

## Chapter 4

### Section 4.05

Ministry of Natural Resources

# Forest Management Program

Follow-up to VFM Section 3.05, *2011 Annual Report*

## Background

Ontario's forests cover more than 700,000 square kilometres or about two-thirds of the province. More than 80% of the forests are on Crown land, and their management—harvesting, renewal, maintenance and so on—is governed mainly by the *Crown Forest Sustainability Act, 1994* (CFSA). The CFSA is designed to provide for the long-term sustainability of Ontario's Crown forests and their management in such a way that they meet the social, economic and environmental needs of present and future generations. In addition, the Ministry of Natural Resources (MNR) has standing authority under Ontario's *Environmental Assessment Act* regarding recurring forest management activities on Crown land, subject to conditions to which MNR must adhere.

Ontario's forest industry is an important source of employment in the province, especially in northern communities. Employment within the industry is estimated at 142,000 jobs. According to Statistics Canada, the value of Ontario's forestry sector products—that is, the province's pulp and paper, sawmill, and engineered wood and value-added wood product—is estimated to be approximately \$10.5 billion per year.

In our *2011 Annual Report*, we noted that the industry had experienced a significant decline due mainly to the increase in the value of the Canadian dollar and the economic downturn in the United States, which affected demand for forest products made in Ontario. As a result, many mills in the province had closed, either permanently or temporarily, resulting in a reduction in timber harvest levels and associated forest management activities.

Most forest management activities on Crown land occur in an area of the province that is about 365,000 square kilometres known as the Area of the Undertaking. Forest management activities are generally not approved north of the Area of the Undertaking, where access is limited. Most of the land south of the area is privately owned. Productive forest within the Area of the Undertaking covers about 262,000 square kilometres; only about 190,000 square kilometres of this area are eligible for forest management activities, with the rest comprising provincial parks, private lands and areas where forest management activities cannot reasonably take place due to the terrain.

At the time of our *2011 Annual Report* and our follow-up, the Area of the Undertaking was divided into 41 Forest Management Units. Thirty-three of the 41 Forest Management Units (38 in 2011) were managed by forest management companies operating under a Sustainable Forest Licence.

Under a Sustainable Forest Licence, which may be granted for up to 20 years, the licence holder is responsible for preparing a Forest Management Plan and implementing the plan by building access roads, harvesting trees, renewing/maintaining the forest, monitoring its forest management activities, and reporting the results of its monitoring to the province. The remaining eight Forest Management Units (three in 2011) were managed by the Crown. The province also grants Forest Resource Licences, which allow an individual or company to harvest in a Forest Management Unit. Before a Forest Resource Licence can be issued, the individual or company must come to an agreement with the holder of the Sustainable Forest Licence. The Forest Resource Licence holder will generally not be responsible for any forest renewal/maintenance activities subsequent to harvesting, because this responsibility typically remains with the Sustainable Forest Licence holder. The province has granted nearly 3,400 Forest Resource Licences (nearly 4,000 in 2011), which have a maximum term of five years.

Under the CFSA, licensed forest management companies are responsible for overall forest sustainability planning and for carrying out all key forest management activities, including harvesting and forest renewal, on behalf of the Crown. The province's role in ensuring the sustainability of Crown forests has increasingly become one of overseeing the activities of the private-sector forest management companies.

Overall, we concluded in our *2011 Annual Report* that improvements are needed if the Ministry of Natural Resources and the Ministry of Northern Development, Mines and Forestry (MNDMF) were to have adequate assurance that the key objective of the CFSA—to provide for the long-term sustainability of Ontario's Crown forests—was being achieved.

Our specific observations were as follows:

- The province considered a one-hectare harvest block to have regenerated successfully if it was stocked with a minimum of 1,000 trees (that is, 40% of what the harvest block

can accommodate). Harvest blocks were also held to a silviculture (the practice of controlling the establishment, growth, composition, health, and quality of forests to meet diverse needs and values) success standard, which is a measure of whether the appropriate or preferred trees have grown back. In the 2008/09 fiscal year, the latest period for which information was available at the time of our audit, we noted that about a third of the licensed forest management companies had not reported the results of their forest management activities, and MNR had not followed up with these companies. The two-thirds that had reported indicated that although 93% of the total area assessed by the companies had met the province's minimum 40% stocking standard, only 51% of the total area assessed had achieved silviculture success.

