Hearing commenced at 4.30 pm

Mr STUART WEST
General Manager, examined:

Mr GAVIN BUTCHER
Director, Policy and Strategy, examined:

Mr RON LUCAS
Director, Finance and ICT, examined:

The CHAIR: On behalf of the Legislative Council Standing Committee on Estimates and Financial Operations, I welcome you to today’s hearing. Can the witnesses confirm that they have read, understood and signed a document headed “Information for Witnesses”?

The Witnesses: Yes.

The CHAIR: It is essential that all your testimony before the committee is complete and truthful to the best of your knowledge. This hearing is being recorded by Hansard and the transcript of your evidence will be provided to you. It is also being broadcast live on the Parliament’s website. The hearing is being held in public, although there is discretion available to the committee to hear evidence in private. If, for some reason, you wish to make a confidential statement during today’s proceedings, you should request that the evidence be taken in closed session before answering the question. Agencies and departments have an important role and duty in assisting the Parliament to review agency outcomes. The committee values your assistance with this. We might start with Hon Sally Talbot.

Hon SALLY TALBOT: Can we start with page 51 and just a couple of questions about significant issues? I note that this reporting period—I do not think it includes two major fire incidents, but you certainly have been dealing with the fallout from the Northcliffe fire and, of course, we had the Waroona–Yarloop fire. I notice that the second dot point on page 51 refers to increasing fire risk. Could I divide this question into two? One is: How are you mitigating the effects of those two major bushfires? What was the extent of the loss from your perspective, and what are you doing in the way of salvage and regeneration? The second part of the question will be: how are you looking forward to being able to manage the more manageable parts of increased fire risk, recognising that a lot of it is outside the management capacity of any of us?

Mr West: Thank you, chair. Just by way of background, which will explain why I pass to my colleagues for some information, I joined the Forest Products Commission in the last week of June this year —

Hon SALLY TALBOT: So you are an old hand now!

Mr West: Thank you, I appreciate the recognition!

Whilst I am getting up to speed and understanding the issues of the past year, my colleagues certainly were here for that period of time and, in fact, Mr Butcher was acting general manager for a good part of that period, so if I look to defer for details in the past, that is some explanation.

It is probably appropriate to say that we have undertaken an awful lot of salvage activities in response to the beyond 3 000 hectares of pine plantation damaged in last year’s fires, and we have salvaged and are still salvaging as best we can the softwood products that come out of those burnt areas. Fortunately, we have been able to find markets and switch product so that we can get those
products into market. We have not completed the resolution of clearing and replanting; that is expected to take another year or two from the next planting season. It is probably appropriate —

Hon SALLY TALBOT: That is in relation to Northcliffe, presumably, is it?

Mr West: In fact, how we go specifically for Northcliffe, I am not too sure whether Mr Butcher might be in the best position to start that detail.

Mr Butcher: The Northcliffe fire was not last year, that was the previous summer. The Waroona fire was last summer.

Hon SALLY TALBOT: Yes, that is why I prefaced my comments by saying “dealing with the fallout of Northcliffe”.

The CHAIR: Can I just ask a question, Hon Sally Talbot?

When you have a fire go through like that, particularly ones around Waroona, obviously all those pine trees are now dead. Is there a limited time you have to actually harvest them before they start to deteriorate?

Mr West: Yes there is, chair, but it depends, of course, on the size and the market. Very large trees seem to hold their potential for recovering a whole range of products. The sooner you salvage them, the better you can get them into an almost green market, remembering that sawmills, predominantly, when they square up a log, they convert the outside into chips, and they can access a number of markets. Some markets do allow contamination of fire char; many do not, so one of the constraints is how productive you can salvage. You might be able to salvage the centre part—the square part of the log—but the economies, if you cannot sell the outside, change. Very small trees, depending on the extent of the fire, can very quickly have no value over time.

The CHAIR: Part of my question was: What is the time frame you usually have to actually harvest them? Do they deteriorate, or can you leave them there for a couple of years before you cut them down?

Mr West: More than 12 months for large trees and if they are not terribly badly burnt, beyond 12 months, so —

The CHAIR: You lose that growth, I suppose, of the tree during that time.

Mr West: That is right, yes.

Mr Butcher: Certainly the tree is dead; it is not growing. It is basically slowly drying out. We made the mistake in the past of actually cutting the trees down and stockpiling them, and then they get stain and they deteriorate far quicker than when they are left standing, so you should only salvage them once you actually have a marketplace. In terms of the question in relation to Northcliffe, about 3 000 hectares of regrowth karri forest was very badly affected in the fire and it would be desirable to salvage, from a timber production point of view. We went to tender to try to find a marketplace for those products, but they were very limited, so we have only been able to sell 100 hectares in the trial we did last year, and we are hoping to continue the trial this year.

