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REPORT BY THE U.S.

General Accounting Office

Potential Impacts Of Tighter Forest Service Log Export Restrictions

Federal law restricts the export of unprocessed timber cut from national forests in the western half of the United States. Also, purchasers of national forest timber are restricted from substituting timber harvested from federal lands for privately owned timber that they export. GAO reviewed the magnitude of and the potential impacts from extending the substitution restriction to cover third parties who subsequently acquire Forest Service timber from the original purchasers--an export industry practice commonly referred to as third-party substitution.

According to the Forest Service and timber industry associations, third-party substitution approximates 100 million board feet annually in the western United States. They said that if the practice were banned, some companies could acquire national forest timber at lower prices because of decreased demand and competition, and the lower prices would result in less government revenues. Also, a ban could disrupt traditional log markets and business practices.

The Forest Service believes it could not enforce a ban on third-party substitution without additional legal authority and staff.



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UNITED STATES GENERAL ACCOUNTING OFFICE
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RESOURCES, COMMUNITY,
AND ECONOMIC DEVELOPMENT
DIVISION

B-215907

The Honorable Mark O. Hatfield
Chairman, Committee on Appropriations
United States Senate

The Honorable James A. McClure
Chairman, Subcommittee on Interior
and Related Agencies
Committee on Appropriations
United States Senate

This report discusses our review of the potential impacts of tighter Forest Service log export restrictions in the West. The report responds to your July 25, 1983, joint request letter and to the June 20, 1984, supplemental request of the Chairman, Subcommittee on Interior and Related Agencies, Senate Committee on Appropriations.

As arranged with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report until 3 days from its publication date. At that time, we will send copies to the Director, Office of Management and Budget; the Secretary of Agriculture; and other interested parties. We will also make copies available to others upon request.


J. Dexter Peach
Director



D I G E S T

Since 1974, a provision has been included in every appropriations act for the Department of Agriculture's Forest Service which restricts purchasers of national forest timber from exporting timber harvested from federal lands in the western half (west of the 100th meridian) of the contiguous 48 states. The provision also restricts purchasers from using this timber in their processing facilities while exporting non-federal timber that could be used in those facilities--a practice called direct substitution. (See pp. 2 and 3.)

Forest Service regulations allow purchasers which had been exporting private timber and purchasing national forest timber during the period 1971-73 (historic levels) to continue to do so for up to 110 percent of their average annual volume during those years. Neither the provision nor the regulations prevent others (third parties) from buying Forest Service timber from the purchaser and substituting it for private timber they export--a practice called third-party substitution. (See pp. 8 and 9.)

On July 25, 1983, the Senate Committee on Appropriations requested GAO to determine

--the Forest Service's definition of third-party substitution applied pursuant to current Forest Service regulations,

--the volume of third-party substitution, and

--the potential impacts of banning the practice and the mechanisms the Forest Service would need to administer a ban. (See app. V.)

On June 20, 1984, GAO was requested to expand its review to address several questions related to direct substitution, including concerns about direct substitution in Idaho.

GAO's review was made at Forest Service headquarters and at three of the Service's western regions. According to the Forest Service,

about 90 percent of the third-party substitution occurs in western Washington, mostly in the Grays Harbor area. The remainder occurs in western Oregon and northern California. GAO concentrated its efforts in western Washington since the preponderance was occurring in that area. To determine the potential impacts of a ban, GAO interviewed six forest industry associations, 28 timber companies, and Forest Service administrators. To obtain the data needed with regard to direct substitution, GAO also contacted 51 firms that had historic levels as of August 1984, reviewed in detail timber sales contracts at three national forests in Idaho, and discussed the administration of substitution restrictions with Forest Service timber management officials and export surveillance officers. (See pp. 5 to 7.)

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According to the Forest Service, third-party substitution is defined as the acquisition of national forest timber from the purchaser by a firm which is not eligible to purchase the timber directly because direct purchase would constitute substitution under Forest Service regulations.

According to the Forest Service and timber industry associations, third-party substitution approximates 100 million board feet annually, or about 2 percent of all national forest timber harvested in the western United States. They told GAO that if the practice was banned, a variety of impacts could occur. Representatives of the timber industry said that some companies could acquire national forest timber at lower prices because of decreased demand and competition, and the lower prices would result in less government revenues. Also, banning third-party substitution could disrupt traditional log markets and business practices and force some companies to change their operations or go out of business. The Forest Service stated that it could not enforce a ban on third-party substitution without additional legal authority and staff.

As of August 1984, the total volume of national forest timber that may be used as replacement for private timber to be exported within the substitution regulations amounted to about 490 million board feet. This limitation is

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comprised of the historic levels of 51 firms located in California, Oregon, and Washington. The Forest Service advised GAO that about 100 million board feet of national forest timber is used as replacement for private timber to be exported annually, and Forest Service reports did not show that timber substitution was occurring in Idaho.

VOLUME OF THIRD-PARTY
SUBSTITUTION

The Forest Service is not required by current law and regulations to maintain records on the extent of third-party substitution. As a result, the precise volume of third-party substitution is not available. In the absence of such data, GAO obtained estimates from the Forest Service, the Small Business Administration (which collects data on Forest Service timber sales for its Small Business Timber Sale Set-Aside Program), and a timber industry association.

The Forest Service reported to the Chairman, House Committee on Appropriations, that third-party substitution amounted to 5.4 million, 14 million, and 29 million board feet in fiscal year 1980 and calendar years 1981 and 1982, respectively (latest data available at the time of GAO's review). GAO found that these volumes were understated, however, because Forest Service regions only included sales to third parties which were exporters and did not have established historic levels. The volumes did not include third-party sales to firms that had historic levels and

--had bought national forest timber directly during the year but had reached their historic levels and could buy no more without violating the substitution regulation or

--were not buying any national forest timber that year because they had exceeded their historic export levels.

The Forest Service's Director of Timber Management told GAO he was unaware that the regions were not reporting those sales. On February 1, 1984, the Forest Service issued instructions to regional foresters to begin reporting such sales. (See pp. 10 to 13.)

Tear Sheet

Opponents of third-party substitution, generally the smaller non-exporting firms, believe the volume of national forest timber used in third-party substitution is much larger than that reported by the Forest Service. However, only one association representing small mill operators in Washington provided GAO an estimate--about 200 million board feet annually. GAO believes this estimate is overstated because of the assumptions used regarding some firms' eligibility to buy timber directly from the Forest Service and its inclusion of large volumes of pulp logs not subject to the export restrictions. (See pp. 14 and 15.)

GAO discussed these two estimates with the forester in charge of the Small Business Timber Sale Set-Aside Program in Washington State. On the basis of his experience and data collected in administering the program, he estimated that third-party substitution amounted to about 118 million board feet annually. Officials of the Forest Service and timber industry associations agreed that the Forest Service estimates reported to the Congress were too low, and most thought the opponent's estimate was too high. Most said that the volume is about 100 million board feet annually. (See pp. 15.)

The 100-million-board-feet estimate represents about 2.2 percent of the 4.7 billion board feet of timber harvested in 1982 from national forest lands west of the 100th meridian, and about 17 percent of the national forest timber harvested in western Washington and northwestern Oregon during the same period. (See p. 10.)

POTENTIAL IMPACTS OF BANNING THIRD-
PARTY SUBSTITUTION AND REGULATORY
MECHANISMS NEEDED TO ADMINISTER
SUCH A BAN

According to Forest Service officials and officials of six industry associations and 28 timber companies in Oregon, Washington, and Idaho, a ban on third-party substitution could result in a variety of impacts. Generally, the smaller non-exporting firms favored a ban while the larger export-oriented firms opposed a ban. Likewise, the potential impacts they cited were positive or negative, depending on the nature of the organizations, and covered a wide range of

impacts, from no effect at all to drastic effects on log markets and exports. However, the following were the most frequently cited impacts:

- A reduction in the price of national forest timber because of decreased demand, a reduction in costs to purchasers, and a commensurate reduction in revenues to the government.
- A disruption in the current practice of buying, selling, and trading various species of logs between companies for use in their specialized mills (e.g., plywood mills) so that each can operate efficiently. The disruption in supplies of logs could cause some firms to reduce or change their operations, divest themselves of domestic operations, or go out of business. (See pp. 17 to 22.)

The Forest Service stated that it has authority to control direct substitution by the purchaser of national forest timber but not by third parties. The only sanctions that the Forest Service can invoke for substitution violations are contractual ones against the purchaser, that is, terminating contracts or debarring a firm from bidding on future contracts. The Forest Service said that if third-party substitution were to be prevented, it would need a law prohibiting the export or substitution for export of national forest timber and providing criminal penalties for violating the law.

The Forest Service said it would need additional personnel for field surveillance, monitoring, and compilation of data to administer a ban. The Forest Service estimates that it would need 15 more employees at an additional \$600,000 per year--approximately doubling the present staff and cost of administering the export control program. (See pp. 22 and 23.)