- MNR's 40% stocking standard had not changed since the 1970s. Several other jurisdictions in Canada hold the industry to higher standards. In fact, we noted that one MNR region, on its own initiative, held companies managing Crown forests in its jurisdiction to a higher stocking standard.
- Before planting, seeding or even natural regeneration can take place, it is often necessary to prepare a site to allow for regeneration to take place under the best possible conditions, thereby increasing the likelihood of success. It is also often necessary to subsequently tend the site, usually by spraying to kill off competing vegetation, to further increase the likelihood of regeneration success. On average, between the 2004/05 and 2008/09 fiscal years (the latest periods for which information was available at the time of our initial audit), only about a third of the area targeted for regeneration either naturally or by direct seeding or planting was prepared and/or subsequently tended. Moreover, the average decreased over that five-year period. In accordance with the CFSA, all Crown

forests are subjected to an Independent Forest Audit once every five years. Independent Forest Audit reports completed in the 2008 and 2009 calendar years expressed concern about inadequate site preparation or about non-existent or inadequate tending practices that were leading to reductions in growth, yield and stand densities, as well as to an increase in the time required for stands to reach free-to-grow status (meaning that the trees are free of insects, diseases and high levels of competing vegetation).

- We noted that Forest Management Plans had been completed in accordance with the requirements of the CFSA and reviewed and approved by MNR staff. However, MNR had not ensured that the most accurate and up-to-date information on forest composition, wildlife habitat and the protection of these habitats was made available at the time the plans were prepared.
- With respect to the province's monitoring of the forest industry, we noted the following:
  - MNR did not maintain a complete list of active harvest blocks in its compliance system to ensure that all harvest blocks could be identified for possible inspection, and not all of MNR's district offices used a risk-based approach for selecting blocks for inspections. Where problems were noted, repeat offenders often did not receive appropriate remedies such as a penalty or a stop-work order.
  - The forest industry is required to report its renewal activities annually to MNR. To verify the accuracy of the reporting, MNR implemented a Silviculture Effectiveness Monitoring program. However, its district offices were not completing many of the required "core tasks" in the program. Where problems were noted, little follow-up action was being taken.
  - We noted that a good process was in place to select the team that conducted the

Independent Forest Audits, but that deficiencies detected during such audits were not being addressed in some cases.

- The average annual harvest between 2004/05 and 2008/09 had been only about 63% of what was planned, and had decreased from almost 80% of what was planned in the 2004/05 fiscal year to about 40% of what was planned in the 2008/09 fiscal year. The shortfall was usually due to existing licensees with sole rights to harvest Crown timber not having a market for the timber. There were indications that other companies that did not have access to timber in Ontario's Crown forests could market Ontario wood. A November 2009 competition for unused Crown wood initiated by MNDMF resulted in the allocation of approximately 5.5 million cubic metres of timber that otherwise would not have been harvested. About 25% of the winning proponents were new mills that planned to invest in the province as a result of this competition. At the time of our audit, MNDMF had no plans to hold similar competitions in the near future. In fact, we noted that MNDMF did not monitor whether there is an excess supply of Crown wood that could be reallocated to others who might be able to market the timber.
- Measures and controls did not fully ensure that Crown forest revenue was appropriately calculated and received on a timely basis and that trusts established to fund forest renewal expenditures incurred by forest management companies were administered and funded adequately.

We also noted that MNR could enhance the usefulness of the information presented in its annual report on forest management by comparing actual levels of key activities—such as harvesting, regeneration (whether occurring naturally or assisted by planting or seeding), site preparation and tending—to planned levels and providing explanations for significant variances.

We made a number of recommendations for improvement and received commitments from MNR and MNDMF that they would take action to address our concerns. (At the time of our audit both ministries were responsible for the management of Ontario's Crown forests. However, in October 2011 that responsibility fully reverted to MNR.)

## Status of Action Taken on Recommendations

According to the information provided to us by MNR, some progress has been made in addressing several of the recommendations we made in our *2011 Annual Report*. For example, it had taken steps to better ensure the sustainability of the Forest Renewal and Forest Futures trusts, as well as to better manage the use of available wood supplies. However, others will require more time to be fully addressed. For example, our recommendations to better ensure the successful regeneration of Crown forests after harvesting have yet to be fully addressed. At the time of our follow-up, MNR was still in the midst of reviewing its current regeneration standards and hoped to finish its review and develop a revised direction, subject to approval, by April 2014.