Hon SALLY TALBOT: One hundred hectares out of 3 000?

Mr Butcher: Out of 3 000, yes. We are hoping to go to further trials in the coming year. In the case of the Waroona fire, we have markets for most of it, but more than half the wood was under 15 years of age, so it was well short of maturity. I think, as Stuart indicated, we got the best markets we could for the material that we have, and we had to find new markets for that. We did lose, effectively, future growth of about half a million cubic metres of timber out of the Waroona fire, which, in terms of losses to our part of the supply chain, was about $29 million in value, but to the whole supply chain it was about $67 million in value loss to the south west communities over the coming years, so it is very significant in terms of that impact.
Hon SALLY TALBOT: What is the value of the remaining 2 900 hectares at Northcliffe? What is the potential value of that, if you can find buyers for the salvaged timber?

Mr Butcher: I think we estimated something around $10 million for salvage; I can take that on notice, if you want an exact number for that.

Hon SALLY TALBOT: Yes, could you, please?

Mr Butcher: But we did do a calculation, which I think was about $10 million for the salvage value of the material that we got out of it.

[Supplementary Information No F1.]

Hon SALLY TALBOT: What is the challenge in finding the market?

Mr Butcher: The existing markets are in place. Our first attempt is to be able to sell timber to our customers.

Hon SALLY TALBOT: What is the problem with the 3 000 burnt out hectares of karri? You are indicating that you tried to sell it but you had not been able to.

[4.40 pm]

Mr Butcher: The traditional market for regrowth karri—for young or relatively young regrowth karri—is being sold into the paper market. As Stuart indicated, some markets do not like charcoal.

Hon SALLY TALBOT: I see.

Mr Butcher: That is the primary problem.

Hon SALLY TALBOT: So you are looking for a narrower market because it is charred.

Mr Butcher: It has charcoal in it, and they do not accept that. There were a number of sawlogs. We have salvaged the better material for sawlog material. I think there was a question; that lasted more than 12 months since the fire, so it did actually hold up surprisingly well when we did not fell it, so we did manage to salvage some of that higher value product.

Mr West: Sorry, chair, could I just add to that? Of course, the interruption to the business activities are that the size of the trees does not necessarily match the size of the trees or the product mix that we are selling so we need to negotiate with our manufacturers to defer their existing diet of their preferred contracted volumes to actually get them to take the things that we need to sell in a hurry. It is additional; of course, there is no new manufacturing capacity so we have to actually try to negotiate for people not to take the wood that they would prefer, but the industry is such that it understands around fire, it needs to have a bit of give-and-take because, at some point, at least the trees it will not take that it would prefer will still be available in the future. That is part of the negotiation and the delay.

Hon SALLY TALBOT: Is there any mitigation you can do? Can you put in place any preventive measures? What have you learned from looking at Northcliffe, Waroona and Yarloop?

Mr West: Perhaps, if I start, chair, but I am sure my colleagues who have been here for the period will be more specific. We understand the benefits of fuel reduction and general fire protection. Some of that is in our control. Some of it is well beyond the Forest Products Commission’s responsibility. There is importance of having coordinated responses and things that are in our control, such as good planning and prevention, as I have just said, but certainly, in this country, in the experience of forestry and wildfire, there certainly have been circumstances where you would potentially suggest that some things are unavoidable—the nature of some things. That is particularly fires that get to a large scale before they get to our assets. It is very different fires commencing in our assets versus our assets being in the path of a large fire; you could almost argue that the prevention activity is well gone before we have any control. In terms of specific responses, maybe Mr Butcher can add.
Mr Butcher: There have been a couple of well-publicised inquiries into this matter and we have contributed to those inquiries. I think the lessons that have come through those processes we would strongly support. I suppose in terms of our lessons, in some cases people do not understand the value of the assets that are being lost. Potentially for us, there is a lesson that while we are not the frontline firefighters, we have an interest in letting the community know about the value of the assets and the risk to those assets. Often people perceive that plantations might be a fire risk, but the fire in Waroona ran for 50 kilometres before it got to it; it actually stopped in the plantation. So there are important lessons that we can make a contribution to fire management in the south west and there are assets that do need to be protected as well as, of course, the importance of all other community assets.

