

Environmental Law Centre

UNIVERSITY OF VICTORIA

February 8, 2008

COPY

John Doyle, Auditor General
8 Bastion Square
Victoria, BC V8V 1X4

Dear Auditor General Doyle:

Re: Auditor General's Review of TFL Private Land Deletions

We act on behalf of the Sea-to-Sea Greenbelt Society on matters related to our October 19, 2007 request for an Audit of private land deletions from Western Forest Products' Tree Farm Licences 6, 19, and 25.

We would like to call your attention to a new and potentially significant issue related to this matter.

As you recall, one of the key criticisms made of the Minister's decision was that the Minister deleted all of WFP's private lands from the TFLs – and simultaneously allowed the company to retain the vast Crown land tenures in those same TFLs. Instead of allowing the TFL agreement to expire – in which case the licensee would remove its private lands at the same time as government took back its Crown tenures – Government allowed WFP to have its cake and eat it too. WFP got its private lands out of the TFL, and yet was still allowed continued possession of all the Crown tenures in TFLs 6, 19, and 25.

New information has come to our attention, indicating that the Minister may have had a legal obligation to at least consider cancelling those WFP Crown land TFL tenures. Indeed, this information raises questions about whether, at the time of the land deletions, WFP was necessarily entitled to continue with its Crown tenures.

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In light of the information outlined below, it is important for your audit to determine whether or not the Minister deleted the private lands without fully addressing the possibility that WFP's corresponding Crown tenures could be cancelled. If Government failed to fully investigate the possibility of cancelling the Crown tenures and returning those timber rights to the Crown, new questions arise about how well the public interest was represented in the negotiations regarding the future of the TFLs. Questions arise about whether the deletion of the TFL private lands – done at the same time that the status quo was maintained on TFL Crown lands -- was good stewardship of Crown resources and assets.

Of course, those questions all relate to the issue of whether Government managed Crown resources and finances in an economic, effective and efficient manner.

First Principle – TFLs May Be Cancelled When Corporate Control Changes

Historically, Tree Farm Licences have been a cornerstone of British Columbia's most important industry. It has long been recognized that the granting of such licences is of the highest importance to the Province. Therefore successive BC governments have recognized that when control of the corporate licensee changes, Government must have the power to review the licence -- to ensure that vital provincial forestry interests are not damaged by the transfer of control of the corporation.

Therefore, the *Forest Act* has long provided that if corporate control of the licence holder changes, the Minister is empowered to cancel the licence agreement to protect provincial interests in forestry.¹

Currently, s. 54.5(1) of the *Forest Act* provides that the Minister may cancel TFL agreements if control over the corporate licence holder has changed, and if the change unduly restricts competition in standing timber, log or woodchip markets. Control is defined as the holding of sufficient shares to elect 50% or more of the directors, or to otherwise effectively control the operations and direction of the corporation.² (See appendix A for the statutory provisions.)

¹ For the 1978 version of the legislative provision, see s. 50, *Forest Act*, S.B.C. 1978.

² The definition of "control of a corporation" is found in section 53(1) of the *Forest Act*.

Change of Ownership of Western Forest Products

In 2006, Tricap Management Ltd. (a wholly owned subsidiary of Brookfield Asset Management) apparently increased its overall ownership of Western Forest Products from 20.5% to 70.1%, thereby putting Brookfield in control of the majority of the Western Forest Product's shares.³ This change of ownership raises questions about whether a change of company control has taken place that may unduly restrict competition in timber, log or woodchip markets.

Should the Minister have Considered Cancelling the TFL?

As discussed, under s. 54.5 of the *Forest Act*, the Minister is given statutory discretion to cancel a TFL if the control of the corporate licence holder has changed, and if the change unduly restricts competition in certain forestry markets.

It is clear that by early 2007 the Ministry had become aware of the 2006 transactions in which Brookfield obtained 70% of WFP ownership. This is reflected in a March 2007 Ministry of Forests' document that indicates that Brookfield owned 100% of Tricap, and Tricap owned 70% of WFP. (See Appendix D⁴.)

In light of this Ministry knowledge, the Ministry should have addressed two key questions:

- Whether the increase of Brookfield's ownership of WFP from approximately 20% to 70% constituted a change of control (direct or indirect) of the company, as per s. 54.5.
- Whether that change of control unduly restricts competition in timber, log, or woodchip markets, as per s. 54.5(1)(b)(ii).