The status of actions taken on each of our recommendations was as follows.

### SUSTAINABLE FOREST MANAGEMENT

#### Forest Renewal

##### Recommendation 1

*To better ensure that the province's Crown forests are successfully regenerated after harvesting, the Ministry of Natural Resources should:*

- *follow up with those forest management companies that have not regularly reported on the results of their forest management activities in*

*meeting the province's stocking and silviculture standards; and*

- *conduct scientific studies and research into practices in other jurisdictions to ensure that the stocking standard is adequate to ensure that forest management companies are held to a regeneration standard that will successfully renew harvested areas with the desired species.*

*Where forest management companies opt for lower-end regeneration activities, MNR should, as part of its review of Forest Management Plans, ensure that there is adequate justification for these less-expensive treatments and assess whether the treatments will achieve planned renewal objectives.*

#### Status

In our 2011 audit, we recommended that MNR follow up with those forest management companies that have not regularly reported on the results of their forest management activities. Forest management companies are required to report to MNR the results of assessments completed on areas harvested seven to 10 years previously within Forest Management Units and whether these areas have achieved the province's stocking and silviculture standards. In the 2008/09 fiscal year (the latest year for which information was available at the time of our 2011 audit), we noted that about a third of the forest management companies had not reported the results of their forest management activities in 2008/09, and MNR had not followed up with these companies. In its response to our 2011 recommendation MNR indicated that forest management companies are required to report annually to MNR on the results of any assessments that they have completed, but are not required to conduct assessments annually; instead, they may accumulate larger harvest blocks for assessment once every few years. Because of this, it is expected that not all companies will report each year. MNR agreed to follow up with any companies that have not reported regularly to ensure that they have a reasonable rationale for not doing so. In 2010/11 and 2011/12, MNR did follow up with forest

management companies that had not reported by sending letters reminding them of their reporting requirements, including noting where no assessments had been undertaken. The Ministry informed us that all 2010/11 and 2011/12 annual reports had been submitted.

In regard to our recommendation that the Ministry research practices in other jurisdictions to ensure that its regeneration standards are adequate, MNR began in 2012 to review and develop guidelines for improving regeneration standards by commissioning studies that evaluated its current methodologies for assessing regeneration success, and compared standards and approaches used in other provinces. MNR hoped to finish this review and develop revised direction, subject to approval, by April 1, 2014.

MNR also informed us that it continues to monitor whether forest management companies are achieving planned objectives by opting for lower-end regeneration activities such as natural regeneration (instead of seeding or direct planting) through its Silviculture Effectiveness Monitoring program. This program consists of a number of “core tasks” that MNR’s district offices are to carry out to assess industry renewal efforts. In 2010/11 and 2011/12, the program was undertaken on 80% of the forest units. However, at the time of our follow-up, MNR was still analyzing the data.

## Forest Management Plans

### Recommendation 2

*In order that Forest Management Plans meet their objectives in ensuring the future sustainability of Crown forests, the Ministry of Natural Resources should ensure that accurate and up-to-date information on forest composition and wildlife habitat and the protection of these habitats is made available at the time the plans are prepared. MNR should also update any silviculture guides used in forest management planning on a timelier basis.*

### Status

At the time of our 2011 audit, MNR intended to have updated its Forest Resource Inventory, which among other things provides information on the composition, age, height and stocking of individual trees within a forest, by 2014. At the time of our follow-up, MNR informed us it was still on target to meet this timeline.

Also, at the time of our 2011 audit, MNR had determined that 42 endangered and threatened species were dependent on the province’s Crown forests and likely to be affected by forest management operations, and therefore needed protection. We noted that for six of these species, no provincial prescriptions (that is, documents specifying the way the species should be protected—for example, by setting up buffer zones between the species and forest management operations) had been developed. At the time of our follow-up, MNR informed us that it had finalized habitat regulations for five of these endangered, forest-dependent species and was consulting on habitat regulation proposals for the remaining species.