Hon SALLY TALBOT: Okay, thank you. I have a couple of other things in “Significant Issues” but I will move on and come back later if we have time. Can I take you to page 31 of the annual report where you talk about the reopening of the Greenbushes sawmill. Of course, it brings a little bit of joy to my heart to see that you are talking about creating local jobs. However, you will be aware, if only because of the questions I have asked in the Parliament, that there is a sign outside the Greenbushes plant asking for backpackers. What is going on there? What can you do with an enterprise like this? You have facilitated the rebirth of that aspect of the industry. Why are we now losing those local jobs?

Mr West: Chair, can I start? I have visited the Greenbushes site; in fact, I have visited almost all, if not all, of our manufacturing sites. I spoke to them particularly in response to the issues raised when the questions were asked about backpackers. My clear understanding from the response from the organisation at the sawmill is that they are looking for workers. They struggle to get local workers so regional workforces and getting people willing to come and do low-skilled jobs is a challenge. I interpret the sign as reminding backpackers that they can get work there and not to walk past and think, “This is a business that doesn’t have a temporary workforce” or that there are no opportunities. I think it is encouraging. Mr Butcher might have more experience with the site but I see it as complementary to getting workers. We want them to maintain a workforce to be productive. I am not aware that they have a particular agenda not to employ local people. In fact, I know they are just challenged to get a workforce. Maybe Mr Butcher has further information.

Mr Butcher: Look, that site has obviously been reopened, which is very good news for the industry in the locality. The company, Auswest, which has purchased it and now, since that time, announced its consolidation of all its activities in the south west will eventually be moving to that site. It will be looking to build up a permanent workforce, by and large, from a transfer of the workforce in Manjimup et cetera. However, any one of these sites always has short-term jobs that, as Stuart has said, may well encourage short-term employees such as backpackers to do it. The industry itself is looking for permanent, skilled and long-term employment.

Hon SALLY TALBOT: Okay, so your hope would be that that invitation to backpackers would be basically confined to the seasonal work?

Mr Butcher: Yes.

Hon SALLY TALBOT: That segues me quite nicely on to your section on the workforce on pages 44 to 45. Mr Butcher, you referred specifically to the fact that the industry is actually looking for full-time employees. I wondered if you could talk us through this couple of pages. The first paragraph refers to the FPC employing casual workers. Am I reading the little chart right on page 44 about 11 full-time/part-time contractors? There is a reference to casual workers in the first paragraph there. How many casual workers do you employ? Is it the number on that chart?

Mr West: Can I clarify that, no, the number on the chart actually refers to full-time or part-time contract employees unrelated to casuals. Casuals primarily relate to our nursery operations. That full-time and part-time contract work, we might have a three-month contract for somebody to come and do something IT-related.
Hon SALLY TALBOT: Yes. Those are not the casual workers.

Mr West: No, they are not.

Hon SALLY TALBOT: So how many casual workers would you have?

Mr West: Again, we might have the data—it looks like Mr Butcher does—but they relate to seasonal work so at the nursery, depending on how many seedlings we are planting and depending on how hot it is and whether we need to shift seedlings around, given that there are millions of individual plants, we might, at very short notice, as in a week’s notice, need three people to come and help do some activities at the nursery. Depending on the re-establishment, the speed of contractors and what have you, we might have a steady stream of plants going out to the field to be planted. Then, if a contractor is working faster than we can accommodate, we might just need one or two or three people, but it looks like Mr Butcher might have the exact numbers.

Mr Butcher: I only have the numbers for the nursery —

Mr West: Yes.

Mr Butcher: — which is where most of the casual workers are employed. At this time of year when we are sowing the seeds, there is a peak in employment and I think about 20 casuals are working at the nursery. At the time of lifting or dispatch when the seedlings are sent out, about 40 casual workers are employed. That has increased this year because of the expansion of the softwood strategy program. In past years, it has probably been about half that.

Hon SALLY TALBOT: Your Aboriginal traineeships, can you tell us about where they are operating? I see that there is reference to the working relationship with the Clontarf Foundation. Have you got Aboriginal traineeships in the Kimberley in relation to sandalwood, or not?

Mr Butcher: No, we do not have any activity in the Kimberley area, but in the goldfields we have been seeking to get a trainee engaged as part of our industry. We started this program towards the end of last year, but, unfortunately, we were not able to get suitable trainees in that time frame. So we are just about to advertise again to go and secure further trainees.

Hon SALLY TALBOT: So this is a new development, is it?

Mr Butcher: Yes, a very new initiative. Certainly, they are regionally based positions, and we hope to engage people with a potential to work on into the industry.

