United States General Accounting Office

GAO

Report to the Chairman, Subcommittee on Forests and Public Land Management, Committee on Energy and Natural Resources, U. S. Senate

October 1996

TIMBER MANAGEMENT

Opportunities to Limit Future Liability for Suspended or Canceled Timber Sale Contracts

GAO/RCED-97-14

GAO

United States
General Accounting Office
Washington, D.C. 20548

Resources, Community, and
Economic Development Division

B-274825

October 31, 1996

The Honorable Larry E. Craig
Chairman, Subcommittee on Forests
and Public Land Management
Committee on Energy and Natural Resources
United States Senate

Dear Mr. Chairman:

Each year, the U.S. Department of Agriculture's (USDA) Forest Service and the Department of the Interior's (DOI) Bureau of Land Management (BLM) award thousands of contracts for the removal of timber from public lands. Since the early 1990s, the Forest Service and BLM have suspended or canceled timber sale contracts for a number of reasons, including their own noncompliance with provisions of the National Forest Management Act of 1976, the Endangered Species Act of 1973, or the National Environmental Policy Act of 1969. Suspending or canceling timber sale contracts to protect threatened or endangered species is a relatively new and growing phenomenon for these federal agencies. Before the 1990s, the Forest Service and BLM rarely suspended or canceled a timber sale because of such concerns.

Both the Forest Service's and BLM's timber sale contracts contain provisions describing the liability that the agencies will incur if they cancel a sale or cannot successfully negotiate a modification with the purchaser following a suspension. Concerned about the potential magnitude of the federal government's liability, you asked us to address the following questions:

- What amounts and types of damages have been awarded to purchasers, and how did the Forest Service and BLM pay for the damages?
- What amounts and types of claims are pending against the Forest Service and BLM, and how do the agencies expect to pay the claims?
- What actions are the Forest Service and BLM taking to minimize the future liability arising from suspended or canceled timber sale contracts?

As agreed with your office, we limited our work to timber sale contracts that the Forest Service and BLM had suspended or canceled to protect threatened or endangered species and the resulting claims or lawsuits settled or pending between October 1992 and June 1996. To provide the

most current information, we updated the data on pending claims through October 1, 1996.

Results in Brief

From October 1992 through June 1996, the Forest Service and BLM paid more than $6.6 million in claims for 49 contracts that were suspended or canceled to protect threatened or endangered species. The Forest Service had 48 of the contracts; BLM had 1 contract. The agencies have paid the purchasers for the value of replacement timber, interest, lost profits, and such unrecovered costs as those incurred in maintaining performance bonds. The Forest Service paid damages of almost $6.5 million from its appropriations. BLM settled its single claim (almost $228,000 plus interest) by modifying another contract held by the purchaser to reduce the amount paid to the federal government for purchased timber without changing the original volume of timber to be harvested.

As of October 1996, the Forest Service had 73 pending claims with potential damages of about $61 million; BLM had 1 pending claim for almost $2.2 million. In addition, data from the Forest Service and other sources showed that the agency could incur at least an additional $198 million. BLM officials estimate that BLM could incur between $35 million and $40 million more in potential future liability.[1] However, estimates of how much, when, and whether the agencies will have to pay any of their potential future liability are uncertain. Uncertainty arises from the agencies' inability to predict the outcome of ongoing and future litigation that could result in the award of more or less in damages than the purchasers claim, the results of countersuits that could be filed by the Forest Service or BLM, or the success of the agencies' efforts to offer replacement timber or other settlements in lieu of paying damages. Forest Service officials stated that the agency may not have the funds to pay for pending and future claims without additional congressional funding. According to a BLM official, if purchasers sought and were awarded damages, the agency would first attempt to reduce the price of existing contracts to offset the damages.

Although BLM has repeatedly revised its timber sale contract to minimize its liability when it must suspend or cancel a timber sale contract to protect threatened or endangered species, the Forest Service has not. Since the late 1980s, the Forest Service has been developing new

[1]Pending claims represent those that the purchasers have filed with the agencies' contracting officers or Board of Contract Appeals or with the U.S. Court of Federal Claims. Potential future liability and/or claims are "me too" claims that purchasers may or may not file depending on the outcome of claims or litigation by other purchasers whose contracts had been suspended or canceled under similar circumstances.

regulations and a new timber sale contract that would limit the government's liability on canceled timber sale contracts and redistribute the risk between the agency and the purchaser. The Forest Service has not finalized either the regulations or the contract.

Background

The Forest Service, through its 9 regional offices, and BLM, through its 12 state offices, award contracts to individuals or companies to harvest and remove timber from the federal lands under their jurisdiction. The contracts set forth specific terms and provisions of the sale, including the estimated volume of timber to be removed, the period for removal, the price to be paid to the government, and the environmental protection measures to be taken. For contracts valued at $2,000 or more, for fiscal years 1990 through 1995, the Forest Service reported that it had awarded almost 24,500 timber sale contracts valued at about $27 billion; for fiscal year 1996, data from the Forest Service showed that it had awarded over 8,000 timber sale contracts valued at more than $4 billion as of the end of April 1996.[2] BLM had about 200 contracts valued at more than $173 million.