POTENTIAL DIRECT SUBSTITUTION IN IDAHO NATIONAL FORESTS

Forest Service officials said if direct substitution was occurring in Idaho, it most likely would occur in three national forests which serve the Lewiston, Idaho, and adjacent port areas. GAO's review of timber sales contract files for the three national forests, and its discussions with Idaho Forest Service and timber industry officials did not disclose that timber substitution was occurring. (See pp. 6, 7, and 13.)

AGENCY COMMENTS

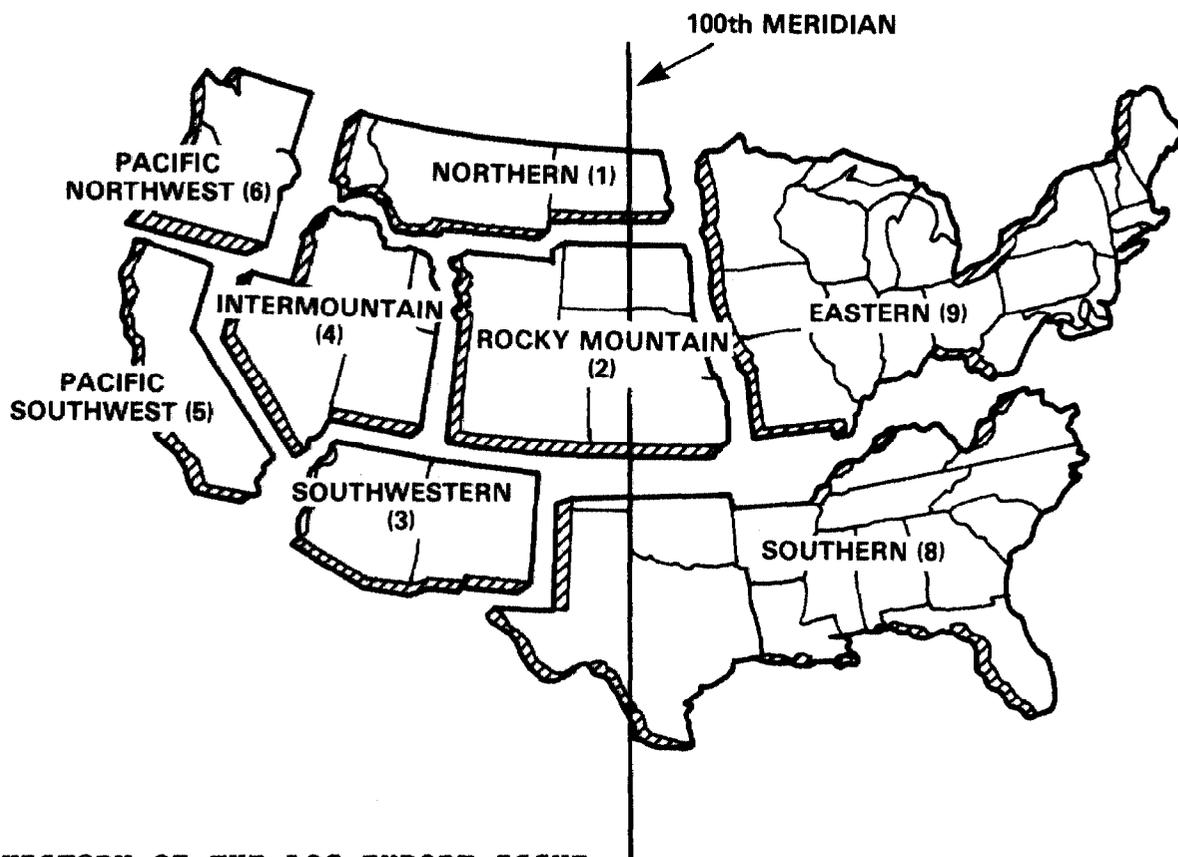
In its July 2, 1984, letter commenting on a draft of this report (see app. IV), the Forest Service said that it concurred in GAO's findings. The Forest Service said that GAO correctly and objectively discussed the situation, the probable magnitude, and the potential impacts of third-party substitution.

The Forest Service provided GAO a copy of the export data reported to the Chairman, House Committee on Appropriations, for calendar year 1983. The reported volume of third-party substitution was 72 million board feet. However, the Forest Service said that if its new reporting requirements were fully implemented, the volume would approximate 100 million board feet. The Forest Service also told GAO that the supplemental data added to this report regarding direct substitution was accurate and fairly presented. (See pp. 9, 15, 16, and 23.)

CHAPTER 1

INTRODUCTION

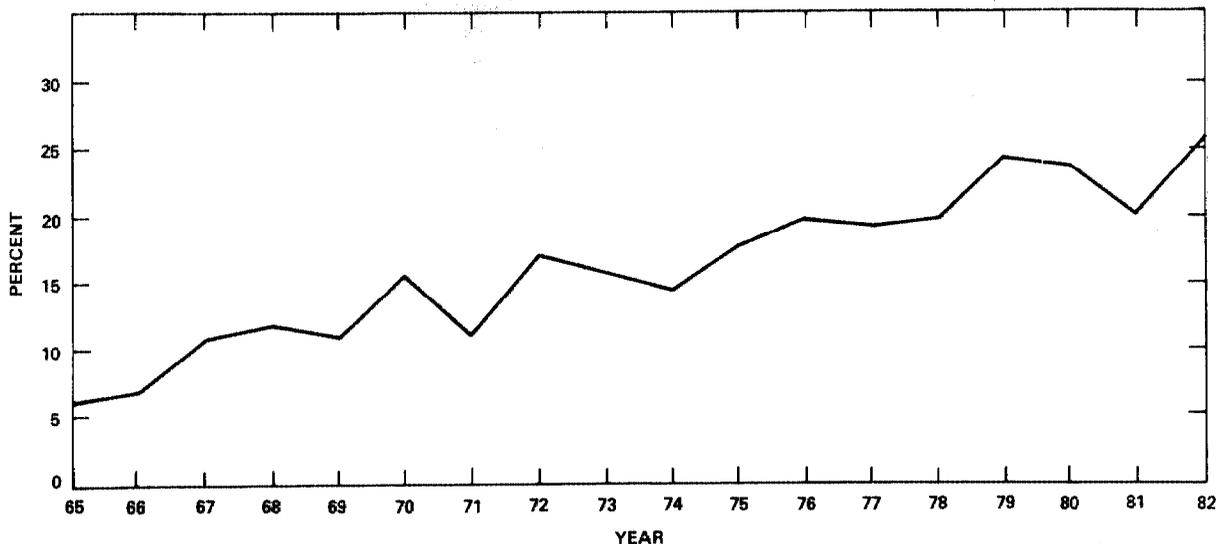
The Department of Agriculture's Forest Service manages and protects 191 million acres of national forest land, most of which is in the western United States. The Forest Service annually sells about 11 billion board feet of timber from the national forests. This timber helps furnish the nation with lumber, plywood, and pulp needed for housing, industrial, and paper product needs. The Forest Service carries out this responsibility through nine regional offices nationwide. Six of these regions manage national forests west of the 100th meridian in the contiguous 48 states--the area subject to Forest Service's log export restrictions.



HISTORY OF THE LOG EXPORT ISSUE

Whether national forest timber should be exported or not has been debated for years in the public and private sectors. Initially, the export market was generally viewed favorably, particularly during the early 1960's, as a needed outlet for selling salvage timber. However, as exports of national forest, private, and other timber grew with time and accounted for a growing share of the timber harvest (see chart on p. 2) public and private concerns were expressed as to the propriety of allowing the unrestricted export of logs because of its effect on the domestic wood-processing industry.

SOFTWOOD LOG EXPORTS AS A PERCENTAGE OF TIMBER HARVEST -
OREGON AND WASHINGTON



On April 16, 1968, the Secretaries of Agriculture and the Interior issued joint orders restricting the volume of timber that could be harvested and exported from Forest Service and Bureau of Land Management (Department of the Interior) lands in unprocessed form. The Secretaries limited the volume of timber that could be exported from federal lands to 350 million board feet annually. They deemed this restriction was necessary to maintain a viable domestic wood-processing industry.

The Secretaries' 350-million-board-foot quota was legislated, effective January 1, 1969, by an amendment to the Foreign Assistance Act of 1968 (82 Stat. 966). The amendment, commonly referred to as the "Morse Amendment," stated that:

"For each of the calendar years 1969 through 1971, inclusive, not more than 350 million board feet, in the aggregate, of unprocessed timber may be sold for export from the United States from Federal lands located west of the 100th meridian."

Section 921 of the Housing and Urban Development Act of 1970 (84 Stat. 1817) extended the expiration date for this provision to December 31, 1973.

In October 1973, a provision attached to the Department of the Interior and Related Agencies Appropriation Act, 1974 (P.L.

93-120, Oct. 4, 1973) in effect prohibited the export of unprocessed timber harvested from federal lands in the West.¹ The act stated that:

"No part of any appropriation under this Act shall be available to the Secretaries of the Interior and Agriculture for use for any sale hereafter made of unprocessed timber from Federal lands west of the 100th meridian in the contiguous 48 States which will be exported from the United States, or which will be used as a substitute for timber from private lands which is exported by the purchaser: Provided, That this limitation shall not apply to specific quantities of grades and species of timber which said Secretaries determine are surplus to domestic lumber and plywood manufacturing needs."

