

24 August 2016

TO: Directors of the Idaho Land Board

FR: Fred Omodt

RE: Negotiated Rulemaking for IDAPA 20.02.14 Rules for Selling Forest Products on State-Owned Endowment Lands

Negotiate to attempt to come to an agreement on something through discussion and compromise

The proposed rule change for selling forest products on State owned endowment lands, 20.02.14, is not a product of negotiation. The sale of cedar poles from IDOL lands has been accomplished by a dual entry system of either removing the cedar poles prior to harvesting the sawlog volume or by logging the sawlogs before the poles are harvested. At the first Negotiated Rule meeting on 6 June 2016 in Coeur d'Alene, the Idaho Department of Lands representatives made it clear that selling cedar poles as a separate and valuable timber product would not be considered during negotiation. This severely limited the Idaho cedar pole industry's access to endowment timber. During the course of this and subsequent meetings, the pole industry conceded that changes needed to be made in the unit of measurement used to sell poles, that the IDOL could eliminate the threshold used to identify a potential pole sale and that the IDOL did not have to offer a minimum number of poles for sale annually. The IDOL did not concede on any point proposed by the pole industry, even in the face of supporting comments by timber company representatives and IDOL staff.

This is the crux of the proposed rule change. Will Western Red Cedar poles be sold as a required product manufactured as poles or will the volume of pole quality cedar on endowment lands be included with cedar sawlog volume on timber sales? If the pole volume is not sold as a separate product that must be manufactured as poles, the higher value of that volume will be lost and viability of Idaho's cedar pole industry will be compromised.

The IDOL based the changes to the proposed rule on a Capstone Project Report entitled Cedar Pole Policy, first submitted to the Department on 3 May 2016. The report identified several aspects of the current rule that triggered a need for a change to the policy for selling cedar poles.

Economic Impacts

Using mostly anecdotal evidence, the Report concluded that there is a doubling of costs when using a two entry harvest plan. No analysis of IDOL policy or field work was used to identify possible changes that reduce these costs.

Again, using anecdotal evidence, the Report claims a six to ten year delay in establishing the next rotation if a double entry system is used for a dedicated pole sale harvest. No examples of such delays are offered.

Next the Report compares the price paid for poles using the current rule of dollars per lineal foot, with the price of poles that would be paid if the unit of measurement was the same as used for sawlogs, dollars per MBF. This point was conceded by the pole industry at the first negotiation meeting and the industry agreed that a MBF unit price would be acceptable.

The Report uses data from pole sales from 31 March 2013 through 31 March 2016 to show that the differential between stumpage prices for WRC sawlogs and cedar poles is much lower than has been thought. But even while making this assertion, the Report concedes that there is a premium paid for poles. Using the time frame of 2013 to 2016 to compare sawlog prices to pole prices ignores the history of the pole value versus sawlog value. In every IDOL Annual Report, starting in 1974-1975, cedar poles have been listed as a separate category and in every report the higher value of cedar poles has been evident.

A similar rule negotiation to change the method of selling poles was initiated by then Idaho Department of Lands Director Stanley F. Hamilton on 6 April 1984. Using virtually the same concerns with the pole sale policy as the current proposal, Mr. Hamilton stated the goal of the negotiation should be 1) to maximize return to the endowments, 2) to simplify sale preparation and administration and 3) to provide the cedar pole industry the opportunity to compete for pole quality cedar. During the discussion on the proposed changes, the pole industry demonstrated that the pole sale policy of double entries provided a much higher return to the endowments than any other proposal being considered.

The current proposed rule change is based on the differential of cedar pole prices and cedar sawlog prices at a time of near historic high stumpage being paid for cedar sawlogs. Sawlog prices are cyclical. The current high prices paid for cedar sawlogs will not continue indefinitely. What will continue, as shown by historical

comparisons, is the higher value paid for WRC pole quality volume when sold as poles.

The Report places a high significance on a Net Present Value calculation by the Capstone Project that indicates a reduced value of the double entry system of pole harvest. The Report states that the indicated 60 year rotation will result in "limited pole availability." The cedar pole industry sales history shows that more than 60% of total sales come from the length classes of 35 through 45 feet, all of which can be grown in the highly productive cedar sites on endowment lands on a shorter rotation schedule. A viable cedar pole program can exist even if shorter rotations are implemented.

The analysis of that NVP projection has been discussed at length by Clayton Cafferta, CFA, for Moss Adams, and his comments are included in the written comments submitted by the McFarland Cascade Holdings, Inc. to the Department of Lands on 30 June 2016. This analysis points out problems with the assumptions made and the conclusions drawn by the Capstone Report.

Reduced competition

The Report states that "Opening more volume up to bidding by removing artificial economic barriers to competition is one way to ...increase the opportunities to bring bidders to auctions."

The idea that there are a large number of potential bidders that will be attracted to the bidding table by including additional WRC volume in sawlog sales is not supported by sales results. There were 35 sawlog sales sold by IDOL between 1 January 2014 and 30 June 2016, north of I90. A single purchaser bought 32 of these sales. Total appraised WRC sawlog volume on these sales was 10,000MBF. The same purchaser bought 9,815MBF of that WRC sawlog volume. No poles were produced and made available to the pole industry from these sales. The Report's assertion that the pole industry can buy poles from the purchaser of cedar volume on sawlog sales is not evident in North Idaho. This pole volume added to sawlog sales in the northern areas would benefit one purchaser.

While there are potential bidders that would welcome the chance to bid on the high value WRC volume, they cannot afford the associated mixed sawlog volume that would be included with the cedar sawlog. These potential bidders depend on sawlog volume generated from pole sales to provide needed sawlogs for their operations. If the pole sale program is eliminated, these manufacturers would have to purchase logs from competitors.

In conclusion, the proposed rule change, 20.02.14, for the sale of forest products is not a negotiated rule change and will not produce the desired goal of the Capstone Project's Report of removing and capturing the value of cedar poles for the benefit of beneficiaries and industry. The proposed rule ignores industry's warnings that the value of cedar poles will be lost by including the pole volume in the standard sawlog sale format and does not acknowledge the changes agreed to by the pole industry. The industry has recognized that changes need to be made in the rule and has compromised significantly toward that end. The IDOL is "throwing the baby out with the bath water" with its proposed rule.

I urge the Land Board, short of a review of the conclusions made by the Capstone Project team, to implement the proposed rule on a temporary basis to study the results of the changes proposed before a permanent change in the pole policy is enacted.

Thank you for your consideration.

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