Finally, in 2005, MNR had reviewed its silviculture guides used by the forest industry when preparing Forest Management Plans and concluded that all but one required revision. At the time of our 2011 audit, MNR was still revising the guides, which prompted us to recommend that MNR update them on a timelier basis. At the time of our follow-up, MNR had still not finished the work and indicated it was on track to be completed by fall 2013.

## Monitoring

### Inspection and Enforcement

#### Recommendation 3

*To improve its monitoring of forest management companies’ operations for compliance with applicable legislation, regulations, and policies, the Ministry of Natural Resources should:*

- *review its current compliance database to ensure that appropriate linkages are made to*

*complete harvest block listings so that all harvest blocks can be identified for possible inspection; and*

- *provide guidance to its district offices in adopting a risk-based approach for selecting blocks for inspection.*

*MNR should also ensure that its district offices are more consistent and effective in the use of appropriate remedies to encourage compliance, especially for repeat offenders.*

### Status

In Ontario, the forest industry is required to inspect all harvest blocks and report to MNR all suspected incidents of non-compliance. MNR then investigates and determines the appropriate remedial action for any non-compliance.

In our *2011 Annual Report*, we noted that MNR's database did not contain a complete listing of active harvest blocks and listed only those that had been inspected by forest management companies. As a result, MNR could not readily compare all active harvest blocks with those that had been inspected and follow up with companies regarding uninspected blocks. This prompted us to recommend that MNR review the completeness of its compliance database to ensure that all harvest blocks can be identified for possible inspection. At the time of our follow-up, MNR had completed such a review to determine whether making appropriate linkages with harvest block data in Forest Management Plans would be warranted; it determined that the system change would cost approximately \$300,000 and take roughly two years to complete. MNR concluded that since the harvest block data is available in Forest Management Plans and Annual Work Schedules, ensuring the completeness of this data in its compliance database was not warranted. In this regard, we note that unless MNR takes the time to compare all harvest blocks listed in each individual Forest Management Plan with those that have been inspected by the forest industry, it will not be able to attain the necessary assurance that the forest industry has inspected all harvest blocks.

With respect to our recommendation to MNR to provide guidance to its district offices in adopting a risk-based approach for selecting harvest blocks for inspection, MNR had developed draft guidance on risk-based planning for consideration in the monitoring of industry forest operations. The guidance included direction on determining how risk is to be assessed, and managed. At the time of our follow-up, MNR informed us that the guidance had been finalized and will be sent to forest managers for implementation starting April 1, 2014.

In our *2011 Annual Report*, we noted that repeat offenders often received verbal or written warnings instead of remedies that might act as more of a deterrent—such as an administrative penalty or cancellation of the forestry licence in serious cases. This prompted us to recommend that the Ministry should ensure its district offices are more consistent and effective in the use of appropriate remedies to encourage compliance, especially for repeat offenders. At the time of our follow-up, MNR had updated its Forest Compliance Handbook to provide more clarity to district offices in this area. For instance, the Ministry combined two previously separate procedures on determining and applying remedies into one, which, according to the Ministry, reduced the complexity of the direction provided to district offices. The Ministry hoped this would improve the consistency in the application of remedies among district offices. A new procedure was also implemented on April 1, 2012, to guide field staff in the appropriate use of written warnings as a remedy.

### Silviculture Effectiveness Monitoring Program Recommendation 4

*To ensure that the Silviculture Effectiveness Monitoring (SEM) program adequately assesses the effectiveness of industry-reported renewal efforts in regenerating Crown forests, the district offices of the Ministry of Natural Resources should complete all core tasks as outlined in the program and follow up with forest management companies on sites found not to have met the free-to-grow criteria to ensure that the*

companies subsequently took appropriate remedial regeneration measures.

*To further enhance the effectiveness of the SEM program, MNR should consider prescribing penalties that district offices can apply to encourage compliance.*

### Status

The Silviculture Effectiveness Monitoring program consists of a number of core tasks that MNR's district offices are to carry out to assess the forest industry's efforts in renewing forests. In our 2011 audit we noted that, for the 2008/09 and 2009/10 fiscal years, district offices that we had visited had on average completed only 40% of the core tasks prescribed in the Silviculture Effectiveness Monitoring program. In response to our recommendation, MNR agreed to take steps to improve the completion rate of the core tasks. However, at the time of our follow-up, MNR statistics indicated that, for the fiscal year 2011/12, the latest year for which statistics were available, the completion rate of the core tasks by district offices had only marginally improved, to 48%.