This provision has been attached to all subsequent Interior and Related Agencies Appropriation Acts.

As written, the provision also prohibited purchasers from using timber harvested from federal lands in their processing facilities while exporting non-federal timber that could have been used in those facilities. This practice is termed "direct substitution." However, in a February 1974 letter to the Chief of the Forest Service, the Chairman, Subcommittee on Interior and Related Agencies, House Committee on Appropriations, explained that the Committee intended to allow historic patterns of trade to continue without disruption. The Chairman said the provision was intended to prohibit firms in the export trade from increasing their log exports in the future through direct substitution.

In March 1974, the Forest Service established regulations implementing the provision, including the provision's restriction on log substitution. The Forest Service defined "purchaser" to mean the person who purchases national forest timber directly from the Forest Service. This definition precludes the purchaser from substituting or replacing private exported timber with national forest timber. The regulations do not prevent others (third parties) from buying the national forest timber from the purchaser and substituting it for the private timber they export. This practice is termed "third-party substitution." A more detailed description of the Forest Service's definition of direct substitution and third-party substitution is discussed in chapter 2.

In 1979, some members of the forest industry began urging the Congress to ban third-party substitution. Subsequently, several

¹Not applicable to species determined by the Secretary of Agriculture to be surplus to domestic needs. The Forest Service reported that surplus species accounted for about 0.06 percent of the timber harvested in 1982.

Members of Congress requested the Forest Service to hold hearings on the third-party substitution issue. These hearings were held in Portland, Oregon, and Seattle, Washington, in August 1979. Fifty-one witnesses testified, including Members of Congress; officials of forest products companies, industry associations, port authorities, stevedoring firms, unions, and Washington State; and representatives of public interest groups. Thirty opposed third-party substitution, and 21 favored continuing the practice.

Those opposed to third-party substitution urged the Forest Service or the Congress to ban the practice because it was damaging the domestic manufacturing industry. They testified that third-party substitution was (1) increasing the timber harvest, thus depleting the national forests, (2) depriving domestic manufacturers of raw materials, thus reducing employment opportunities, and (3) increasing demand for timber, thus driving prices up.

Organizations involved in exporting logs, however, were in favor of third-party substitution. They testified that a ban on the practice would be costly and difficult for the Forest Service to administer, and that it would eliminate jobs at exporting facilities and at exporter-owned domestic mills. They also testified that a ban would disrupt the desirable practice of exchanging logs to obtain species, sizes, and grades best suited for individual plant operations.

The Forest Service advised the Members of Congress who had requested the hearings that the Forest Service opposed a ban on third-party substitution. The Forest Service said the volume of such substitution was small and that if forced to make a choice, private landowners would suspend domestic mill production rather than forego the export market for their private logs. In addition, the Forest Service said a ban would be difficult and costly to administer and would disrupt traditional log markets, placing a hardship on the industry.

In May 1980 and February 1981, Representative James H. Weaver of Oregon introduced legislation to protect domestic timber supplies (H.R. 7255 and H.R. 639). Both bills included provisions to limit or eliminate substitution of timber from federal land for private exported timber, including third-party substitution. In conjunction with these bills, the Subcommittee on Forests, Family Farms, and Energy, House Committee on Agriculture, held hearings at which many concerns expressed in the 1979 Forest Service hearings were repeated. Neither bill passed.

In 1983, the Senate Committee on Appropriations discussed the issue of third-party substitution. The Committee's Report No. 98-184 on the Department of the Interior and Related Agencies Appropriation Bill for 1984 stated that the Committee would

request us to investigate the matter of third-party substitution in the Forest Service timber sales program.

OBJECTIVES, SCOPE, AND METHODOLOGY

On July 25, 1983, pursuant to the Committee's report, the Chairman, Senate Committee on Appropriations and the Chairman, Subcommittee on Interior and Related Agencies, Senate Committee on Appropriations, requested us to provide the following information (see app. V):

- The Forest Service's definition of third-party substitution pursuant to current Forest Service regulations.
- The federal timber volumes affected by this substitution, and the current magnitude of the export program and the indirect substitution problems.
- The potential impact that expanding the current prohibition to include third-party purchasers would have on the industry and the public, and the feasibility of the Forest Service to administer such a prohibition.
- Other regulatory mechanisms that would be used in administering such a prohibition.

In subsequent discussions with the requesters' offices, we agreed to (1) provide the Forest Service's definition of third-party substitution, (2) determine the volume of national forest timber used in third-party substitution, and (3) determine the impacts of banning such substitution and identify the mechanisms needed by the Forest Service to implement a ban. In addition, we agreed that our review would be limited to the Forest Service's national forest system and that we need not study the Department of the Interior programs or the non-federal timber export market. Furthermore, we agreed that our review would be done in the following states located in three Forest Service regions: Washington and Oregon (region 6), California (region 5), and Idaho (region 1).

To obtain a definition of third-party substitution, we reviewed transcripts of previous Forest Service and congressional hearings and interviewed Forest Service timber management officials. We also asked the Forest Service's Director of Timber Management to provide the Forest Service's official definition.

To ascertain the volume of timber involved in third-party substitution, we interviewed Forest Service timber management staff and reviewed records at three Forest Service regional offices and at four national forests. Since the Forest Service advised us that about 90 percent of all third-party substitution occurs in western Washington (region 6), we concentrated on this area. The area is served mainly by four national forests--Mount

Hood in Oregon; and Olympic, Gifford Pinchot, and Mount Baker-Snoqualmie in Washington. In addition, we reviewed files and talked to officials in the Seattle office of the Small Business Administration. These officials administered the Small Business Timber Sale Set-Aside Program under which much of the national forest timber is sold. The Small Business Administration collects statistical data on the disposition of timber from national forest timber sales sold to small businesses.

To determine the effect of a ban on third-party substitution, we talked with six forest industry associations representing over 250 firms in Oregon, Washington, and Idaho. We obtained the views of the trade association officials and asked them to identify representative companies in their associations which could describe how a ban would affect the industry and their individual operations. From the lists of companies they furnished, we judgmentally selected 28 companies in Oregon, Washington, and Idaho and spoke with their officials. In our selection, we tried to achieve a mix of proponents and opponents of third-party substitution. Also, we talked to Forest Service program administrators to determine the feasibility of administering a ban on third-party substitution. A listing of the private companies, associations, and federal agencies we interviewed is shown in appendix I.

To determine regulatory mechanisms which could be used to administer a ban on third-party substitution, we interviewed the Forest Service's Director of Timber Management and his staff at Forest Service headquarters and the timber management staff in region 6. In addition, we reviewed transcripts of the 1979, 1980, and 1981 congressional hearings dealing with third-party substitution.

At the conclusion of our review into the third-party substitution issues, the Chairman, Subcommittee on Interior and Related Agencies, on June 20, 1984, requested us to expand our review and answer several questions related to direct substitution. Specifically, he asked us to expand our review to include a discussion of timber tributary areas, add additional material on historical levels of timber exports by firms having contracts for federal timber, and obtain 1983 Forest Service data on third-party substitution.

The Chairman's staff in subsequent discussions advised us that the Chairman was especially concerned that substitution might be occurring in the state of Idaho--particularly in the Lewiston area. We agreed, therefore, to analyze the disposition of national forest timber which might have flowed into the Lewiston, Idaho, and the adjacent Clarkston, Washington, port areas and been substituted by either the purchasers or third parties for private timber exported. The Forest Service identified three national forests in Idaho which could be likely sources of logs for those areas--the Clearwater, Nez Perce, and Panhandle.

We reviewed contract files for timber sales made between January 1, 1983, and July 1, 1984, by the Clearwater, Nez Perce, and Panhandle national forests. In each file we examined purchaser certifications of historic levels of purchase and export, non-substitution of timber purchased, and disposition of domestically processed and exported timber. The purpose of reviewing these certifications was to detect any instances where purchasers had (1) substituted national forest timber for private exported timber or (2) sold such timber to a third party who was an exporter that may have used it in substitution.

We reviewed Forest Service regulations and manuals dealing with tributary areas and discussed control procedures with Forest Service timber management officials and export surveillance officers in region 6 and in Washington, D.C. We also examined correspondence between national forest timber purchasers and region 6 timber management staff in which the latter ruled on substitution questions and established policies on tributary areas, historic levels, and substitution.

To ascertain the companies with historic levels, the volumes of timber involved, the tributary areas to which the levels pertained, and to identify any changes which might have taken place,

--we requested the Forest Service to provide us the most current data for all regions with forests subject to the export restrictions (regions 1-6) and

--we contacted all companies identified by the Forest service and asked them to verify or correct the Service's data.

Our review was made in accordance with generally accepted government auditing standards.

