personnel issues within the structure?

7. Concluding Comments

This Discussion Paper reflects the breadth and depth of the comments received from the workshop participants, in recommending what the key characteristics should be, even if there was not always complete agreement, or if the identified characteristics were not directly linked to a particular organizational structure.

The co-chairs invite any interested parties to comment on any of the above material or questions posed in the paper, in the context of what organizational characteristics are critical to the efficient delivery of the BCTS mandate.

Comments on this paper are requested by August 15, 2006 if possible, and no later than August 31, 2006.

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