Both the Forest Service's and BLM's regulations and procedures specify that the agencies can extend the time for completing a timber sale contract under certain circumstances and that they can modify, suspend, cancel, or partially cancel a timber sale contract for various reasons, including the need to protect threatened or endangered species and their habitat. The Forest Service's and BLM's procedures outline similar steps to take when deciding whether to suspend or cancel a timber sale contract. For example, within the Forest Service and BLM, the contracting officer can suspend a contract to protect threatened or endangered species. However, only the Chief of the Forest Service and BLM's state directors are authorized to cancel contracts for environmental reasons. (App. I provides additional information on the Forest Service's and BLM's procedures.)

Various Actions That Occurred Around 1990 Have Resulted in Federal Liability

From October 1992 through June 1996, the Forest Service and BLM paid more than $6.6 million in claims for 49 contracts that were suspended or canceled to protect threatened or endangered species. The Forest Service had 48 of the claims; BLM had 1. The agencies have paid the purchasers for the value of replacement timber, interest, lost profits, and unrecovered costs incurred under the contracts. BLM settled its claim of almost $228,000 (plus interest) by modifying another contract held by the purchaser to reduce the amount paid to the government without changing the original

[2]These data do not include sales for such products as Christmas trees, cones, and burls.

volume to be harvested. Data from the Forest Service show that it settled 48 claims (totaling almost $6.5 million) from timber management appropriations.[3] According to timber management officials, the Forest Service attempts to find replacement timber when it must cancel all or a portion of a sale. However, the data that the Forest Service provided to us do not indicate whether the agency took such action to settle past claims for contracts suspended or canceled to protect threatened or endangered species.

According to Forest Service and BLM officials and attorneys representing some timber sale purchasers, the agencies rarely suspended or canceled timber sale contracts before the 1990s to protect threatened or endangered species. Before that time, public interest groups raised little opposition to timber sales, particularly as they affected threatened or endangered species. After that time, new scientific information about forest ecosystems came to light, environmental advocacy groups became more aggressive and effective, the public and the media focused greater attention on environmental issues, and the listing of new threatened or endangered species by the Fish and Wildlife Service under the Endangered Species Act led to the suspension or cancellation of timber sale contracts. One central issue in the Pacific Northwest concerned whether and how much of the remaining old-growth forests should remain available for timber harvesting or be left undisturbed, in part to protect the habitat of the Northern spotted owl, marbled murrelet, various salmon populations, and other species.

In addition, in the early 1990s, various environmental groups brought legal actions to suspend or cancel timber sale contracts. For example, in May 1991, the U.S. District Court for the Western District of Washington ordered the Forest Service to stop selling timber in much of the area inhabited by the Northern spotted owl until the agency had prepared a management plan and environmental impact statement for the species. Similarly, in June 1992, the U.S. District Court for the District of Oregon ordered BLM not to proceed with timber sale contracts because the agency had not prepared a supplemental environmental impact statement. The primary cause of the suspensions was that the Forest Service and BLM had failed to produce plans that satisfied the requirements of such laws as the

[3]We limited our work to environmental claims related to protecting threatened or endangered species. Other environmental claims can arise from noncompliance with the National Forest Management Act. Claims unrelated to environmental protection can arise from such contractual grievances as breach of contract. For example, two purchasers in Alaska have filed claims for about $2 billion against the Forest Service alleging, among other things, breach of contract by the agency.

National Forest Management Act of 1976, the Endangered Species Act of 1973, or the National Environmental Policy Act of 1969.

Purchasers who disagree with a Forest Service or BLM decision to suspend or cancel a timber sale contract may submit a claim to the responsible agency's contracting officer for a decision. Under the Contract Disputes Act, appeals from the contracting officer's decision may be filed with the respective agency's Board of Contract Appeals or the U.S. Court of Federal Claims. Either party may appeal a decision of one of these bodies to the U.S. Court of Appeals for the Federal Circuit. Generally, claims arising from the suspension or cancellation of timber sale contracts to protect threatened or endangered species have resulted from disagreements between the federal agencies and the purchasers over the types and amounts of compensation to which the purchasers are entitled. Once a court decides the merits of a case, the purchasers can seek reimbursement for their attorneys' fees under the Equal Access to Justice Act if the purchasers meet the criteria defined in the act.[4] If the court awards attorneys' fees, the Forest Service or BLM generally has to pay the fees from appropriations.

Significant Uncertainty Exists About the Amount of Future Liability

Any estimate of future liability must be viewed with uncertainty. The outcome of ongoing and future litigation is unpredictable and could result in the award of more or less in damages than the purchasers claim. In September 1996, for example, USDA's Board of Contract Appeals awarded a purchaser over $4.2 million (plus interest) on a $10 million claim for five timber sale contracts that the Forest Service had suspended in September 1992. Also uncertain are the results of countersuits that could be filed by the Forest Service or BLM, the success of the agencies' offers to replace timber in lieu of paying damages, and the settlement of claims that have not yet been filed.