Hon SALLY TALBOT: Perhaps you would like to take on notice a question about what your expectations are for this program. It just seems to me that you are a small agency, but the opportunity to provide this kind of training and apprenticeships to young people outside the metropolitan area is quite significant.

Mr West: Chair, it might be just worth it if I prompt Mr Butcher. Of course, we are a small agency with quite a stable workforce, so our capacity to influence Indigenous recruitment, similar to my experience around the whole country, is challenging. But we employ quite a large contractor base who are regionally based who have opportunity. It might be worth Mr Butcher just bringing to the committee’s awareness the activities we have done with our contractors, because we see that as having the potentially greater impact on employment, potentially in regional areas.

Mr Butcher: Exactly. We probably employ more people through our contracts than we actually have in our own workforce—pretty definitely actually. In our recent tendering process in terms of re-establishing the sandalwood industry for the next 10 years, we tendered for the harvesting, the processing, the sales of oil for local manufacture and a marketing agent. For each of those positions, we required that the tenderers address criteria which included regional investment and Aboriginal engagement, so they had to prepare an Aboriginal engagement plan as part of their process, which looks at how well the contractor will contribute to the broader Aboriginal community, including
potentially employment benefits. Out of that process, we were able to offer a preferred tenderer basis to a new contract engaging an Aboriginal business as a part owner of a new enterprise in the goldfields, as well as re-engaging businesses with strong Aboriginal engagement in the harvesting process. We certainly do not see it just as an employment issue; it is about building the strength in business as well.

The CHAIR: Does that satisfy your question, member, or do you want something on notice?

Hon SALLY TALBOT: I would like something on notice. Given that it is a new program, what are your projections for the next 12 months or the next five years? How would you like to see a program like this operating?

[Supplementary Information No F2.]

Hon SALLY TALBOT: What sort of practical outcomes will you be looking for? As you know, there is a good model, the Priority Start program, which makes all government contracts subject to commitments on traineeships and apprenticeships. Is it something like that we are looking at or is it a less formal arrangement?

The CHAIR: Can I just move to another member for a moment? We can come back to you.

Hon SALLY TALBOT: Yes.

The CHAIR: Hon Alanna Clohesy has a couple of questions.

Hon ALANNA CLOHESY: I have just a couple of quick questions. When did the Treasurer provide the commission with an indication that Treasury was no longer considering selling a component of the Forest Products Commission?

Mr West: Chair, I am not too sure if my colleagues will have the exact date. We have got a dated letter. We can take that on notice.

[Supplementary Information No F3.]

Mr West: That might be the most accurate. I cannot remember the date; I am sorry.

Hon ALANNA CLOHESY: When did the Treasurer provide the commission with formal advice? Similarly, when did the Treasurer provide the commission with advice initially to ready itself for divestment? When did that occur?

Mr West: Certainly, chair, if you are okay, we will take that on notice as well.

[Supplementary Information No F4.]

Hon ALANNA CLOHESY: Originally, I understood that the whole of the Forest Products Commission was going to be up for sale and then it was a component of the softwood.

Mr Lucas: My understanding is it was only the plantation estate.

Hon ALANNA CLOHESY: The softwood plantation assets?

Mr Lucas: That is my understanding. That might have been a year before the Treasurer said no.

Hon ALANNA CLOHESY: Maybe we can get some clarification on that. This part relates to the annual report. Where in the annual report is the advice from the Treasurer or the minister to the commission to prepare the commission for sale or that component of the commission for sale?

Mr Lucas: From memory, last year’s annual report mentioned it was potentially up for sale and because that was withdrawn, there was no need to mention anything in subsequent events in this report.

Hon ALANNA CLOHESY: As far as I am aware, the Treasurer did not withdraw the potential for the sale until May 2016, which is why I asked the question when did the Treasurer instruct the commission to prepare for sale or prepare components for divestment, because that should be reported in the annual report. It happened over two budgets. The first one was 2014–15 and the
The second one was 2015–16. The second lot of instruction in the 2015–16 budget, depending on when the Treasurer provided that advice, should be included in this annual report.

Mr West: I might seek some clarification, but my understanding was this was a central government—a Department of Treasury—initiative where they were looking at divesting one of their assets which we manage. I do not believe the FPC was given the responsibility to manage or to prepare itself. It was requested to provide information to central government on certain elements.

Hon ALANNA CLOHESY: So a task force—a project team—that was set up in Treasury?

