FOREST INDUSTRY CONTRACTORS ASSOCIATION

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Forestry Contracts Best Practice Guide

The recent log price downturn has affected contractors throughout New Zealand. The log price now seems to be on the increase, so whether you're going to start setting up, renewing and/or reviewing contracts we want to ensure you put your best foot forward.

Taking lessons learned from recent months, FICA has consulted our sponsors and partners in finance and accountancy to put together this forestry contract advice guide for all contractors to consider.

What is this guide?

- Take the lessons learnt from the recent downturn
- Provide a best-practice advice guide for everyone to consider
- Incorporate contract considerations when setting up / renewing / reviewing contracts

Summary Checklist

1. Do you have a 120-day notice period?
2. Is there provision for paying stand-down rates for circumstances outside your control?
3. What is your profit margin?
4. What weight do you capitalize them with new equipment?
5. Is there an allowance for variable costs?
6. What are the infrastructure needs and implications?
7. Who is going to be contracted to do the log cartage?
8. Is there an uplift penalty clause?
9. Has a harvest plan been completed?
10. What are the location factors and implications?
11. What are the special conditions of the forest?
12. Will the contract be a fixed-term contract or is it intended to be open ended?
13. Can you terminate your contract without penalty?

120 Day Notice Period

1. Do you have a 120 day notice period?

Allow for a 120-day period to provide flexibility in a downturn, as traditionally markets bottom out within 3 months and then you would hope they will turn around and decide to continue logging the job again.

A. The first 90-days at a reduced production rate (say 10% reduction in contract volumes per month).
B. At the end of 90 days the forest owner can serve 30-day termination notice if they still are unhappy with market prices.

Stand-down rate

2. Is there provision for paying stand-down rates for circumstances outside your control?

If something happens outside your control e.g. adverse weather events, road failures, poor trucking, interrupted shipping etc, ensure there is a clause allowing for payment of a stand-down rate.

Profit margin

3. What is your profit margin?

If in an exposed woodlot environment, ensure you have a stacked rate with no less than a 10% profit margin.

4. What weight do you capitalize your rate with new equipment?

This depends on whether you are a one crew operation or multiple with the ability to pull back to corporate crews and how much confidence you have in ongoing work. Consider trade-offs are re-debt/repair/
production risks, appropriate weightings attached to each are very dependent on individual circumstances

Variable costs

5. Is there an allowance for variable costs?

A. Ensure there is a monthly escalation clause for key variable inputs (particularly fuel).
B. Ensure there is an annual review clause covering all costs for contracts over 12 months (such as wages, capex).

Infrastructure

6. What are the infrastructure needs and implications?

A. Does the forest need road-lining and skids prepared? If yes, who will be contracted to do the logging work for this infrastructure prior to clear-fell?
B. What are the timeframes for staging road-lining/skid logging and the clear fell? i.e. are the new roads and landings going to be 'green' when the clear fell crew arrives, or will they have had a chance to settle?
C. Is the local roading network able to handle logging trucks? What are the bridges like? Are there rivers in the valley's that could flood and impede access to the job?
D. Is the work solely a summer job or can you work all year round? Woodlot winter logging can be difficult with under-funded infrastructure.
E. Has a Resource Consent been granted for the logging of this forest? Read it and see what issues have been raised by the local authority.
F. Most importantly, do daily production targets reflect the realities of the above?

Site location

7. What are the location factors and implications?

A. Consider the site in relation to ports or sawmills. If it's a long way away from market, then it will be the first to be affected by log price collapsing.
B. Will an isolated location increase your costs to get machinery repairs? Everything becomes more expensive so should you consider using new or near new machinery to mitigate this cost and downtime risk? (Refer 4).
C. Transporting into woodlots can be expensive and difficult to transport too, some requiring significant walking of machines due to bridge and access conditions. This should be factored as it also chews into valuable production time.

Uplift / Cartage

8. Who is going to be contracted to do the log cartage?

Assess the cartage contractor, meet them and talk through issues. If you can, try and get a gauge as to how busy they are and if they are happy with the cartage rates.

9. Is there an uplift penalty clause?

Uplift needs to be locked in with a penalty clause that can be invoked. Cartage rates have got to be sustainable for log trucks, so they don't divert elsewhere.

10. Has a harvest plan been completed?

A. What are the average haul distances for the clear fell operations?
B. What are the maximum haul distances?
C. Is there a market for the pulp, or will it be left behind so the contractor won't get paid for pulling it?

Special considerations

11. What are the special conditions of the forest?

A. Are there areas bounding streams/rivers, protected native forest, wahi tapu, etc? You need to be able to determine risk mitigation contingencies and special pricing conditions around these issues. Where does the liability with these issues lie?
B. Is the entire forest economic to log or are there areas that will need to be left due to the cost of logging/roading them?
C. What are the boundary issues with neighbours (restricted access, assisted tree falling, fence reinstatement etc)? Does the forest owner get on with the neighbouring farmer? Even go to the extent of visiting the farmer and get an understanding of the neighbouring farmers' expectation around the harvest and post-harvest reinstatement.
D. What is the local community attitude to forestry? Are people likely to be unhelpful and even hostile towards forestry contractors?

Contract term

12. Will the contract be a fixed-term contract or is it intended to be open ended?

Exit clause for contractor

13. Can you terminate your contract without penalty?

Make sure you can terminate your contract with reasonable notice and without penalty. Often contractors must leave a job for financial reasons only to find that income is withheld on the basis that remedial work is required at the job site.

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