³ See Appendix B to this submission, Item 7 (A) of *Form 20-F/A* filed by Western Forest Products on April 1st, 2006 and pp. 15 and 16 of the company's 2006 *Audited Financial Statement*. Also see Appendix C, pp. 7 and 32 of the *Annual Information Form* filed by Western Forest Products, dated March 27, 2006. In addition, see Appendix D, *Ownership and Inter-Corporate Linkages of Selected Forest Companies in British Columbia*, prepared by the Economic and Trade Branch, Ministry of Forests, based on information publicly available in March 2007.

⁴ See p. 2, top diagram, and the notation at the bottom of that page.

If the answer to both questions was yes, the Ministry was obligated to consider whether WFP's TFLs should be cancelled, pursuant to s. 54.5. Therefore those two important questions are considered below.

1. Did Tricap's (Brookfield's) purchase of additional shares, which increased its ownership of WFP to 70%, change control of the company, as per s. 54.5?

WFP was clearly aware of the Minister's power to cancel its TFLs under s. 54.5, if corporate control of WFP changed. In WFP's filed 2006 *Annual Information Form* (Appendix C), WFP discusses the importance of not allowing Brookfield (Tricap) to hold more than 49% of WFP's common shares, for fear of triggering the cancellation provisions of s. 54.5.

That *Annual Information Form* describes WFP's strategy for ensuring that Brookfield (Tricap's) new 70% ownership of WFP never be reflected in majority control of voting shares. This would be done by creating a class of non-voting shares, and so on.⁵

Significantly, however, the WFP document appears to leave open the possibility that control may have been allowed to exceed 49% at some point:

However, it may be necessary in certain limited circumstances to undertake subsequent financing or other transactions in order to prevent the occurrence of a change of control as a consequence of the issuance of securities in accordance with the Subscription Receipt Agreement, and we may determine that it is not possible or practical, from a business perspective, to implement such transactions. If such change of control were to occur, whether by the subsequent acquisition of additional Common Shares by Tricap Management or by other members of the Tricap Group or otherwise, there could be significant adverse consequences to Western...if Tricap Management...were to acquire sufficient Common Shares to constitute a change or acquisition of control of Western, and the Minister of Forests were to be satisfied the change or acquisition of control unduly restricted competition in

⁵ See Appendix C, p. 32.

standing timber, log or wood chip markets, the Minister of Forests could make a determination to cancel all or a part of our Forest Act tenures...⁶

[Emphasis added]

Note that WFP states that it may not be "possible or practical" for them to implement the transactions necessary to prevent the change of control that would trigger s. 54.5.

This concession raises a critical question – was the limit of 49% ever actually exceeded? Did this possibility of exceeding that limit – which is admitted – actually come to pass? We are told that it may not have been "possible or practical" for WFP to prevent "the occurrence of a change of control". The natural question is, did that change of control ever happen?

In other words, after Brookfield (Tricap) obtained 49% of the voting shares during the 2006 WFP rights offering, did they subsequently (even inadvertently) obtain additional shares to exceed 50%? Did Brookfield achieve majority control of WFP at any time prior to the January 25, 2007 decision of the Minister to delete the TFL private lands?

Alternatively, consider that the WFP document states that the non-voting shares owned by Tricap will indeed have certain powers – they will have the right to vote on liquidation, dissolution, winding-up, sale, lease or exchange of all or substantially all of property, etc.⁷

Do those substantial powers of Tricap's (Brookfield's) non-voting shares, combined with 49% of actual voting shares, combined with the un-stated but prima facie influence granted by their total ownership of 70% of WFP, put them in a position to "otherwise effectively control the operations and direction of the corporation"? Clearly, effective control of operations and direction of the corporation can be exercised with something less than 50% of voting shares.

Indeed, it worth noting that the "direction of the corporation" seems to have changed, since Brookfield took majority ownership. As you will see in the Addendum to this document, Brookfield is an entity that focuses on real estate sales and development. Since Brookfield took majority ownership, we have seen

⁶ See Appendix ____, p. 32.

⁷ See p. 32, *Western Forest Products 2006 Annual Information Form*, Appendix C.

WFP move into real estate sales in a focused way, in contradistinction to its previous focus on forestry operations.

At a minimum, the Ministry of Forests should have fully inquired into the critical question of whether control of WFP had actually changed, so as to trigger a s. 54.5 review of the licence. Did the Ministry consider this, and inquire into it?