Mr West: That is right, and I am pretty confident that we were not a formal member of that task force. We were just, for example, asked what areas of plantation do we have, what is their age class—information like that. We were providing supportive information to a government process. It certainly was not the commission’s role; it was not determining what it was or was not doing in terms of a sale. That was not the domain of the commission. Therefore, prior to this annual report, those discussions were occurring in government, so it was not something the commission put in this report. Before the conclusion of this financial year, the government had announced it was not doing it, so in actual fact, any relevant reference in here would only likely have said that the government talked about doing something which it is not doing. We are just carrying on business as usual. There was no initiative—nothing that the commission was doing. This is a summary of the year, so there was nothing that changed. The commission went about its business as usual.

Hon ALANNA CLOHESY: If I could get answers to those questions about the timing of that, that would be appreciated.

The CHAIR: I think last year when we met, the commission was saying that with the drying climate, areas where you used to have softwood plantations now are not becoming viable, so you are moving into the wetter areas in the south west where the economic haulage distance allows for that. What is the economic haulage distance for softwood plantations?

Mr West: Again, Mr Butcher might be able to add to this, but in general—I am trying to be cooperative, so, please, do not misinterpret this—it often depends on the value of the product. If you are transporting very large, very valuable products, haulage will be a minor component; if you are transporting very small, low-value products, haulage can exceed the overall value of the contents of the load. The industry generally talks about 100-kilometre haulage distances in general.

The CHAIR: To a mill?

Mr West: Yes, that is right—to a manufacturing destination. From the sources, from the stumps where you cut them down, to their point of next value-adding or processing, we talk generally about 100 kilometres. There will be certain products that it would certainly be less than that for, but 100 kilometres based on $1.50 a litre for diesel and efficiency of trucks is about normal. There are some high-value products that could certainly well exceed that, and in the country there are certainly haulage distances of 150 kilometres or even more. Again, for things like fire salvage, quite often there is also an additional compensation. For example, if you have got burnt logs that you cannot do anything else with and you have to pay a lot of management overhead to mulch or burn or do something else, maybe you can save yourself $50 a tonne in dealing with it by paying $30 a tonne more in freight, and the net benefit is actually a $20 per tonne saving. So there are other reasons why you might subsidise your costs in haulage to make it a longer, viable distance to make savings with the opportunity cost. If you do not do that, you will have increased costs imposed on yourself.

[5.00 pm]

The CHAIR: I have got a couple of questions. With some of the fires that we have had where young plantations have been burnt, how many hectares have we had where they are just not economically viable and you have had to just mulch and burn?
Mr Butcher: For example, in the fires we had last year in Esperance—you will recall there was a large fire—there was about a couple of hundred hectares of our plantations burnt in that fire. We could not haul them to our market in Bunbury; it is far too far to haul. Effectively, that just becomes, as you say, a mulch-and-burn operation. Equally, for anything that is perhaps below about six years of age, there is really no viable method of picking up those logs and actually converting them into even a low-grade product. The costs are far too great.

The CHAIR: Would you consider power poles to be a big product that you would haul from a longer distance than 100 kilometres?

Mr West: Potentially, yes. They are a high-value product. Yes, that is right, so maybe Mr Butcher will have experience. The market flows fluctuate.

Mr Butcher: They certainly are a premium product and we cannot actually produce enough power poles within the state. We import them.

The CHAIR: That was going to be my next question.

Mr Butcher: Sorry about that.

The CHAIR: I was going to ask: how many poles short are we in this state for what we produce and how many do we actually have to import?

Mr Butcher: We are certainly well short of the number. I do not know the exact number. It depends on the demand for Western Power at the time, but certainly we are well short of the number. We used to produce jarrah poles, probably until the 1990s, but the industry has moved on to plantation poles. Softwood poles, which are now treated, routinely become the product and they are imported from South Australia. I would be guessing a proportion, but it would certainly be less than half the demand that we can supply locally.

Hon SALLY TALBOT: Western Power is one of your contractors?

Mr Butcher: It is a customer of our customer, I think.

The CHAIR: Okay; a customer of your customer, and we are supplying less than half. What is the value of a power pole?

Mr West: To FPC, the value is about $120 a cubic metre, I think, but I can take that on notice.

The CHAIR: What is the average cubic metre for a power pole? When you are talking about an amount per cubic metre, you have got me lost a little bit there. Is the average power pole one cubic metre, two cubic metres?

Hon SALLY TALBOT: It sounds like one of the NAPLAN tests!

The CHAIR: You cannot answer and I cannot understand it.

Mr West: We can take that on notice.