CHAPTER 2

THIRD-PARTY SUBSTITUTION

As requested, we asked the Forest Service to define third-party substitution pursuant to current Forest Service regulations. In his letter to us dated January 11, 1984, the Acting Associate Deputy Chief of the Forest Service stated that:

"Third-party substitution is the acquisition of National Forest timber from a National Forest timber sale purchaser by a firm which is not eligible to purchase the National Forest timber directly because direct purchase would constitute substitution under 36 CFR 223.10."

Forest Service regulations (36 CFR 223.10) define direct substitution as the purchase of unprocessed national forest timber to be used as replacement for unprocessed timber from private lands which is exported by the purchaser. Unprocessed timber means, in general, trees or round logs that have not been processed into lumber or by-products. The purchaser is the person who purchases national forest timber directly from the Forest Service.

According to the regulations, substitution occurs when (1) a purchaser increases its national forest timber purchases in any calendar year more than 10 percent above its historic level and in the same calendar year exports unprocessed timber from private land in the tributary area or (2) a purchaser increases exports more than 10 percent above its historic level in any calendar year while the purchaser has national forest timber under contract.

Historic level is the average annual volume of unprocessed timber purchased or exported in calendar years 1971, 1972, and 1973. According to the Forest Service, as of August 1984 the total volume of national forest timber that may be used as replacement for private timber to be exported within the substitution regulations amounted to about 490 million board feet. This limitation is comprised of the purchase and export historic levels of 51 firms located in the states of California, Oregon, and Washington. The Forest Service also advised us that about 100 million board feet of national forest timber is used as replacement for private timber to be exported annually. A detailed breakdown of these historic levels by company and their tributary areas is in appendix II.

A tributary area is that geographic area from which unprocessed timber is delivered to a specific processing facility or complex. A purchaser who hauls timber over long distances will have a large tributary area, whereas a purchaser who has purchased timber close to its mill will have a relatively small tributary area. According to Forest Service procedures, a tributary area will be expanded if the log supply area expands.

However, reductions in the tributary area shall be made only after a definite change in purchasing is clearly established.

Firms that did not purchase national forest timber or export private timber from a specific tributary area during the years 1971-73 would not have historic levels in that area. As a result, the regulations make these firms ineligible to purchase national forest timber in the tributary area in any year in which they export private timber from it. In addition, firms with historic levels that are exporting private timber from a tributary area become ineligible to purchase more national forest timber in that area from the Forest Service in any 1 year once they reach 110 percent of either historic level--purchase or export--for that tributary area. Pertinent Forest Service procedures regarding historic levels and tributary areas is in appendix III.

According to a December 7, 1976, opinion of the Department of Agriculture's Office of the General Counsel, the substitution regulation (36 CFR 223.10) applies only to purchasers buying directly from the Forest Service. The General Counsel concluded that the regulations, as written (1) do not prohibit a third party that buys national forest timber from exporting other logs and (2) may not be extended to cover third parties who buy from direct purchasers of national forest timber. Hence, purchasers are not restricted from selling timber to a third party.

AGENCY COMMENTS

The Forest Service said that we correctly cited its definition of third-party substitution. (See app. IV.) The Forest Service also told us that the supplemental data we developed on direct substitution was accurate and fairly presented.

CHAPTER 3

MAGNITUDE OF THIRD-PARTY SUBSTITUTION

The Forest Service is not required by current law and regulations to maintain records on the extent of third-party substitution of national forest timber. Therefore, information on the precise volume of third-party substitution is not available. However, the Forest Service has estimated the volume of such substitution for fiscal year 1980 and calendar years 1981 and 1982. The Service reported that third-party substitution has not exceeded 29 million board feet annually during those years. Timber industry representatives that favor restricting substitution stated that the Forest Service estimates were low and that the volume was about 200 million board feet annually. Basic data from which we could make a precise estimate were not available from either the Forest Service or timber industry. On the basis of our review of the above estimates; the facts, assumptions, methodology used, and other information; and discussions of the estimates with Forest Service and timber industry representatives, the extent of third-party substitution appears to be between the two estimates. According to the Forest Service and timber industry associations, third-party substitution amounted to about 100 million board feet annually.

One hundred million board feet represents about 2.2 percent of the 4.7 billion board feet of national forest timber harvested in regions 1 through 6 in 1982--a relatively small amount. However, according to the Forest Service, about 90 percent of the third-party substitution occurs in western Washington; therefore, the amount becomes more significant if compared with timber harvested from national forests serving this geographic area. In 1982, for example, this would have been about 17 percent of the timber harvested in the one northwestern Oregon and three western Washington national forests.

FOREST SERVICE VOLUME ESTIMATES HAVE BEEN LOW

The law and regulations pertaining to controlling both the export and substitution of national forest timber do not require that the Forest Service monitor and report on third-party substitution. However, in House Report 96-1147 on the fiscal year 1981 Appropriations Bill for the Department of the Interior and Related Agencies, the House Committee on Appropriations stated that it continued to receive complaints about the growth of third-party substitution; it therefore directed the Forest Service,

" . . . if feasible, to investigate and report on . . . volumes of logs purchased from or sold to third parties and substituted for exported private logs over the last year by individual buyers and sellers."

In response to this directive, the Forest Service has submitted reports to the Chairman, House Committee on Appropriations, for fiscal year 1980 and calendar years 1981 and 1982. Calendar year 1983 data had not been compiled and reported when we completed our review.¹

The Forest Service reported to the Committee that it considered third-party substitution to be insignificant during 1980 and 1981. The 1980 report stated that "The volume involved in third-party substitution is not significant to the overall timber supply situation in the Northwest and does not justify additional regulations." The 1981 report concluded that "The minor volume of possible third-party substitution does not warrant additional regulations." Finally, with respect to the 1982 statistics, Forest Service officials told us that, in their opinion, this volume was still insignificant, and more restrictive regulations were not warranted.

The reports showed the volume of national forest timber harvested in Forest Service regions west of the 100th meridian in the contiguous 48 states and subsequently sold to third parties. The reports also showed that all third-party substitution occurred in California, Oregon, and Washington, with no third-party substitution occurring in Idaho. The following table shows the volume (in million board feet) reported by the Forest Service for fiscal year 1980 and calendar years 1981 and 1982.

¹On July 2, 1984, the Forest Service provided us its 1983 report to the Committee. (See app. IV.)

<u>Year</u>	<u>States</u>	<u>Total harvest volume</u> (million board feet)	<u>Third-party substitution</u>	
			<u>Volume</u>	<u>Percent of harvest</u>
1980	Calif., Oreg., & Wash.	4,292	5.4	0.1
	Remaining states	<u>1,255</u>	<u>None</u>	None
	Total	<u>5,547</u>	<u>5.4</u>	0.1
1981	Calif., Oreg., & Wash.	4,071	14.0	0.3
	Remaining states	<u>1,690</u>	<u>None</u>	None
	Total	<u>5,761</u>	<u>14.0</u>	0.2
1982	Calif., Oreg., & Wash.	3,395	29.0	0.9
	Remaining states	<u>1,256</u>	<u>None</u>	None
	Total	<u>4,651</u>	<u>29.0</u>	0.6

The Forest Service has acknowledged that the reported volumes may not account for all timber sold to third parties during those years. The volumes were developed from reports provided to the Forest Service by national forest timber purchasers. These reports, which are required by the Forest Service, show the disposition of unprocessed national forest timber harvested by purchasers during the previous year. However, when the Forest Service implemented the reporting requirements in 1981, they were not made retroactive to earlier timber sales. As a result, sales made before that time are subject to different reporting requirements which require purchasers to report the disposition of harvested timber only when a sale is completed. Many of these older sales are still not completed; therefore, the disposition of the timber has not yet been reported.

Uncompleted sales may partially explain why the Forest Service understated the volumes. However, we also found that Forest Service personnel in the national forests were not reporting certain types of sales which represented potential third-party substitution. To verify the accuracy of the reported data, we visited all three national forests in western Washington and one in northwestern Oregon, and analyzed the Forest Service records. In general, the records only included sales to third parties that

were exporters with no historic levels of national forest timber purchases or private timber exports. The existing records did not account for

--third-party purchases by firms with historic levels that had bought national forest timber directly during the year but reached their purchase and/or export ceilings and therefore could buy no more and

--third-party purchases by firms with historic levels that were not attempting to buy national forest timber directly that year because they were exceeding their historic export levels.

An official of a company in the first category told us that the company makes third-party purchases of millions of board feet of national forest timber annually--9 million board feet in 1983--to supplement its direct purchases of national forest timber. The company, which exports private timber, explained that it owns a mill which requires the type of large, old-growth timber available from the national forests--the only source for such timber in the area. The mill's capacity is greater than the company's own historic purchase level; therefore, the company must periodically make third-party purchases of additional national forest timber to keep its mill in full production.

An exporting company in the second category testified at the 1979 Forest Service hearings that it makes third-party purchases of 60 million board feet of national forest timber annually for its domestic mill operations. These volumes were not reported in the Forest Service's records. In January 1984, this company told us that it was still exporting large quantities of private logs and making third-party purchases of Forest Service timber for its mills.