Claims pending against the Forest Service and BLM for contracts suspended or canceled to protect threatened or endangered species totaled almost $61 million and about $2.2 million, respectively, as of October 1996. Purchasers have filed claims for such expenses as property taxes and insurance; the salaries of officers and watchmen; depreciation; idle equipment, including logging trucks, skidders, loaders, graders, and other assorted vehicles; interest; and the value of replacement timber. When pending claims, the agencies' "best estimates" of potential future

[4]The Equal Access to Justice Act does not allow the award of attorneys' fees to businesses with a net worth exceeding $7 million or with more than 500 employees.

liability, and other information are considered, the Forest Service's potential future liability as of October 1996 could be at least $259 million; BLM officials estimate that the agency's potential future liability could be between $37 million and $42 million. Table 1 shows the number and amount of the pending claims and the "best estimates" of potential future liability.

Table 1: Pending Forest Service and BLM Claims and Estimated Potential Future Liability for Timber Sale Contracts Suspended or Canceled to Protect Threatened or Endangered Species Since Fiscal Year 1992

Dollars in millions

	Pending claims		"Best estimate" of potential future liability	
Agency	**Number of claims**	**Amount of damages claimed**	**Number of possible claims**	**Amount**
Forest Service	73	$ 61	203	$ 198[a]
BLM	1	2	22	35-40
Total	**74**	**$ 63**	**225**	**$233-238**

[a]The amount shown relates to possible "me too" claims for 154 contracts; the Forest Service did not estimate damages for 49 such claims. It also includes an estimated $26 million that attorneys representing one purchaser said would be filed in the future.

Forest Service

According to timber management officials, purchasers had not, as of October 1996, filed claims for the additional $198 million. For example, $170 million of the $198 million potential future liability represents an estimate of potential claims that are still up in the air because of a recent settlement agreement. On September 17, 1996, the Justice Department and 15 timber companies (44 section 318 sales) agreed that the Forest Service would provide alternative timber to the companies between 1997 and 1999, after completing environmental analyses related to the replacement timber being offered. Under the agreement, the purchasers waive all rights to file claims for delays in providing replacement timber that occur after the date of the agreement.

Given the above settlement agreement and a multiplicity of court cases, it is difficult, according to Forest Service officials, for the agency to determine a reasonable damage estimate. Forest Service officials added that the September 1996 settlement agreement does not preclude environmental groups from filing suits to prevent the sale of replacement timber that could be offered to the purchasers. This possibility adds further uncertainty to estimates of the Forest Service's future liability.

Funding for Pending and Future Settlements May Be a Problem

According to Forest Service officials, the agency may not have the funds to settle pending and future claims. In the past, the agency has not requested a specific appropriation to settle claims but has reprogrammed funds or used funds carried over from prior fiscal years. However, the amount of settled claims was significantly smaller than the amount of potential future claims. Timber management officials are concerned that a large judgment against one or several forests could cause the Forest Service to stop all or some programs in the forests or request supplemental appropriations to pay the damages.

Under the Forest Service's policies, the cost of administering a timber sale contract is a cost of the forest on which the sale occurs, and any costs associated with claims are to be covered by the forest's funds. Therefore, the applicable forest would first pay the damages out of current appropriations from the account of the program responsible for administering the contract—for example, timber management or salvage sales. The policy also states that the involved forest and region may have to reprogram funds to cover these costs. The Forest Service has the discretion to reprogram funds within the National Forest System Appropriations Account. In fiscal year 1996, the Congress appropriated $1.3 billion for that account.

The policy further notes that funds must be available to avoid violating the Anti-Deficiency Act and states that contracting officers should not issue a decision on a claim unless funds are available. The policy also states that the Forest Service does not have the authority to use either the Timber Sale Deposit Fund or the National Forest Fund accounts to pay for settling claims because federal law requires the deposit of all receipts from timber sales into a miscellaneous receipts account of the U.S. Treasury except in specific situations that do not include payments for contract claims.

Officials from the Forest Service's Northwest Region told us that they have considered other options to fund future damages. For example, the Forest Service and the purchaser could mutually agree to the amount of the damages and establish credits that could be transferred to existing contracts or held in a "bank" for future contracts. Second, the agency could allow the forests to offset the damages when a purchaser has defaulted on other contracts. Timber management officials said they had discussed these two options with regional, headquarters, and USDA officials. They noted, however, that neither the legislation nor the regulations applicable to the Forest Service allow the agency to implement these options. Third, the Congress could enact legislation allowing the

Forest Service to use funds, derived from the sale of timber under contracts that were subsequently suspended, that the agency had deposited in the Timber Sale Deposit Fund or the National Forest Fund.

For claims that purchasers have already filed, Forest Service officials estimate that some of the damages may come due in fiscal year 1997. Because some claims have only recently been filed and because USDA's Board of Contract Appeals or the Court of Federal Claims can take between 2 and 5 years to issue a ruling, some of the liability may not be realized until beyond 1997. In addition, countersuits and appeals could further delay the date when the liability could become due.

BLM

As of October 1, 1996, BLM had one claim pending for almost $2.2 million. In 1992, the U.S. District Court for the District of Oregon ordered BLM to halt timber sale contracts because of concerns about the Northern spotted owl. As a result of this decision, BLM suspended 23 timber sale contracts. The purchaser of 1 of the 23 suspended contracts has filed a claim with the Department of the Interior's Board of Contract Appeals for about $2.2 million. Attorneys from the office of DOI's regional solicitor in Portland, Oregon, could not estimate when the Board would render a decision on this claim.