The CHAIR: At F5, if you can provide for us the actual shortfall in the number of power poles, the percentage of the total power poles that Western Power uses and how many cubic metres or the actual value of a power pole?

[Supplementary Information No F5.]

Mr West: We will do our best to endeavour from Western Power to see their demand but, of course, we only know what they have asked us to supply. Once we supply, whether they have got broader demand and they are prepared to share that or not —

Hon SALLY TALBOT: It is really just how many you supply.

Mr West: Yes. I am not sure. The ambiguity around the response of course—we sell logs to a processor and we sell by the cubic metre and the processor converts it into a pole. He cuts
whatever length Western Power wants, rounds it off and makes it smooth and what have you and he would sell, I suspect, by the cubic metre because of their weight, so that is why we —

The CHAIR: There must be an average size pole.

Mr West: Yes; we will endeavour —

Hon ALANNA CLOHESY: I will not be able to sleep tonight without knowing that!

Hon PETER KATSAMBANIS: You did answer my question as to whether you provide a pole or a log that gets to the processor. What sort of timbers are usually sought after for power poles?

Mr West: I will hand it over to Mr Butcher, but I will say that, depending on their need, they become flexible in what they will take so, historically, they were all hardwood but in the absence of hardwood poles, the industry switched to softwood poles and actually went to my past state, South Australia, to use softwood poles. But Mr Butcher will be able to tell you what they have used.

The CHAIR: South Australia used concrete and metal last time I was there.

Mr West: Yes, but we sell timber poles to Western Australia.

Mr Butcher: Certainly, softwood poles are used here for public supply, although occasionally hardwood poles are used on private properties for their own purposes. The change happened at a time when a pole in the native forest could be a sawlog so the decision was made to supply them a sawlog and value-add the sawlog and put it back where, essentially, that would keep the industry going to a greater value in terms of employment than poles, which would just be cut up and stood up.

Hon SALLY TALBOT: There is an entire report by the Standing Committee on Public Administration in the previous Parliament.

Hon PETER KATSAMBANIS: I refer to your effectiveness indicators on page 48 and the quantity of native forest hardwood logged timber. You are well behind between target and actual. What is the explanation for that?

Mr West: I will hand to Mr Butcher but, effectively, it is primarily in response to two things—market demand and our customers just not ordering what they are entitled to order but also what the forest produces. As you will be aware, the forests are very unique and whilst we anticipate providing a product range, once we start producing products, it might not actually deliver the combined length and form or straightness. So whilst we anticipate delivering something, we often cannot.

Hon PETER KATSAMBANIS: I accepted part of that but I imagine that when you are setting targets for the upcoming year—we are talking about hardwood—you would have a fair idea of what is there, where it is, how big it is, because it is hardwood; it has been around for a while. It is not like wheat that you are hoping the crop will grow. When you have a target of 292 000 jarrah logs, for instance, and you get to 147 207, that is why I start asking the question about variation. Perhaps you have some optics around that.

Mr West: One of the key things is that we had unscheduled closure for months of one of our major hardwood customers, which I am sure Mr Butcher will add to, so that was no sales.

Mr Butcher: The targets are the forest management plan targets. When the forest management plan was brought down at the end of 2013 and we were able to tender for those volumes, we were able to find effective markets for almost all the first and second-grade sawlogs. The markets for, particularly the jarrah and the marri lower grade material, the other bulk volume, was nowhere near target. It is really a challenge for us to go and find markets for that. It is not an annual target, I suppose; it is the 10-year target that comes out of the forest management plan. In the sawlogs, there is a rise and fall in demand each year, in particular this year. The closure of Deanmill and the
movement of Auswest facilities to Greenbushes has deferred some of their demand. But, essentially, it is a cyclical product, I guess, in terms of its position in the marketplace.

Hon PETER KATSAMBANIS: Is that position a factor of the fact that end-user tastes or demands have changed or is it simply a case that your production is being priced out of the market because, for instance, with jarrah, I do not notice too much of a lack of demand for jarrah? It is much sought after even in re-use, so are we talking about a situation in which your cost of production makes you uncompetitive in the market?