The Forest Service's Director of Timber Management told us he was not aware that national forests were not reporting timber sold to third-party companies in these two categories. He agreed that such sales should be reported as potential third-party substitution. On February 1, 1984, the Forest Service instructed the Regional Foresters in regions 1 through 6 to include sales in these two categories in addition to those they had been reporting to the House Committee on Appropriations.

In addition, because of Chairman McClure's particular concerns regarding the potential for substitution in the Lewiston area of Idaho, we reviewed the contract files which showed the disposition of Forest Service timber sales made in the 3 national forests that serve the Lewiston area. Our analysis showed that none of the timber from these national forests was substituted for privately exported timber.

ESTIMATE BY OPPONENTS OF THIRD-PARTY
SUBSTITUTION APPEAR HIGH

Those who oppose third-party substitution have stated that they believe the volume of timber involved in such substitution is large. One forest industry association estimated that the volume was about 200 million board feet in 1979. The association represents about 30 companies that operate lumber, plywood, veneer, and shake and shingle mills in Washington state.

The association's executive vice-president testified before the Subcommittee on Forests, Family Farms, and Energy, House Committee on Agriculture, in 1980 and 1981 that he believed about 200 million board feet of national forest timber was used annually in third-party substitution in western Washington and along the Columbia River. This estimate was the only one we found, other than those of the Forest Service, that attempted to quantify the volume. This official told us that he made his estimate mainly on the basis of discussions with timber buyers in western Washington and northwestern Oregon. He stated that in many cases where information could not be obtained directly from the companies involved, it was obtained from those which regularly did business with the companies and represented the collective best estimates of those interviewed. He said that some data were taken from testimony that companies presented at the Forest Service-sponsored hearings in 1979. He expressed the belief that the 200-million-board-foot volume figure represented most of the third-party substitution.

The official specifically identified nine companies that he believed were restricted from purchasing national forest timber sales because of their private log-exporting activities. He stated that in 1979, these nine companies purchased 165 million board feet of national forest timber from original national forest timber purchasers.

We found, however, that five of the nine companies which the official estimated had combined third-party purchases of 50 million board feet were eligible to purchase national forest timber directly from the Forest Service. All five had historic purchase and export levels. Four of the five were awarded national forest timber sale contracts in 1979. And all five had active national forest timber contracts with region 6 as of June 30, 1983.

Also, we found that the association's estimate included 60 million board feet for another company, on the basis of that company's testimony in the 1979 Forest Service hearings. Included in this amount were 10 to 20 million board feet of pulp logs which are not subject to export restrictions.

The association official told us that he believed his estimate was representative at the time he testified but that the

volume might be lower for more recent years because of the downturn in the economy.

POTENTIAL VOLUME PROBABLY AVERAGED
100 MILLION BOARD FEET ANNUALLY

After reviewing the two sets of estimates and the assumptions and methodology used to make them, it appears that the amount of third-party substitution was probably between the high and low estimates. We discussed these estimates with the forester in charge of the Small Business Administration's Small Business Timber Sale Set-Aside Program in Washington state. On the basis of his experience and data collected in administering the program, he estimated that the volume of third-party substitution in Washington averaged about 118 million board feet annually during the period 1976-80.

We discussed this estimate with officials of three timber industry associations in Washington and Oregon. One official said the estimate was low, while the other two believed that 100 million board feet was probably a good estimate.

We also discussed the estimate with Forest Service headquarters officials. The Director of Timber Management questioned certain assumptions the Small Business Administration official had used to estimate the volume but agreed that about 100 million board feet annually may be a reasonable estimate. The Director said that several years ago, he and his staff estimated that potential third-party substitution was about 100 million board feet, mostly in the Grays Harbor area of Washington. In a letter to us dated January 11, 1984, the Acting Associate Deputy Chief of the Forest Service confirmed this:

"When log export hearings were held in 1980, we developed estimates that about 100 million board feet of National Forest timber was being sold to third parties who were not eligible to buy the timber directly."

Neither official could tell us why the Forest Service reported lesser amounts to the House Committee on Appropriations for 1980, 1981, and 1982, except that those were the volume estimates the regions had submitted. Both the Acting Associate Deputy Chief and the Director said they believed the volume of timber involved in third-party substitution was probably less than 100 million board feet in 1983 because of the decreased level of export in the last several years.

AGENCY COMMENTS

The Forest Service said that we have provided an objective discussion of the situation and probable magnitude of third-party substitution. (See app. IV.) The Forest Service also provided us a copy of its 1983 export data (not available at the time of our

review) reported to the House Committee on Appropriations. The Forest Service reported the volume of third-party substitution during calendar year 1983 to be 72 million board feet. However, it stated that possibly more than 72 million board feet was involved because its reporting system neither accounted for older sales nor included those types of sales cited on page 13. The Forest Service concluded by saying that if its new reporting requirements were fully implemented, the level of third-party substitution would approximate 100 million board feet.

CHAPTER 4

POTENTIAL IMPACTS OF BANNING THIRD-PARTY SUBSTITUTION, AND REGULATORY MECHANISMS NEEDED TO ADMINISTER SUCH A BAN

As discussed in chapter 1, Members of Congress; the Forest Service; officials of the forest products companies, industry associations, port authorities, stevedoring firms, and unions; and representatives of public interest groups have expressed strong views in earlier Forest Service hearings both for and against a ban on third-party substitution.

According to timber companies and industry associations, the imposition of a ban on third-party substitution would result in a variety of impacts. Generally, the smaller non-exporting firms favored a ban while the larger export-oriented firms opposed a ban. Likewise, the potential impacts they cited were positive or negative, depending on the nature of the organizations, and covered a wide range of impacts, from no effect at all to drastic effects on log markets and exports. However, the most frequently cited impacts of a ban were that (1) the price of national forest timber would be reduced because of less demand and competition, (2) traditional log buying and trading practices would be disrupted, (3) certain firms would have to change their practices, divest themselves of incompatible plant operations, or even go out of business, and (4) the Forest Service would probably receive less revenue when selling timber. These impacts, for the most part, would be experienced in western Washington, especially in the Grays Harbor area.

The Forest Service believes it would not be able to administer a ban on third-party substitution under its current authority and with its present resources. If it were banned, Forest Service officials said they would need new legislative authority to invoke sanctions against those practicing third-party substitution and would need more personnel and funds to carry out a monitoring and surveillance program to ensure compliance with a ban.

POTENTIAL IMPACTS OF BANNING THIRD-PARTY SUBSTITUTION

In 1982, the forest industry in Oregon, Washington, and Idaho that could be affected by a ban comprised about 3,700 firms, employing about 88,000. About 72 percent of these firms were logging companies, employing about 30 percent of the workforce. The remaining firms were mostly lumber, veneer, and plywood mills. These firms ranged from small, family-owned mills employing a few people and owning no timberland, to very large publicly owned corporations with numerous mills, thousands of employees, millions of acres of their own timberland, and several hundred million board feet of log exports.

These firms differ in their historical operating practices and geographical location which determines, in part, their ability to purchase national forest timber and export private logs. Therefore, the impact of banning third-party substitution of federal logs would vary in nature and severity depending on the firm's location, source of logs, type of markets, and type of facilities--all of which influence historical operating practices.

To assess the impacts of banning third-party substitution, we interviewed Forest Service officials and officials of six industry associations and 28 timber companies in Oregon, Washington, and Idaho.

Four industry associations interviewed favored banning substitution. These organizations represented about 175 mainly small, non-exporting firms. The other two, which represented about 85 firms involved in forest products and log-exporting industries, favored continuing existing substitution practices.

Of the 28 timber companies interviewed, half were engaged in log export activities and half were not. They were almost evenly split between those favoring third-party substitution and those wishing to ban it. The 14 exporters favored continuing the existing practice, 13 non-exporters wished to ban it, and 1 had no comment.

The Forest Service officials we interviewed opposed banning third-party substitution. They believed that such a ban would be costly and nearly impossible to enforce and that the estimated volume of third-party substitution did not justify additional controls.

During our review, we asked the industry associations and timber companies to describe how a ban on substitution would affect their operations--either negatively or positively. They mentioned a variety of impacts, of which the most frequently cited were

- a reduction in the price of national forest timber because of decreased demand, a reduction in costs to purchasers, and a commensurate reduction in revenues to the government and

- the current practice of buying, selling, and trading various species of logs between companies for use in their specialized mills (e.g., plywood mills)--so that each can operate efficiently--would be disrupted, causing some firms to reduce or change their operations, divest themselves of domestic operations, or go out of business.

These impacts are discussed in detail below.

Some firms would benefit from lower national forest timber prices

Thirteen companies and the six industry associations told us they believed that banning third-party substitution would cause national forest timber prices to decrease. They believed that large firms which exported their own and other private timber had increased their domestic use of national forest timber acquired through third parties, thus increasing the demand and price of national forest timber. A ban, they said, would reduce that demand and the price, thus increasing the profits of those firms still able to buy national forest timber.