With respect to our recommendation that MNR should consider prescribing penalties to encourage compliance, MNR agreed in 2011 to evaluate the Silviculture Effectiveness Monitoring program to ensure that the appropriate incentives were in place to make sure that when remedial regeneration measures are required, these measures are completed by the forest industry. To this end, MNR completed a review of its Silviculture Effectiveness Monitoring program in May 2013, but indicated that changes stemming from the evaluation will be proposed as part of the next revision to the Forest Management Planning Manual and other guidance documents scheduled to begin in early 2014.

### Independent Forest Audits

#### Recommendation 5

*The Ministry of Natural Resources should ensure that action plans and status reports that address the recommendations of the Independent Forest Audits are completed on a timely basis and ensure that it assesses*

*the extent to which previous recommendations were satisfactorily addressed.*

### Status

Every Forest Management Unit in Ontario is subjected to an Independent Forest Audit, which assesses a Forest Management Unit's sustainable forest management practices, at least once every five years. Upon the audit's completion, MNR and the Forest Management Unit must submit an action plan to address reported deficiencies within two months of receiving the final report, and then complete a status report two years after submitting the action plan. In our *2011 Annual Report*, we noted that forest management companies had not completed a number of the action plans and status reports for audits previously conducted on a timely basis. In its response to our recommendation, MNR said it would formally review Independent Forest Audit processes and protocols in 2011, and the results would inform ongoing improvements to the Independent Forest Audit process, including the process in place to assess the extent to which previous recommendations by auditors have been addressed. Shortly thereafter, MNR held early meetings with Sustainable Forest Licence holders on action plan development and streamlined review processes to ensure action plans and status reports were completed on a timely basis. The Ministry indicated that the action plans and status reports that were most recently due were, on average, submitted on time and, for the most part, the actions taken had satisfactorily addressed the recommendations of previous audits.

### Planned Versus Actual Harvest

#### Recommendation 6

*To help ensure that forests are being managed on a sustainable basis and that harvest operations are carried out in accordance with approved plans, the Ministry of Northern Development, Mines and Forestry should:*

- *enhance its ability to monitor on an ongoing basis the excess supply of Crown wood that can be reallocated to new companies that can use or market the wood; and*
- *conduct research into successful practices used in other jurisdictions to address significant variances between planned and actual harvests.*

### Status

In 2011, we noted that in those forest management units where licensees had sole rights to harvest Crown timber, but did not have a market for that timber, the actual harvest tended to fall well short of the planned harvest. There were indications that other companies that did not have access to timber in Ontario's Crown forests could market Ontario wood, which prompted us to recommend that the Ministry should better monitor the excess supply of Crown wood that can be reallocated to new companies that can use or market the wood. In its response to our recommendation, the Ministry indicated that, in the longer term, it had undertaken an initiative to modernize its tenure and pricing system in an effort to allow better access to Ontario's wood supply, thereby improving the likelihood that planned harvest volumes will actually be used.

In the meantime, in October 2011, a database and reporting tool called Trackwood was released to monitor the wood supply and identify surpluses. The information in Trackwood is updated as it becomes available. Monthly updates of the available wood supply are now shared with licensees, existing mills, new industry proponents, communities and the government's economic development staff. MNR also posts these updates on its website where the public may view them.

At the time of our follow-up, MNR had also researched practices used in Quebec and British Columbia relating to the promotion and full use of the available wood supply. MNR indicated to us that, as part of the initiative to modernize its tenure and pricing system, it was still working with the forest industry to develop a regulation that, if the available wood supply was not sufficiently used, would provide for the cancellation of a Sustainable Forest

Licence, or a supply agreement or commitment. Discussions with forestry industry representatives were ongoing and at the time of our follow-up, MNR could not provide a timeline for the regulation's implementation.