[5.10 pm]

Mr West: That is a pretty good understanding of the circumstance. We are not aware that demand is particularly diminishing. These products have strong market brand association and strong demand. The introduction of competition for other species internationally does add to that but everyone suffers competition. One of the challenges we have is that when we go to a parcel of forest, as Mr Butcher said—the second part of table 1 on page 48—for the first and second grade logs, the actual is far closer to the target, but in the other products it is far below. So when we go to a piece of forest, we find we can sell the good part of the products, but the market for the low parts may not be there or might not have an ability to pay, because they might be as low down as firewood, for example, and it just might not be cold weather—putting aside this current winter that we have been through! Therefore, the economics of the whole block might mean that it is not economic to harvest that block and so we go to a different block or we change our regime. That does influence the cost of harvesting, but it also influences our decision on where we harvest and how we harvest, so it is probably more likely that we go to less productive areas or areas that have a different product mix. That might add to our costs; we might have to increase our roading costs to get there or we might have to do something different, because we have got to sell most of the whole product mix just to be viable, but also for good management practices.

Hon PETER KATSAMBANIS: I understand. I will leave it at that.

Hon SALLY TALBOT: Can I take you to the whole question of onerous contracts and I will give you a question? I also indicate that I want to ask you as well about the potential shortfall of pine. If they are the same thing, you can answer them together; if they are not, you can enlighten me. We will start on page 57 where you have got the onerous contracts. I think it is about —

Mr Lucas: Note 19.

Hon SALLY TALBOT: Yes, note 19, and then note 34 is about the shortfall of pine. There is also page 71 where you have got the whole section there about what an onerous contract is. My question about the onerous contracts is: how are they accounted for in the financial statements?

Mr Lucas: For the definition of “onerous contracts”, I refer you to the second point of note (ii), “Provisions — other” on page 71. There is a definition of “onerous contracts”. What they represent is the non-core share farms that we have deemed to be uneconomic. They were written off in 2010 and this is the value movement in the onerous contract evaluation of each year.

Hon SALLY TALBOT: Just give me that reference again—page 71; what was the section number?

Mr Lucas: If you go to note (ii) on page 71, it has got the definition of “onerous contracts”.

This is a writedown in the value of the liability because the onerous contracts that were written off included plantation sandalwood in that 2010 —

Hon SALLY TALBOT: That is my second question: which contracts have you deemed as being onerous?

Mr Lucas: The eucalypt pine —

Hon SALLY TALBOT: Is there a long list? Does it makes sense to take it —
Mr Lucas: No, there are only three small areas. They were all deemed uneconomic in 2010 and written off. Each year, we look at how that value has changed and we have to move the variations through the profit and loss statement. This variation here of $2 871 000 is actually reducing the liability, because in valuing the plantation sandalwood as at 30 June 2016, it actually had a value of $3 million, and that was brought back into the books as an asset.

Hon SALLY TALBOT: So an asset can change from being onerous in, say, 2014–15 and then be an asset in 2015–16.

Mr Lucas: The onerous contracts relate to the various share farm profit-à-prendre contracts that are out there and whether they have value in net present value terms. When we value those at the end of the year, if the net present value is negative, it is not an asset. In terms of plantation sandalwood, it had a positive value and therefore it was written back onto the books as $3 009 000, which is positive.

Hon SALLY TALBOT: Yes. So this is quite different from the potential shortfall of current pine resources?

Mr Lucas: Correct; that is a contingent liability note.

Hon SALLY TALBOT: So then I am looking at page 98.

Mr Lucas: Page 98, is that just a contingent liability note?

Hon SALLY TALBOT: Yes.

Mr Lucas: That is basically the Wesbeam and Wespine contracts; under state agreements, is there enough resource to supply those contracts long term? The Auditor General looks at this each year, based on management comments in regard to how it is managing that and the resource, which is valued by Indufor Asia Pacific. It is a New Zealand company and it does an independent valuation on the resource. We look at what the wood flows are—therefore, the two major contracts—and whether there is enough wood to meet the state supply agreement. Force majeure comes into play, which means our requirement to supply against the state agreement comes down, and the review as at June 2016 said that in our view there is no need to formally recognise any of those contracts as an onerous contract at this stage.

Hon SALLY TALBOT: So they are not recognised as onerous contracts?

Mr Lucas: No, it is a note to say that there is a potential, but there are things in play —

Hon SALLY TALBOT: So it is like a red flag; it is like a warning sign?

Mr Lucas: It is a red flag, and that has been there for at least four or five years.

Hon SALLY TALBOT: Yes, I know it has appeared regularly. So that is a process you go through every year to work out —

Mr Lucas: We review it every year and the Auditor General looks at it.

Hon SALLY TALBOT: So is it currently sitting as an asset?

Mr Lucas: The pine plantations are an asset and they are valued at $177 million in the books. This note is about whether the contracts relating to the asset have an onerous nature.