Seven companies and four associations told us they favored banning substitution for the above reason. Two of these companies said they cannot compete for national forest timber with firms that export logs. The other five said the large firms make large profits on their exports of privately owned timber, which enables them to pay high prices to logging companies that purchase national forest timber. The logging companies, in turn, can outbid non-exporting mill operators for national forest timber. The seven companies and four industry associations said that exporting companies employ agents (usually logging companies) to purchase national forest timber, then resell that timber to the exporting companies for use in their domestic mills.

Three of the companies and one association, however, said that such factors as inflation psychology, bidding practices, and speculation have a much larger impact on timber prices than the incremental demand resulting from third-party purchases. One mill operator said he could not continue to operate very long with production and timber costs equaling \$250 per thousand board feet when market prices for processed lumber were only \$220 per thousand board feet. Regardless of the cause, high timber prices continue to be a primary concern to many companies.

The Forest Service and 13 companies and 5 associations we talked to told us that a ban on third-party substitution would reduce national forest timber sale revenues, thus reducing Department of the Treasury receipts. Because a ban on substitution will reduce the demand for national forest timber, the Forest Service would probably receive lower bids for the timber. The actual extent to which reduced demand would affect price is uncertain. It would depend on many variables, including the supply of Forest Service timber in a particular area, the degree of change in competition resulting from a ban on third-party substitution, and the perceived economic outlook for the industry.

Lower bids for Forest Service timber could result in part from increased transportation costs associated with transporting timber that the original purchaser cannot efficiently use. This readjustment of established log markets would involve added transportation costs, which would be reflected in compensating lower

bid prices for national forest timber. These increased transportation costs would be greatest in Washington's Grays Harbor area because it has few non-exporting local mills to buy excess logs. Log markets would have to be found in Olympia and Tacoma, Washington, some 50 to 75 miles away. However, in other areas, such as Oregon's Willamette Valley, the ban would probably have little effect because many non-exporting mills are available to buy the logs.

If other processors are not found for those species, grades, or sizes of timber that the purchaser's mill cannot process efficiently, the purchaser may elect to process the timber regardless of inefficiencies or sell the timber for pulp, which returns a lower price. Doing either would reduce the financial return on this timber, and therefore would be reflected in the price offered for national forest timber.

Traditional log markets and business practices would be disrupted

Nearly every national forest timber sale in the Pacific Northwest includes some species, sizes, or grades of timber which cannot be efficiently processed in any one timber-processing facility owned by the purchaser. Furthermore, few, if any, firms own a sufficient variety of mills within a small enough geographical area to efficiently use the variety of timber contained in an individual sale. Most timber generally cannot be economically hauled more than about 100 miles. Virtually all mills must buy, sell, and exchange logs to obtain the species, grades, and sizes of logs which best fit their specific facilities and dispose of those that do not. Thus, a ban on third-party substitution would disrupt existing patterns of buying and selling logs and require purchasers of national forest timber to locate new buyers for species, grades, and sizes of logs that they cannot efficiently process in their mills.

The logging companies now purchasing national forest timber and reselling it solely to exporting companies for their domestic operations would no longer be able to do so. This may force some logging companies out of business, thus reducing competition. Others, whose remaining customers are non-exporting domestic manufacturers, may not be able to pay as much for national forest timber because they may not be able to resell it for as much as they did to exporting companies.

Fifteen companies and 3 industry associations told us that a ban on third-party substitution would disrupt these traditional log markets. However, they differed on what they believed the nature and extent of the disruption would be because each firm would be affected differently.

Officials of one large company described how a ban on third-party substitution would disrupt its operations. This company exports about 120 million board feet of privately obtained logs

annually and buys about 40 million board feet directly from the Forest Service each year to supply its one "old growth" lumber mill in Oregon. Both of these transactions are within the company's 1971-73 historical levels. The company's mill requires about 45 million board feet of large old-growth logs--logs typically found in national forest timber sales. However, when the company harvests the 40 million board feet of national forest timber annually, it usually obtains only about 20 million board feet of logs suitable for its old-growth mill. The remaining 20 million board feet of timber harvested is resold to other local mills. The company buys the additional 25 million board feet of old-growth timber needed to supply the mill from other sources. About one third of the old-growth timber is acquired from other purchasers of national forest timber through third-party purchases.

A ban on third-party substitution would require this company to seek old-growth logs from other sources farther away--such as the Washington State Department of Natural Resources--at a higher cost. Or, the company may choose to close its mill if these higher costs make this already marginal mill uneconomical to operate. In addition, firms now selling national forest timber to the company could incur higher trucking costs to move that timber to other non-exporters' mills that are capable of processing old-growth timber.

Furthermore, a ban on third-party substitution would force some other companies to change or cut back operations, such as curtailing one or more shifts at a mill, while forcing others to choose between continuing to export logs or operating their domestic mills. For example, in 1979 when testifying at Forest Service hearings, four companies in the Grays Harbor area of Washington each stated that it would continue to export and, if necessary, discontinue its domestic mill operations if third-party substitution were banned. Their positions remain essentially the same today. A ban on third-party purchases would, therefore, have little impact on the export level. These four companies are major log exporters, with combined 1983 exports of about 700 million board feet.

Twelve companies told us that, if third-party substitution were banned, they would either divest themselves of their domestic mill operations or severely curtail them. These companies' facilities would be either abandoned, sold to firms eligible to purchase national forest timber (if possible), or cut back in production. These actions could result in severe economic and social dislocations for many employees at the facilities.

For example, the vice-president of one company that owns a mill and log-exporting firm in the Grays Harbor area told us that company officials have decided to close or sell the plant if

forced to choose between continuing to export logs and operating the domestic mill. The mill might be sold or, lacking a buyer, closed--increasing unemployment by about 150.

The vice-president of another firm with several mills and log-export activity said that he did not like the current situation allowing third-party purchases, ". . . but I've learned to live with it." He said he and the industry had learned to operate under the existing rules and regulations and that to change them would disrupt his and others' operations. These disruptions would include ceasing 2 million to 3 million board feet of log exports in one area and locating a new source of logs in another.

The executive vice-president of one industry association stated that he doubted if banning third-party substitution would seriously disrupt existing log markets. In his opinion, only two or three companies in western Washington would have to decide whether to reduce log exports or divest themselves of mills. He believed many more companies would elect to reduce exports than divest themselves of their mills.

The vice-president of another association, which is composed of 24 plywood mills and sawmills, told us that Oregon's Willamette Valley would also experience little adverse impact. He said that numerous, small non-exporting companies are in the area and that finding a market for surplus logs would be no problem.

REGULATORY MECHANISMS NEEDED TO ADMINISTER A BAN

According to the Forest Service, under its existing authority and with its current resources, it cannot administer a ban on third-party substitution. The Director of Timber Management told us that the only prohibition against export or substitution for export is provided in the annual appropriations provision, which permits contractual penalties--termination of contracts and debarment from bidding on future contracts--against the original purchaser.

The Acting Associate Deputy Chief of the Forest Service told us that:

"If the present export language of the Appropriation Act were revised, the Forest Service would revise the log export provisions of the timber sale contract to prohibit the resale of logs to third parties who were not eligible to purchase the sales directly. The provision would also require the purchaser to incorporate a similar requirement in any subsequent resale agreement. The problem in enforcement would be that the Forest Service has a contractual arrangement only with the original purchaser. If the third-party were to resell the logs to someone who was not eligible to buy them directly the Forest Service's only recourse would

be against the original purchaser. An action against the original purchaser under such circumstances is of doubtful outcome."

In effect, therefore, no sanctions exist which the Forest Service can invoke to penalize third-party purchasers from substituting national forest timber for private exported logs. Also, because the Forest Service has no contractual relationship with third-party purchasers, monitoring sales and trades of private timber would be difficult, if not impossible. The Director of Timber Management said that if third-party substitution were to be prevented, the Forest Service would need a law prohibiting the export or substitution for export of national forest logs and providing criminal penalties for violating it.

The Director also said that the cost and level of work that would be required to enforce a ban on third-party substitution would be high because of the need for tracking subsequent sales. The Acting Associate Deputy Chief of the Forest Service said that:

"In order to make the added contractual language meaningful additional efforts in sale administration would be required. We estimate this effort would require an additional 15 person years and about \$600,000 per year."

The Forest Service's Timber Management staff prepared this estimate. We were told that it provided for 14 more employees in regions 5 and 6, and one employee in region 1. The Forest Service informed us that as of January 1984, the Service was spending 16 person years to administer its export control program at a cost of about \$500,000 annually.

AGENCY COMMENTS

The Forest Service agreed with our discussion of the potential impacts of third-party substitution and said that they would be costly and complex. (See app. IV.) It also confirmed that additional authority would be necessary to administer an effective ban on such substitution.