According to an attorney from the regional solicitor's office, if the Board's decision is favorable to the purchaser, some or all of the remaining 22 companies could file similar claims. The court lifted the injunction in January 1995, and the companies have been harvesting timber since that time. According to a BLM official and an attorney from the regional solicitor's office, the potential liability could be between $35 million and $40 million if the other 22 purchasers filed and were successful in their claims. These officials pointed out, however, that BLM has not conducted any analyses to support the estimated liability.

A BLM official noted that the 22 purchasers have probably finished harvesting timber from the sales. Therefore, if the purchasers were successful in their claims, BLM would first determine whether the purchasers had other contracts with the agency and, if so, attempt to negotiate a settlement that would modify existing contracts to reduce the price by the damages awarded without changing the original amount of timber to be harvested. According to an official, if that action was not sufficient to settle the damages or if the purchasers did not agree to the settlement, BLM would have to fund the damages from appropriations.

The Forest Service Can Further Limit Its Future Liability; BLM Has Completed Its Action

Both the Forest Service and BLM have taken some actions to minimize the future potential liability arising from the suspension or cancellation of timber sale contracts to protect threatened or endangered species. Although BLM has completed the actions to limit its liability, the Forest Service has spent years drafting and redrafting proposed changes to its regulations and standard contract language.[5] The Forest Service has not finalized either document. In commenting on a draft of this report, officials from USDA's Office of General Counsel and the Forest Service's Timber Management staff pointed out that changes in environmental laws, the increase in the number of lawsuits, and the impact of the resulting court rulings contributed to the delay in finalizing draft regulations and a draft timber sale contract.

Forest Service

The existing Forest Service timber sale contract includes three provisions that can come into play when the agency suspends or cancels a timber sale contract to protect threatened or endangered species. The following summarizes the three provisions:

- If the Forest Service suspends a contract to prevent serious environmental degradation or resource damage or to comply with a court order, the purchaser's claim is limited to the out-of-pocket expenses incurred as a direct result of the suspension. The contract specifies that such out-of-pocket expenses do not include lost profits, the cost of replacement timber, or any other anticipated losses.
- If the Forest Service cancels a contract to be consistent with a forest plan, to comply with a court order, or to respond to a determination that continued timber harvesting would seriously degrade the environment, cause resource or cultural damage, and/or jeopardize sensitive, threatened, or endangered species, the purchaser is entitled, under provision CT9.5, to out-of-pocket expenses and to reasonable compensation for the cost of acquiring comparable timber to replace that lost through the cancellation.
- If, for the same reasons, the Forest Service cancels a contract, the purchaser is entitled to out-of-pocket expenses but not, under provision CT9.52, to compensation for the value of replacement timber.

However, the language of CT9.52 differs from the language in the Forest Service's regulations addressing the cancellation of contracts for environmental protection. Those regulations state that the Forest Service

[5]Although the proposed regulations and contract had not been released for public comment, USDA provided us with a July 1996 version to review.

will provide reasonable compensation to the purchaser for unrecovered costs and for the value of replacement timber. One purchaser has filed a suit with the U.S. Court of Federal Claims alleging, among other things, that CT9.52 is not consistent with the Forest Service's regulations. Officials from USDA's Office of General Counsel said that it is not atypical for a case in the U.S. Court of Federal Claims to take several years to be resolved.

Draft Cancellation Regulations Would Use a New Formula to Calculate the Value of Replacement Timber

In August 1990, the Forest Service published proposed regulations on canceling timber sale contracts. The Forest Service did not issue final regulations because it identified additional changes that were needed and litigation was occurring at that time. In 1992, the Forest Service again revised its regulations on cancellations. The 1992 revision incorporated, among other things, the contract provisions affecting (1) the protection of endangered species' habitat and (2) the settlement that will be provided when the agency cancels a timber sale contract to protect threatened or endangered species. The agency had expected to publish the proposed regulations for comment in January 1994. (App. II provides additional details on the proposed regulations.)

Since that time, USDA has been reviewing the proposed regulations. According to Forest Service officials, on September 26, 1996, USDA gave its approval for the Forest Service to send proposed regulations to the Office of Management and Budget (OMB) for its review and approval. At an October 1996 meeting, according to officials from the Forest Service and USDA's Office of General Counsel, OMB asked the Forest Service to provide additional information on the economic impact of the proposed regulations. The Deputy Director for Timber Management told us that the Forest Service expects to provide the required analysis to OMB by December 1996 but could not estimate when proposed regulations would be published for public comment.

Draft Timber Sale Contract Would Reduce the Government's Risk

In January 1988, the Forest Service completed its consolidated revision of the two most frequently used timber sale contracts, which had not been revised since the fall of 1973, and provided the draft to USDA for its review. In 1993, the Forest Service and USDA initiated a second effort to revise the timber sale contract, but neither draft has been published for comment or implemented because USDA is still reviewing it. If the Forest Service had finalized the contract, USDA's Associate General Counsel, Natural Resources Division, and other officials from that office believe that some of the current liability might be greatly reduced because the proposed

contract would give the government more flexibility to modify contracts and delete timber areas affected by threatened or endangered species.