## CROWN FOREST REVENUE

### Stumpage Fees

#### Recommendation 7

*To ensure that the province receives the proper amount of revenue for the use of Crown forest resources, the Ministry of Northern Development, Mines and Forestry should:*

- *develop overall provincial guidance for establishing wood measurement factors to ensure consistency and accuracy among the regions when determining stumpage fees;*
- *increase the number of scaling audits performed each year to ensure that all mills are subject to the required audit every five to seven years in accordance with MNDMF guidelines; and*
- *design and implement system controls in the stumpage fee information system so that invalid licence holders, and mills and haulers that are not authorized to receive and transport wood, are identified for appropriate follow-up.*

*MNDMF should also formally assess the implications of renewing harvest licences where significant stumpage fees are outstanding.*

#### Status

To calculate stumpage fees, the mills measure nearly all Crown timber harvested and report to MNR on the species of trees and the respective volumes received. MNR estimates the percentage of defective or undersized wood, which does not incur stumpage fees, by checking the number of undersized logs in a sample of loads received by mills. In our *2011 Annual Report*, we noted that there was no overall provincial guidance on how these estimates should be done, and that all three regions we visited used different methods. At the time of our follow-up, MNR had developed a 10-year provincial

sampling plan to eliminate these inconsistencies and provide the framework for new regional sampling plans. At the time of our follow-up, two regions had finalized their plans and the third was in the process of finalizing its plan.

According to MNR guidelines, all mills are to be audited every five to seven years to verify that they have adequate procedures to accurately measure the Crown timber they receive. In our *2011 Annual Report*, we noted that an average of only 10 such audits had been carried out annually in the preceding nine years. At this rate, given that more than 200 mills in the province receive and measure Crown timber, it would have taken more than 20 years to audit them all. In response to our recommendation to increase the number of scaling audits each year, MNR indicated that it had reduced the scope of the audits on larger mills in cases where the audit team felt it did not compromise the audit's objective. On these larger mills, MNR examined documentation covering periods of six to 12 months, and has since reduced this period to three to six months. MNR indicated that this reduction enables it to audit the larger mills more quickly and hence allows it to do more audits overall. However, for the 2012/13 fiscal year, we noted that MNR had audited 10 mills, the same as the average number that were being audited at the time of our *2011 Annual Report*. When we questioned the Ministry on this, it indicated that in addition to shortening the review period on audits, it is also pursuing other options, such as training more staff to audit mills. This will enable it to conduct more audits in the future.

In 2011 we noted that many invoices had been processed for species that forest management companies did not have a licence to harvest, or haulers were not authorized to haul. In response to our recommendation, MNR indicated that it has proposed changes to the system that would flag any unauthorized receipt/transport of wood as an "invalid tally." Once a tally is flagged, the system would not allow it to be processed until it is verified manually and followed up appropriately. At

the time of our follow-up, MNR expected to complete these changes to the system in the 2013/14 fiscal year.

With respect to our recommendation to assess the implications of renewing the harvest licences of companies with outstanding stumpage fees, MNR sent a memo to its regional directors in March 2012 recommending withholding licence approval to companies in arrears until a repayment arrangement was in place. MNR also provided us with an example of harvest approvals being withheld for a large company in April and May 2013 until the company had paid its outstanding stumpage fees. In 2011, \$45 million in stumpage revenue was in arrears. As of June 2013, this amount had dropped somewhat to \$40.6 million, and \$13.6 million of it had been approved for write-off by an Order-in-Council.

## Forest Renewal and Forestry Futures Trusts

### Recommendation 8

*To ensure that the Forest Renewal Trust and the Forestry Futures Trust are sufficiently funded for their intended purposes, the Ministry of Natural Resources should:*

- *review the significant variances in renewal rates calculated by district offices for the same species of trees to ensure that such variances are justified;*
- *review the overall minimum balance that is to be maintained in the Forest Renewal Trust to ensure that the amount is a true reflection of the actual annual forest renewal obligation and ensure that licensees annually maintain their portion of the minimum balance;*
- *review the Forestry Futures Trust charge to ensure that it is sufficient to fund the initiatives that the trust is intended to fund; and*
- *consider requiring Sustainable Forest Licence holders to provide some form of financial assurance that can be used to cover potential silviculture liabilities if a licensee becomes insolvent or surrenders its licence.*

### Status

In our *2011 Annual Report*, we found that levies deposited to the Forest Renewal Trust, established to fund forest renewal expenditures incurred by forest management companies, varied significantly across district offices even for the same species of tree. At the time of our follow-up, MNR indicated that the authority to establish these forest renewal levies had been taken from district managers and given to regional directors, and its renewal charge-setting process was revised in December 2012 to reflect this change. For the 2013/14 fiscal year, the revised process now must consider a licensee's past reimbursements of eligible renewal expenditures, a forecast of the volume and species of trees to be harvested by the licensee, and the amount of future reimbursements.