Hon SALLY TALBOT: It is different to what you have just explained according to the definition of the onerous asset, because the asset would still be worth something, but your problem is that it has become a liability because you cannot fulfil the contracts. It is a bit different, is it not? Not the devaluing of the asset.

Mr Lucas: The plantation asset is the value of the standing trees at 30 June, and that is $177 million. The contracts that we have to supply out of that plantation, are they onerous or not? The answer at this stage is that there is a red flag, but they are not. If they were, we would have to introduce a liability into our books to say we are going to not get the benefit out of those contracts
that we thought and we have to work out what that liability might be and account for it through the
profit and loss statement and balance sheet.

Hon SALLY TALBOT: What will be the thing that triggers the change of status from being on
a watchlist to being an onerous asset? What will it be? You know now what the asset is and you
know what the contract is committing to, so what is the uncertainty?

Mr West: We have a number of opportunities. For example, one of our customers may choose to
reduce their demand, which might impact on our supply favourably to us.

Hon SALLY TALBOT: So it is not contracts that you have got currently in place?

Mr West: It is, but as every year goes on—next year, one of our customers may take less wood.
We have got a number of contracts so that therefore changes our ability to supply.

Hon SALLY TALBOT: If one falls over, you can supply the others.

Mr West: That is quite right, but conversely, there could be something like another dreadful fire
that impacted significantly on our plantation estate, except that Mr Lucas made reference to force
majeure, so these contracts have some capacity to recognise what is outside our control through
contractual obligations. For example, there may be another jurisdiction in Australia that says,
“We have got a major timber supply problem. We want to ship really cheap logs over to
Western Australia for your processors.” That might mean they do not need to purchase our local
logs and defer them for a while. The future is ambiguous, so we do not want to describe something
as a liability when, indeed, we do not know that for sure.

Hon SALLY TALBOT: So you cannot actually give the committee at this stage the current
potential shortfall of pine resources? Could you do it as of today by volume and value?

Mr West: I guess that would be on the assumption that deliveries or demand was the same.

Hon SALLY TALBOT: All things being equal.

Mr West: That is right. We could do a calculation based on assumptions, that is quite possible, as
at today.

Hon SALLY TALBOT: Could you take that on notice?

Mr West: Just to clarify, that is —

Hon SALLY TALBOT: As of today, what is the current potential shortfall of pine resources by
volume and value?

Mr West: To the existing customers, assuming today’s level of supply or our best estimate of levels
of supply?

Hon SALLY TALBOT: Maybe you need two columns.

Mr West: Supply is seasonal. For example, the housing market, one of our major customers
converts our wood —

Hon SALLY TALBOT: Yes, I have read that section.

Mr West: They are likely to order far less timber in the —

Hon SALLY TALBOT: But then on the other hand, you have got that mitigation of the light
timber construction for the high rise, have you not?

Mr West: The best advice we have from our customers who produce housing timber is that their
demand is likely to be very weak and they have indicated that they will be taking far less timber, so
it is unlikely to be offset by advance use of stick timber in high-rise building. So, no, we do not —

[Supplementary Information No F6.]

Mr West: If you are comfortable, chair, we will indicate what it is based on.
Hon SALLY TALBOT: Do any of the existing contracts have compensation payments or liabilities for the state that you would have to meet for the failure of the contract?

Mr Lucas: With the state agreements, my understanding is that if there is compensation payable there, it is a Department of State Development issue.

Hon SALLY TALBOT: So it becomes a DSD liability.

Mr Lucas: It becomes a DSD liability, yes. We are obligated to supply a volume of timber under the state agreement, and the contingent liability note says at this stage, at 30 June 2016, we view our ability to supply that with force majeure taken into account.

Hon SALLY TALBOT: Do you do the calculation about what the compensation would be or is that DSD?

Mr West: It is not us. The state agreements, of course, are with State Development, so that is their domain.

Hon SALLY TALBOT: But State Development does not come to you and say, “Okay; what’s the shortfall? “What’s the liability?” They do it themselves.

Mr West: That would be right, yes.

The CHAIR: On behalf of the committee, I thank you for your attendance today. The committee will forward the transcript of evidence, which highlights the questions taken on notice together with any additional questions in writing, after Monday, 31 October 2016. Responses to these questions will be requested within 10 working days of receipt of the questions. Should you be unable to meet this due date, please advise the committee in writing as soon as possible beforehand. The advice is to include specific reasons as to why the due date cannot be met. If members have any unasked questions, I ask them to submit these to the committee clerk at the close of the hearing. Once again, thank you for your attendance today.

Hearing concluded at 5.21 pm