On September 27, 1996, Forest Service officials told us that the Chief had approved the proposed contract and was planning to meet with USDA's Under Secretary for Natural Resources and the Environment about it. They could not estimate when or whether USDA would approve releasing a proposed contract for public comment. (App. II provides additional details on the draft contract.)

BLM

BLM has not had many claims for contracts suspended or canceled to protect threatened or endangered species. BLM's contract provisions and regulations allowing extensions of the completion date have significantly limited cancellations. In addition, beginning in 1996, BLM's contracts have limited purchasers' damages to unrecovered costs when cancellations have resulted from the Endangered Species Act.

Since 1984, BLM's timber sale contract has included a provision that allows the agency to suspend a contract to protect threatened or endangered species. If its subsequent analysis shows that mitigating actions can address the concerns or that the concerns no longer exist, BLM can extend the contract's completion date for time equal to the operating time that has been lost because of the suspension. According to a BLM official, valid reasons for granting extensions include delays necessitated by the Endangered Species Act, court injunctions by parties outside of the contract, and reviews of cultural resources. From 1992 through June 1996, BLM extended the completion dates for 52 contracts, primarily to comply with the Endangered Species Act.

If its subsequent analyses show a continuing problem, BLM attempts to negotiate a modification with the purchaser. If unsuccessful, BLM cancels the contract. According to BLM officials, the agency has not canceled any timber sale contract since at least fiscal year 1992. In 1991 and again in 1994, BLM revised the provision and expanded the circumstances under which the agency could suspend operations to consult or reinitiate consultation with the Fish and Wildlife Service and other agencies. For example, BLM could suspend operations while certain raptors and owls were nesting or upon discovering "survey and manage species" identified for protection in a resource management plan. Following the suspension, the purchasers can resume timber harvesting operations; BLM does not incur any liability.

In addition, BLM's regulations and standard timber sale contract provisions are consistent and do not require the agency to compensate purchasers for the value of replacement timber when contracts are canceled or partially canceled. However, until 1996, BLM's contract was silent on the types of damages that purchasers could claim following a cancellation or partial cancellation. Rather, BLM relied on its contracting officers, DOI's Board of Contract Appeals, and the courts to determine whether payment for damages was warranted and how much was to be awarded.

Since March 1996, BLM's contract has included a provision that limits the purchaser's damages to the actual costs that have not been recovered by the value of the timber removed from the contract area. For example, if the purchaser builds a road to harvest a sale, BLM would compensate the purchaser only for that portion of the road's construction costs applicable to the portion of the sale that had been canceled. BLM uses a formula to determine the government's liability. BLM compensates purchasers for such unrecovered costs only when contracts are canceled or partially canceled to protect species listed under the Endangered Species Act.

According to a BLM official and an attorney from the office of DOI's regional solicitor in Portland, Oregon, BLM had considered adding provisions to reduce the federal liability, such as unilaterally canceling a timber sale contract for the convenience of the government, but they noted that such actions may not be in the agency's best interest, since the more restrictive a contract, the less purchasers are likely to bid for the timber. As of September 1996, BLM officials with whom we met said that they believe the agency has sufficient protection and has no plans to either expand its contract provision or take any other action that could further limit the agency's future liability. BLM's past success in negotiating a noncash settlement with a purchaser seems to support the agency's belief.

Conclusions

BLM has suspended or canceled significantly fewer timber sale contracts than the Forest Service, and BLM has consistently taken actions to protect itself from the damages that could arise from suspending or canceling timber sale contracts to protect threatened or endangered species. In contrast, as evidenced by the current lawsuit alleging inconsistency in the language of its cancellation regulations and standard timber sale contract provisions, the Forest Service's actions have not fully protected the agency.

Although complying with various environmental laws before offering a timber sale would help protect the agencies against future suspensions or cancellations and the damages that could follow, effective regulations and a contract that has the same suspension and cancellation language as the regulations would go a long way to further minimize the potential for future claims, lawsuits, and damages. Many years have passed since the Forest Service started to develop proposed regulations and a revised contract that would minimize the agency's future liability. However, the Forest Service has not yet released these documents for public comment—a process that would help it identify the issues that still need to be addressed. Although various circumstances contributed to the delay in issuing draft regulations and a contract for public comment, the dialogue that would result from the expeditious publication of both documents may lead to more consistent actions by the industry and a better understanding of the regulatory and contractual requirements by both the industry and the public.

Recommendation

We recommend that the Secretary of Agriculture direct the Chief of the Forest Service to expeditiously release for public comment proposed regulations for canceling timber sale contracts and a revised timber sale contract.

Agency Comments

We provided USDA, the Forest Service, DOI, and BLM with a draft of this report for comment. We met with officials from these agencies, including attorneys in USDA's Office of General Counsel; the Deputy Director, an assistant director, and other members of the Forest Service's Timber Management staff; an assistant director from BLM's Lands and Renewable Resources staff; a forester in BLM's Oregon State Office; and attorneys from the office of DOI's regional solicitor in Portland, Oregon. These officials agreed with the report's findings, and USDA and the Forest Service agreed with the recommendation. USDA and Forest Service officials also provided us with additional reasons for the delay in issuing new cancellation regulations and a new timber sale contract and expressed concern about the specificity of the information provided on these documents. Officials from USDA, the Forest Service, and BLM and attorneys from the office of DOI's regional solicitor in Portland, Oregon, suggested clarifications to our report that we incorporated as appropriate.