COMPANIES AND ASSOCIATIONS INTERVIEWED
CONCERNING THIRD-PARTY SUBSTITUTION

COMPANIES

Oregon

Bald Knob Land & Timber Company
Battles Logging Company
Caffall Brothers Forest Products, Inc.
Crown Zellerbach Corp.
Mazamma Timber Products
The Murphy Co.
Southside Loggers
Stimson Lumber Company
Willamina Lumber Company

Washington

Anderson and Middleton
Boyd Lumber Corporation
Cascade West Forest Products
Dahlstrom Lumber Company
Don Bell Logging Company
Glenn T. Anderson Lumber Company
H.O. Lumber Products, Inc.
ITT Rayonier
Mayr Bros. Logging Co.
Merrill & Ring, Inc.
Mitsui & Company
Pacific Lumber & Shipping Co.
Puget Sound Plywood, Inc.
West Coast Orient Co.
Weyerhaeuser Company

Idaho

Boise Cascade Corp.
Guy Bennett Lumber Company
Potlatch Corporation
Willow Creek Timber Company

ASSOCIATIONS

Inland Forest Resource Council, Missoula, Montana
Northwest Independent Forest Manufacturers, Tacoma, Washington
Northwest Timber Association, Eugene, Oregon
Pacific Rim Trade Association, Portland, Oregon
Washington Citizens for World Trade, Seattle, Washington
Western Forest Industries Association, Portland, Oregon

1984

HISTORIC LEVELS OF COMPANIESPURCHASING NATIONAL FOREST TIMBER

Company	National forest tributary area	Historic quota ^a		Substitution limit ^b
		Purchases	Exports	
—————(thousand board feet)—————				
Anderson & Middleton	Olympic	17,200	8,400	8,400
Arcata Lumber Co.	Six Rivers, Klamath	12,534	5,086	5,086
Bald Knob Land & Timber Co.	Siskiyou	11,657	3,586	3,586
Battles Logging Co.	Mt. Hood	596	23	23
Bohemia, Inc.	Plumas, Tahoe, El Dorado, Stanislaus Mendocino	42,040	28,775	28,775
Boise Cascade Corp.	Siuslaw	13,796	3,901	3,901
	Willamette	5,676	14	14
	Gifford Pinchot	21,797	3,857	3,857
	Mt. Baker-Snoqualmie, Wenatchee	76,992	1,350	1,350
Brazier Forest Products	Mt. Hood, Gifford Pinchot	31,695	293	293
Broughton Lumber Co.	Gifford Pinchot	6,224	1,991	1,991
Buse Timber Co.	Mt. Baker-Snoqualmie	11,401	7,442	7,442
Caffall Brothers Forest Products, Inc. ^c	Mt. Hood, Gifford Pinchot	63,719	43,200	43,200
Champion International	Willamette	24,420	340	340
	Gifford Pinchot	9,926	3,227	3,227
Coos Head Timber Co. ^c	Siskiyou	3,632	54	54
Crown Zellerbach Corp.	Gifford Pinchot, Mt. Hood	40,568	150,443	40,568
	Olympic, Mt. Baker-Snoqualmie	8,690	65,600	8,690
Frank Lumber Co.	Mt. Hood, Willamette	13,493	602	602
Freres Lumber Co.	Mt. Hood, Willamette	27,647	736	736
Georgia-Pacific Corp.	Siuslaw	8,950	2,051	2,051

^aRepresents 110 percent of historic level.^bMaximum amount of Forest Service timber that could be substituted for private timber exported.^cNo Forest Service timber under contract.

Company	National Forest tributary area	Historic quota ^a		Substitution limit ^b
		Purchases	Exports	
————(thousand board feet)————				
Hemphill-O'Neill Lumber Co., Inc. ^c	Gifford Pinchot	623	2,800	623
International Paper Co.	Gifford Pinchot	29,902	4,925	4,925
ITT Rayonier ^c	Olympic	14,946	53,350	14,946
Louisiana-Pacific Corp.	Gifford Pinchot, Mt. Baker-Snoqualmie	40,694	7,338	7,338
	Six Rivers, Lassen, Mendocino, Shasta-Trinity	92,095	14,167	14,167
Lyle Wood Products ^c	Gifford Pinchot	6,210	3,652	3,652
Manke Lumber Co.	Olympic, Mt. Baker-Snoqualmie	7,600	12,600	7,600
Mayr Bros. Logging Co.	Olympic	13,400	20,300	13,400
Merrill & Ring, Inc.	Olympic	29,037	11,350	11,350
Michigan-California Lumber Co. ^c	El Dorado	40,025	9,693	9,693
Mt. Adams Veneer Co.	Gifford Pinchot	24,468	944	944
Mountain Fir Lumber Co., Inc.	Mt. Hood, Siuslaw	24,200	5,868	5,868
Multnomah Plywood Corp.	Gifford Pinchot, Mt. Hood	13,475	894	894
The Murphy Co.	Siskiyou, Siuslaw, Willamette	66,789	3,059	3,059
Ocean Terminals ^c	Siskiyou	3,852	8,942	3,852
Pacific Lumber & Shipping Co.	Gifford Pinchot	48,752	19,580	19,580
Pine Mountain Lumber Co.	Klamath, Shasta-Trinity	29,392	13	13
Pope & Talbot, Inc. ^c	Olympic, Mt. Baker-Snoqualmie	1,306	5,068	1,306
Publishers Paper Co.	Mt. Hood, Siuslaw, Gifford Pinchot	120,052	5,158	5,158
	Mt. Baker-Snoqualmie, Olympic	28,215	9,552	9,552

^aRepresents 110 percent of historic levels.

^bMaximum amount of Forest Service timber that could be substituted for private timber exported.

^cNo Forest Service timber under contract.

Company	National Forest tributary area	Historic quota ^a		Substitution limit ^b
		Purchases	Exports	
————(thousand board feet)————				
Puget Sound Plywood, Inc.	Mt. Baker-Snoqualmie, Gifford Pinchot	12,313	3,639	3,639
Reservation Ranch	Siskiyou, Umpqua, Klamath, Six Rivers, Modoc, Shasta-Trinity	56,893	20,571	20,571
Ken Rogge Lumber Co.	Siskiyou	1,441	10,332	1,441
Rosboro Lumber Co.	Willamette, Siuslaw	39,429	543	543
St. Regis Paper Co. ^c	Gifford Pinchot, Mt. Baker-Snoqualmie	8,356	61,903	8,356
SDS Lumber Co.	Gifford Pinchot	23,067	9,001	9,001
Seaboard Lumber Co.	Mt. Baker-Snoqualmie, Olympic	21,417	7,616	7,616
Seattle-Snohomish Mill Co.	Mt. Baker-Snoqualmie	3,335	2,098	2,098
Sierra-Pacific Industries	Shasta-Trinity, Six Rivers	28,527	9,470	9,470
Simpson Timber Co.	Olympic	120,200	8,500	8,500
	Mt. Hood, Willamette	17,785	1,943	1,943
Summit Timber Co.	Mt. Baker-Snoqualmie	52,283	70,471	52,283
Vanport Manufacturing Co., Inc.	Mt. Hood, Gifford Pinchot	37,500	1,848	1,848
Washington Loggers, Inc.	Mt. Baker-Snoqualmie	12,441	999	999
Wasser & Winters Logging	Mt. Baker-Snoqualmie, Gifford Pinchot	35,122	78,290	35,122
West Coast Orient Co.	Mt. Baker-Snoqualmie, Gifford Pinchot, Mt. Hood	25,360	32,039	25,360
Wetsel-Oviatt Lumber Co.	El Dorado	23,063	1,027	1,027
Wilkens, Kaiser & Olsen	Gifford Pinchot	3,839	73	73
Total		<u>1,610,057</u>	<u>850,587</u>	<u>491,996</u>

^aRepresents 110 percent of historic level.

^bMaximum amount of Forest Service timber that could be substituted for private timber exported.

^cNo Forest Service timber under contract.

FOREST SERVICE MANUAL PROVISIONS

REGARDING HISTORIC LEVELS AND TRIBUTARY AREAS

TITLE 2400 - TIMBER MANAGEMENT

2430.92 - Export and Purchase Quotas

2430.92a - Historic Levels. Historic levels are always associated with the tributary area to a processing facility. The historic level is increased by 10 percent to determine the historic quota. The historic quota is the maximum allowable purchase of Forest Service timber or export of unprocessed timber from private land allowed in the administration of the export restrictions. The procedure is the same regardless of the volume purchased or exported in any 1 year. The historic level is based upon the 3-year base, regardless of whether or not the purchaser was in existence. For example, the historic levels and quotas for a purchaser who did not buy any National Forest sales in 1971 and who did not export any private timber in 1973 would be calculated as shown in exhibit 1.

The historic level of purchase and export may be zero for new firms or firms that did not buy any National Forest timber or export any private timber during the base period. Firms with a historic purchase and export level of zero are prevented from buying any National Forest timber in any year in which they export private timber.

The volume of surplus species is not included in determining the historic level. However, the volume of minor species such as alder is included as long as it meets the minimum quality standards.