In our *2011 Annual Report*, we noted that as of March 31, 2011, five licensees had not maintained their minimum balance totalling \$4 million in the Forest Renewal Trust, contravening the terms of their licences. At the time of our follow-up, three Sustainable Forest Licence holders did not meet their minimum balance requirement, totalling a little over \$230,000. MNR indicated that it was actively pursuing the recovery of shortfalls from these licensees. MNR had also begun to develop a process for quantifying and maintaining a statement of outstanding forest regeneration liabilities in order to evaluate whether funds held in individual trust accounts are sufficient to cover these liabilities. This involves analyzing annual report data submitted by licensees to assess whether all regeneration obligations have been fulfilled.

Since our 2011 audit, MNR has also completed a review of the Forestry Futures Trust charge to assess whether it is adequately funded. At the time of our follow-up, MNR was considering an adjustment to the Forestry Futures Trust charge for inflation as a result of the review.

As part of an overall strategic and operational review of both trusts commissioned by MNR in March 2012, the Ministry was considering a

number of options for requiring Sustainable Forest Licence holders to provide some form of financial assurance. One option that MNR was considering at the time of our follow-up was an insurance fund as a hedge against the event of bankruptcy or some other occurrence that would prevent a licensee from completing regeneration activities. An actuarial analysis of the regeneration liability and the probability of default would determine the size of the fund and the premiums. Since consultations with stakeholders would first need to be conducted on the various options under consideration, MNR could not provide a timeline for when potential changes might be made.

## REPORTING

### Recommendation 9

*To enhance the value of its annual report on forest management, the Ministry of Natural Resources should compare actual levels of key forest management activities—such as harvest and regeneration (that is, natural, planting, seeding, site preparation, and tending)—to planned or target levels and should provide explanations for any significant variances.*

### Status

In its 2009/10 annual report on forest management (tabled in the Legislature December 2012), MNR included planned harvest area and volume levels. MNR has yet to table the 2010/11 annual report. When we questioned why the report had not yet been tabled, MNR indicated that it is up to the discretion of the government since there is no legislative timeline for tabling. The 2010/11 annual report, when tabled, will include planned regeneration levels as well. MNR indicated that future reports will include a more detailed analysis of actual versus planned levels of harvest and regeneration, and explanations of any significant variances.

## OTHER MATTER

### Licensing of Mills

#### Recommendation 10

*The Ministry of Northern Development, Mines and Forestry should ensure that forest resource processing facility licences are granted only to those forest resource processing facilities that demonstrate that they have sufficient financial resources to operate, and ensure that forest resource processing facilities submit the required annual returns on a timely basis.*

#### Status

To obtain a licence, mills are required to submit a business plan to the Ministry, which must be satisfied that the applicant has the ability to finance, operate and manage the facility. In our *2011 Annual Report*, we noted that licences had been issued to some mills that had submitted business plans that did not demonstrate the applicant's ability to adequately finance the facility.

At the time of our follow-up, MNR had instituted new requirements for the assessment and documentation of the financial resources of new forest resource processing facilities (mills) applying for a licence. For instance, as part of a business plan

that demonstrates that a prospective mill has the ability to finance, operate and manage the facility, it is required to submit, among other things, audited financial statements for the past three years, pro forma income statements, balance sheets and cash flow statements for the first five years of operation, credit rating and the name of the financial institution supporting its application.

Mills are also required to submit an annual return that reports on the facility's operations based on the volume processed. In our *2011 Annual Report*, we also noted that about two-thirds of the annual returns were either not submitted on a timely basis, or not submitted at all. In March 2013, MNR completed a project to improve the timeliness of the submission of annual returns by forest resource processing facilities. The project simplified the submission and approval processes in the electronic system that handles facility annual returns (eFAR). At the time of our follow-up, the Ministry informed us that for the 2007–2011 period, returns covering 87% of the volume processed had been submitted. The due date for 2012 returns was September 30, 2013, and at the time of our follow-up, returns covering 57% of the volume processed had been submitted.