Attorneys in USDA's Office of General Counsel and the Deputy Director, Timber Management, noted that changing environmental circumstances,

the tremendous increase in the number of lawsuits, and the decisions resulting from the numerous lawsuits filed by public interest groups and the timber industry over the last 8 years have resulted in draft cancellation regulations and a draft timber sale contract that differ significantly from the Forest Service's original proposals. They also noted that these and other issues contributed to the delay in moving forward with the two proposals. We incorporated these views in the draft where appropriate.

USDA and Forest Service officials were concerned about the specificity of the information that we had provided on the draft regulations and draft timber sale contract because the agency has not released the two documents for public comment. They explained that both proposals are very sensitive and would shift some of the risk from the government to the industry. We modified some information on the draft regulations and contract to provide a more general discussion of their expected impact.

We performed our work from May 1996 through September 1996 in accordance with generally accepted government auditing standards. Appendix III contains details on the scope and methodology of our review.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 7 days after the date of this letter. At that time, we will send copies to the Secretaries of Agriculture and the Interior and the Director, Office of Management and Budget. We will make copies available to others upon request.

This work was performed under the direction of James K. Meissner, Associate Director for Timber, who can be reached at (206) 287-4810 if you or your staff have any questions about this report. Other major contributors to this report were Mary Ann Kruslicky and John S. Kalmar, Jr.

Sincerely yours,

Victor S. Rezendes
Director, Energy, Resources,
and Science Issues

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Abbreviations

BLM	Bureau of Land Management
DOI	Department of the Interior
GAO	General Accounting Office
OMB	Office of Management and Budget
USDA	U.S. Department of Agriculture

Agencies' Procedures for Suspending or Canceling Timber Sale Contracts

The Bureau of Land Management's (BLM) and the Forest Service's procedures outline similar steps that the agencies should take when deciding to suspend or cancel a timber sale contract for environmental reasons, including concerns about threatened or endangered species. BLM has delegated the responsibility for suspending a contract to the contracting officer. The Forest Service has delegated the responsibility to suspend a contract to the forest supervisor, who can redelegate the authority to the contracting officer. Table I.1 summarizes the agencies' procedures for suspending a contract.

Table I.1: BLM's and the Forest Service's Procedures for Suspending a Timber Sale Contract to Protect Threatened or Endangered Species

BLM	Forest Service
Notify purchaser orally or in writing	Prepare suspension notice
Prepare suspension notice	Deliver suspension notice
Deliver suspension notice	Negotiate a contract modification
Negotiate a contract modification or send a letter warning of cancellation	Resume operations if contract is modified
Resume operations if contract is modified	Move to terminate contract if agreement on modification cannot be reached
Move to terminate contract if agreement on modification cannot be reached	

The procedures for canceling a timber sale contract differ from those for suspending one. Within BLM, the state director is authorized to cancel a timber sale contract to prevent environmental degradation. According to an official, BLM's canceling of a timber sale contract is a "rare occurrence." None of the information provided to us by BLM indicated that it had canceled a timber sale contract since fiscal year 1992 to protect threatened or endangered species. Within the Forest Service, only the Chief can cancel a timber sale contract upon determining that its continuation would cause serious environmental degradation. In addition, the courts have ordered or the Forest Service has agreed to voluntarily cancel timber sale contracts. Table I.2 summarizes BLM's and the Forest Service's procedures when canceling a timber sale contract.

Table I.2: BLM's and the Forest Service's Procedures for Canceling a Timber Sale Contract to Protect Threatened or Endangered Species

BLM	Forest Service
Contracting officer notifies state director	Forest supervisor or contracting officer notifies regional forester
State director concurs	Damages are determined
Damages are determined	Chief reviews and decides on the action to be taken
Regional solicitor reviews proposed action	Contracting officer's decision (cancellation notice) is sent to purchaser
Termination notice is sent to purchaser	Board of Contract Appeals or U.S. Court of Federal Claims rules if purchaser appeals contracting officer's decision
Board of Contract Appeals or U.S. Court of Federal Claims rules if purchaser does not accept settlement	

Forest Service's Draft Cancellation Regulations and Timber Sale Contract

Draft Regulations Would Make Compensation Similar to That of Other Agencies

In an effort to limit the financial liability of the Forest Service when it must, for reasons of public policy or statutory direction, cancel a timber sale contract, in August 1990, the agency published proposed regulations concerning the cancellation of timber sale contracts. The Forest Service did not issue final regulations because it subsequently identified additional changes that should have been included in the 1990 proposed regulations and because litigation was occurring at that time. In 1992, the Forest Service again instituted an effort to incorporate two of its contract provisions—one to protect the habitat of endangered species and the other to specify the settlement that will be provided when the agency cancels a timber sale contract to protect threatened or endangered species—into its regulations. The Forest Service had expected to publish the proposed regulations for public comment in January 1994. According to Forest Service officials, on September 27, 1996, the U.S. Department of Agriculture (USDA) gave its approval for the Forest Service to send proposed regulations to the Office of Management and Budget (OMB) for its review and approval. They also noted that OMB is required to complete its review within 30 days and said that USDA would then have to approve the Forest Service's publication of the regulations for public comment.