Exhibit 1

Calendar Year	Purchases ^a	Private Timber Exported
1971	0	400 MBF
1972	3,500 MBF	500 MBF
1973	4,000 MBF	0
Total	7,500 MBF	900 MBF
Historic Level (Total ÷ 3)	2,500	300
Historic Quota (Historic Level x 1.10)	2,750	330

^aSale date is the award date as it appears on the front page of the timber sale contract.

TITLE 2400 - TIMBER MANAGEMENT

2430.92b - Tributary Areas. Initially, the tributary area for a given facility is determined from the historic source of logs for that facility in the 1971-1973 base period. However, the tributary area should be reanalyzed as purchasing patterns change. The tributary area shall be expanded if the log supply area expands. Reductions in the tributary area shall be made only after a definite change in purchasing is clearly established.

A purchaser who hauls long distances will have a large tributary area, whereas a purchaser who has purchased logs within a minimum haul distance of a mill will have a relatively small tributary area.

The tributary areas for two mills shall be combined in the administration of the export restrictions if the timber from a sale is hauled to both mills for processing.

2430.92c - Transfers of Historic Levels and Quotas. The historic levels of purchases and exports are not assets owned by a purchaser and hence are not available for sale. However, there are circumstances under which the historic levels may logically be transferred from one entity to another.

The general rule on such transfers is that a historic level goes along with the business entity that established the level. In cases where there is a successor in interest (such as a merger or complete purchase of one firm by another), the historic level automatically transfers. In all other cases, the matter shall be referred to the Regional Forester who shall consult with the Regional attorney and make a ruling. These other cases shall be decided on the nature of the transaction within the tributary area of the selling firm. If the selling firm disposes of all its assets within a tributary area, the historic levels may follow the rest of the transfer. Assets unrelated to the forest products business may be excluded from the sale without affecting the historic level transfer.

If the transfer of historic quotas is not allowed, the third party agreement shall not be approved if it would result in an export violation.



United States
Department of
Agriculture

Forest
Service

Washington
Office

12th & Independence, SW.
P.O. Box 2417
Washington, DC 20013

1420

JUL 1984

Mr. J. Dexter Peach
Director, Resources, Community and
Economic Development Division
General Accounting Office
Washington, DC 20548

Dear Mr. Peach:

We have reviewed the GAO draft report entitled "Potential Impacts of Tighter Forest Service Log Export Restrictions." The report is well done and we concur with the findings.

The Senate Committee on Appropriations' request for your investigation included four topics. Our comments are listed below in conjunction with those topics.

Topic (1).

The accurate Forest Service definition of "third-party substitution" or of "indirect substitution" applied pursuant to current Forest Service regulations.

Comment (1).

Chapter 2 of the draft report correctly states the Forest Service definition.

Topic (2).

The Federal timber volumes affected by this substitution, and the current magnitude of the export program and the indirect substitution problems.

Comment (2).

Chapter 3 provides an objective discussion of the situation and probable magnitude of third-party substitution. It was pointed out on page 11 of the report that the calendar year 1983 export data had not been completed and reported as of April, 1984. We have compiled the 1983 data since your work on this issue, and a copy of our calendar year 1983 report to Chairman Whitten of the House of Representatives Committee of Appropriations is enclosed.

You may note that we report that 72 million board feet of western National Forest logs were acquired by firms that, because of export restrictions, were



FS-6200-117-R-B

Mr. J. Dexter Peach

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not eligible to buy the timber directly. We believe that the difference in 1983 volume reported in this category from the volume reported in past years is primarily due to the improved reporting, rather than an increase in third-party substitution. We believe that possibly more than 72 MMBF was involved in third-party substitution because our reporting system does not account for older sales nor have we been able to include the types of sales cited on page 12 of the draft report. If our new reporting requirements were fully implemented, we believe they would show a level of third-party substitution of approximately 100 million board feet.

Topic (3).

The potential impact that expanding the current prohibition to include second and third-party purchasers would have on the industry and the public and the feasibility of the Forest Service to administer such a prohibition.

Comment (3).

We agree with your Chapter 4 discussion of this topic. The impacts would be costly and complex.

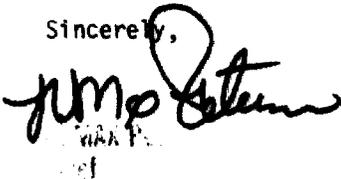
Topic (4).

Other regulatory mechanisms that would be used in administering such a prohibition.

Comment (4).

As stated on page 23 of your report, we believe that additional authority would be necessary to administer an effective ban on the third-party substitution.

Sincerely,



J. Dexter Peach

Enclosure

Disposition of National Forest Timber Harvested and Private Timber Exported
During CY 1983 by Purchasers of National Forest Timber 1/

APPENDIX IV

Region	I National Forest Timber Processed Domestically <u>2/</u>		II National Forest Timber Sold Domestically <u>3/</u>		III Sold Domestically To Processors Who Could Not Have Purchased Directly <u>4/</u> (Included in II)		IV National Forest Surplus Timber Exported or Sold for Export <u>5/</u>		V Total National Forest Timber in Sample <u>6/</u>	VI Private Timber Exported or Sold for Export by Purchasers <u>7/</u>
	Volume (MMBF)	%	Volume (MMBF)	%	Volume (MMBF)	%	Volume (MMBF)	%	Volume (MMBF)	Volume (MMBF)
Northern	900	84	172	16	none	---	none	---	1072	none
Rocky Mountain	346	100	none	---	none	---	none	---	346	none
South Western	378	100	none	---	none	---	none	---	378	none
Intermountain	417	100	none	---	none	---	none	---	417	none
Pacific Southwest	1325	79	347	21	(38)	(2)	4	0.1	1676	6
Pacific Northwest	2039	57	1526	43	(34)	(1)	4	0.1	3569	64
Total	5405	73	2045	27	(72)	(1)	8		7458	70

- 1/ As proposed by required 36 CFR 223.10. The data was reported by purchasers of National Forest timber sales.
- 2/ National Forest timber processed domestically by purchasers of National Forest timber.
- 3/ National Forest timber sold by purchasers of National Forest timber to a domestic buyer.
- 4/ National Forest timber sold by purchasers of National Forest timber to a domestic buyer who, because of export restrictions, could not have purchased National Forest timber directly.
- 5/ National Forest surplus timber sold by purchasers of National Forest timber to be exported, or exported.
- 6/ Total National Forest timber included in the sample (Sum of Columns I, II, and IV).
- 7/ Private timber exported or sold for export by purchasers of National Forest timber sales.

APPENDIX IV

MARK O. MATFIELD, OREG., CHAIRMAN

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United States Senate

COMMITTEE ON APPROPRIATIONS
 WASHINGTON, D.C. 20510

July 25, 1983

Honorable Charles A. Bowsher
 Comptroller General
 United States General Accounting Office
 441 G Street, N.W.
 Washington, D.C. 20548

Dear Mr. Bowsher:

During the consideration of the FY 1984 appropriations bill for the Department of the Interior and Related Agencies, the issue of exporting Federal timber was discussed in substantial detail. For a number of years, the Interior and Related Agencies appropriations bill has carried the following general provision:

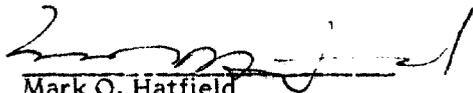
"No part of any appropriation under this Act shall be available to the Secretaries of the Interior and Agriculture for use for any sale hereafter made of unprocessed timber from Federal lands west of the 100th meridian in the contiguous 48 States which will be exported from the United States, or which will be used as a substitute for timber from private lands which is exported by the purchaser: Provided, That this limitation shall not apply to specific quantities of grades and species of timber which said Secretaries determine are surplus to domestic lumber and plywood manufacturing needs."

The current restriction prevents the export of Federal unprocessed timber, except for grades and species determined to be excess to domestic needs, and it also prevents the use of Federal timber as a substitute for private timber that is exported. At issue is the amount and impact of substitution of Federal timber for private exported timber and the resale of Federal timber to firms that export logs from non-Federal sources.

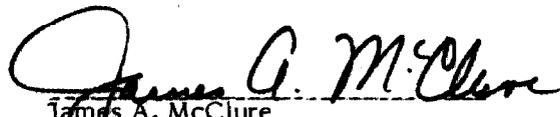
Accordingly, we would request the General Accounting Office to investigate the issue of "indirect" or "third-party" substitution of Federal logs for private, exported logs and to report back by March 1, 1984 on the following:

- (1) The accurate Forest Service definition of "third party substitution" applied pursuant to current Forest Service regulations.
- (2) The Federal timber volumes affected by this substitution, and the current magnitude of the export program and the indirect substitution problems.
- (3) The potential impact that expanding the current prohibition to include second and third party purchasers would have on the industry and the public and the feasibility of the Forest Service to administer such a prohibition.
- (4) Other regulatory mechanisms that would be used in administering such a prohibition.

Sincerely,



Mark O. Hatfield
Chairman
Committee on Appropriations



James A. McClure
Chairman, Subcommittee on
Interior and Related Agencies

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10/10/10

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