Was this potential change of control of the licensee considered, to determine whether Government had the right to reacquire the Crown TFL tenures for the public? At the same time that the company was asking the Government to jettison the long-established structure of the TFLs and release all private lands, did Government ever consider whether it had the right to re-acquire the Crown tenures from those lands?

Furthermore, was the issue ever raised by Government with WFP during TFL negotiations?

2. Could the change of control unduly restrict competition?

If the Minister found that "control" of WFP had changed, he would have been obliged to consider the other prerequisite for a Ministerial cancellation of TFLs. Among other things, section 54.5 authorizes cancellation of a TFL when control of a licence holder changes, if the change "unduly restricts competition in standing timber, log or woodchip markets". Therefore, if the Minister had evidence of a change in control, he was obliged to consider whether such undue restriction of competition would take place.

On the issue of restriction of competition, it should be noted that Brookfield has, in recent years, gained control of most of Vancouver Island's public and private timberlands. Brookfield has become the majority owner of:

- Western Forest Products, British Columbia's largest coastal forest company,
- Canfor's former TFL 37 public lands,
- The vast tracts of Weyerhaeuser's former TFL 44 public lands

(through WFP's acquisition of Cascadia, largest Crown tenure holder and one of the largest lumber producers on the BC coast),⁸ and

- Weyerhaeuser's former coastal private lands (deleted from TFL 44 in 2004 and subsequently spun off into Island Timberlands, second largest private timberlands holder in BC, 50% owned by Brookfield.)⁹

The convergence of ownership of forest companies is graphically illustrated in the Ministry of Forests document found at Appendix D (p. 2 at the top).

Significantly, on November 10, 2005 – the same day that Brookfield's Tricap purchased 51.3 million Subscription Receipts to buy WFP -- WFP announced its own acquisition of Cascadia Forest Products¹⁰.

Obvious questions arise about the impact of this converging ownership structure on competition on timber, log and woodchip markets. Did the Minister of Forests investigate those questions when he removed all private lands from the TFLs, while allowing WFP to retain possession of all the Crown tenures in the same TFLs?

In other words, did he fully investigate the possibility that the public might have had the right to acquire the Crown TFL tenures from WFP at about the same time as he was deleting all the private lands from those TFLs?

If the Ministry did not thoroughly investigate these matters at the time that it was determining the future of these Tree Farm Licences, questions arise about whether it exercised due diligence to manage Crown resources and finances in

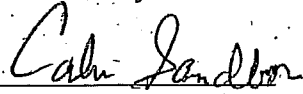
⁸ See WFP's *Annual Information Form*, March 27, 2006, at p. 6.

⁹ See, for example, the Ministry of Forests graph in Appendix D, p. 2 at the top,

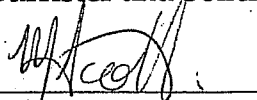
¹⁰ See WFP's *Annual Information Form*, March 27, 2006, pp. 6-7.

an economic, effective, and efficient manner. We respectfully request that you inquire into these matters.

Yours truly,



Calvin Sandborn
Barrister and Solicitor



Michaelin Scott
Law Student

ADDENDUM

What is this corporation called Brookfield Asset Management Inc.?

On its website, Brookfield describes itself:

Brookfield is a global asset manager focused on property, power and other infrastructure assets with approximately US\$90 billion of assets under management.

We own and manage one of the largest portfolios of both premier office properties and hydroelectric power generation facilities as well as transmission and timberland operations, located in North and South America and Europe...

Property

...We provide our clients with the opportunity to invest with us in our areas of expertise, including: core office, opportunistic real estate, Brazilian real estate and mezzanine lending.

Brookfield Properties is a commercial real estate corporation that owns, develops, and operates premier assets in the downtown cores of high-growth North American cities. Our signature properties define the skylines of many major metropolises including New York, Boston, Washington, D.C., Los Angeles, Houston, Toronto, and Calgary...

From the World Financial Center in New York to Brookfield Place in Toronto, from Bankers Hall in Calgary to Bank of America Plaza in Los Angeles, Brookfield Properties' distinguished portfolio attracts...

The corporate website boasts about its new 26 acre development in Manhattan:

Brookfield Properties is pleased to present its vision for Hudson Yards, the most significant development opportunity for New York City in the 21st Century.¹¹

¹¹ Brookfield Asset Management website.