The July 1996 version of the Forest Service's draft regulations that we reviewed would clarify when, why, and by whom contracts may be canceled; remove redundant provisions; provide a new formula for compensation when the government must cancel timber sale contracts; and limit the financial liability of the United States on certain contracts. The regulations would also include the language of the Forest Service's Settlement for Threatened and Endangered Species contract provision (CT9.52) and change the formula for calculating compensation for the value of replacement timber to be similar to that of other agencies.

In the preamble to the draft regulations, the Forest Service states that assuming most of the risk is no longer in the public interest nor is it fiscally feasible, given the increasing uncertainties surrounding national forest timber sales. The preamble notes that the draft regulations would give agency officials the flexibility to adjust management activities on National Forest System land. The preamble also notes that these and other changes are necessary because the agency cannot continue to bear most of the financial risk and burden of contract cancellations arising from its compliance with the increasingly complex and rigorously enforced environmental laws and regulations.

Draft Timber Sale Contract Would Reduce the Government's Risk

In January 1988, the Forest Service completed its draft consolidated revision of the two most frequently used timber sale contracts (2400-6 and 2400-6T), which had not been revised since the fall of 1973.[1] The draft was not published for comment and was never implemented. In its April 1993 Timber Cost Efficiency Study—Final Report, the Forest Service indicated that it would revise its timber sale contracts. In July 1993, at the direction of the Assistant Secretary of Agriculture for Natural Resources and Environment, USDA and the Forest Service began a second initiative to develop a revised timber sale contract.

We reported in April 1994 that the Forest Service had sent the revised contract to the Secretary of Agriculture in January 1994, expecting it to be issued by October 1994.[2] As of October 1996, the Forest Service had not published the revised contract for public comment. According to officials from the Forest Service and USDA's Office of General Counsel, interested parties, including the industry, should have a chance to comment on the revision because they may be able to suggest changes that will improve the contract or identify aspects of it that will not work on the ground. On September 27, 1996, Forest Service officials told us that the Chief had approved a proposed contract and was planning to meet with USDA's Under Secretary for Natural Resources and the Environment about it. Officials could not estimate when or whether USDA would approve the Forest Service's release of a draft contract for public comment.

In developing the draft contract, USDA and the Forest Service reviewed timber sale contracts used by several states, the Department of the Interior, and private parties to sell private timber and reviewed court decisions to identify specific ambiguities and weaknesses in the current timber sale contracts.[3] According to the conclusion, the draft contract would distribute liability and risk "more equitably" between the parties and bring the contract into conformity with standard business practices. For example, the draft contract would permit the Forest Service to modify the contract to protect natural resources, including threatened or endangered species, and to adjust the contract's terms to give the

[1]The Forest Service uses Form 2400-6 when the payment for timber is made after the logs have been cut, removed from the sale area, and measured by scalers, and Form 2400-6T when it measures the trees and estimates the volume before awarding the contract.

[2]See Forest Service: Status of Efforts to Achieve Cost Efficiency (GAO/RCED-94-185FS, Apr. 26, 1994).

[3]The states included California, Michigan, Minnesota, Montana, North Carolina, Oregon, South Carolina, and Washington. The private parties included Weyerhaeuser and International Paper Company.

purchaser additional harvesting time or money in consideration of such modifications.

Currently, the Chief of the Forest Service may cancel a contract to comply with a court order or upon determining that the contract's continuation would degrade the environment, be inconsistent with land management plans, damage cultural resources, or jeopardize threatened or endangered species. Although the Forest Service's regulations provide other circumstances under which the Chief may cancel, the existing contracts do not include the additional actions. The draft contract would incorporate the other circumstances specified in the regulations and permit the Chief to also cancel a contract (1) if continued operations would violate a federal law or conflict with the management of other forest resources, (2) upon a physical change in the sale area or damage that materially diminishes the value of the timber, and (3) upon a final determination that the purchaser had violated environmental quality regulations on a national forest. The Forest Service would reimburse the purchaser for any unrecovered out-of-pocket expenses.

In the cost and benefit analysis supporting the draft contract, the Forest Service concluded that the agency and the timber industry would realize a net benefit of more than $7 million from the contract's implementation. The Forest Service also estimated that the contract revision could affect about 3,000 timber sales each year, the costs for purchasers to administer the revised contract would increase about 10 percent over the costs of administering the current contracts, the government would receive about $26 million less for the timber sold, litigation costs to both parties would be reduced by about $330,000 annually, and damages would be reduced by between $20 million and $30 million over the next 4 to 5 years.

Although major differences exist between federal and state laws, regulations, and guidelines, we noted that the timber sale contract used by Oregon seems to restrict the types of damages more than the Forest Service's contract, yet the state is able to market and sell large volumes of timber. For example, under Oregon's timber sale contract, the state can terminate the contract in whole or in part whenever such action is in the state's best interest. If Oregon terminates a part or all of a timber sale contract, the purchaser is not entitled to lost profits, the cost of replacement timber, or any other consequential damages. Also, any interest earned on moneys deposited by the purchaser remains with the state.

The vice presidents of two industry organizations with whom we met told us that Oregon has only about 2 to 3 percent of the timber sales in the state (the Forest Service has about 15 percent), deals with only one or two forests, sells to a limited group of purchasers, and awards its contracts for short terms; therefore, purchasers are willing to accept more restrictive provisions. They also noted that since Oregon uses timber sale revenues for such activities as schools, the state has an incentive to resolve problems rather than suspend or cancel contracts and incur damages.

Objectives, Scope, and Methodology

The Chairman, Subcommittee on Forests and Public Land Management, Senate Committee on Energy and Natural Resources, asked us to determine (1) the amounts and types of damages awarded to purchasers whose timber sale contracts have been suspended or canceled and the ways the agencies have paid the damages, (2) the amounts and types of claims pending against the Forest Service and Bureau of Land Management (BLM) and the sources of funds from which the agencies expect to pay the claims, and (3) the actions that the Forest Service and BLM are taking to minimize the future liability arising from suspended or canceled timber sale contracts. As agreed with the Chairman's office, we limited our work to timber sale contracts that have been suspended or canceled to protect threatened or endangered species and to claims settled or pending between October 1992 and June 1996. To provide the most current information, we updated the data on pending claims through October 1, 1996.

To obtain the information in this report, we reviewed relevant Forest Service and BLM regulations, policies, and procedures related to awarding, suspending, and canceling timber sale contracts. We reviewed reports by GAO, the Congressional Research Service, and the U.S. Department of Agriculture's (USDA) and the Department of the Interior's (DOI) Offices of Inspector General on various aspects of the Forest Service's and BLM's timber programs. We also obtained legal briefs that had been submitted to the U.S. Court of Federal Claims on some of the pending lawsuits and reviewed rulings issued by that court as well as by USDA's Board of Contract Appeals, the U.S. District Court for the Western District of Washington, and the U.S. District Court for the District of Oregon. We visited the Forest Service's and BLM's offices responsible for timber sale contracts in the Pacific Northwest. We selected this location because almost all of BLM's timber sale contracts are awarded by its Oregon State Office and 35 percent of the Forest Service's timber sale contracts over $2,000 are awarded by its Pacific Northwest Region. We also met with the Vice President of the Northwest Forestry Association, which represents timber companies located in Oregon and Washington State, and the Vice President of the Independent Forest Products Association, which represents timber companies throughout the United States.

To determine the types and amounts of damages awarded to purchasers for suspended or canceled timber sale contracts, we reviewed the applicable provisions of each agency's timber sale contract. We also met with timber management officials at the Forest Service to discuss the types and amounts of damages paid to timber purchasers. In addition, at

our request the Forest Service gathered data from each forest on the claims paid and the source of the funds used to pay the claims. We also contacted all 12 BLM state offices to determine the damages that were paid since fiscal year 1992 for timber sale contracts that were suspended or canceled to protect threatened or endangered species. For the one claim paid by BLM, we obtained information from the state office and the office of DOI's regional solicitor in Portland, Oregon.

In documenting the types and amounts of claims pending against the Forest Service and BLM and the sources of funds from which the agencies expect to pay the claims, we relied on information provided by the forests and BLM's state offices. A Forest Service timber management official requested each forest to gather information on the claims that were pending for timber sale contracts that had been suspended or canceled to protect threatened or endangered species. We reviewed the data and compared them with the data the Forest Service had provided to the Subcommittee. We discussed the pending claims with officials from USDA's Office of General Counsel and gathered data from a local law firm that represents several timber purchasers to determine the rationale for their clients' claims and the amounts they are seeking in damages. We also contacted attorneys in six of the Forest Service's nine regional offices to determine the reasons that purchasers filed claims. For BLM's one pending claim, we gathered supporting documentation and discussed the basis for the claim with a BLM state office official and an attorney in the office of DOI's regional solicitor in Portland.

We discussed with Forest Service and BLM officials the actions the agencies can take to minimize the future liability arising from suspended or canceled timber sale contracts. We obtained copies of the provisions in each agency's timber sale contract that have been used to limit the agencies' liability when timber sale contracts have been suspended or canceled to protect threatened or endangered species. We discussed the provisions' merits with officials from USDA's Office of General Counsel as well as with BLM state officials and regional solicitors. We reviewed drafts of the Forest Service's July 1996 regulations and contract revisions. The draft regulations are aimed at reducing the Forest Service's liability for canceled timber sales and the draft timber sale contract would assign risk differently between the Forest Service and purchasers. We discussed the history and relevance of both proposals with officials from the Forest Service and USDA's Office of General Counsel as well as with private attorneys who had drafted a proposed timber sale contract at the industry's request. Finally, we discussed with BLM state officials and an

attorney in the office of DOI's regional solicitor in Portland the actions that BLM has taken or plans to take to limit its future liability for timber sale contracts that are suspended or canceled to protect threatened or endangered species.

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