

**IN THE MATTER OF THE *FOREST ACT*, R.S.B.C. 1996, C. 157 and IN THE MATTER
OF THE *TIMBER HARVESTING CONTRACT AND SUBCONTRACT REGULATION*,
B.C. REG. NO. 22/96 and IN THE MATTER OF THE FORESTRY REVITALIZATION
PROPOSAL MADE BY CASCADIA FOREST PRODUCTS LTD.
DATED OCTOBER 11, 2005**

BETWEEN:

POWELL DANIELS CONTRACTING

CLAIMANT

AND:

CASCADIA FOREST PRODUCTS LTD.

RESPONDENT

**ARBITRATION AWARD
FORESTRY REVITALIZATION PROPOSAL OF CASCADIA FOREST PRODUCTS
LIMITED DATED OCTOBER 11, 2005**

SOLE ARBITRATOR:

Paul J. Pearlman, Q.C.

DATE OF HEARING:

December 11, 12, 13, 14, 17, 2007
January 21, 2008

DATE OF AWARD:

February 24, 2008

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Introduction

1. This Arbitration concerns a fairness dispute pursuant to s. 33.22(h) of the *Timber Harvesting Contract and Subcontract Regulation*, B.C. Reg. 22/96 as amended (the "*Regulation*"), between Powell Daniels Contracting ("Powell Daniels") and Cascadia Forest Products Ltd. ("Cascadia").
2. The dispute arose on October 31, 2005, when Powell Daniels made its fairness objection to Cascadia's Forestry Revitalization Proposal dated October 11, 2005.
3. Powell Daniels objected to Cascadia's Forestry Revitalization Proposal on the basis that it did not comply with the AAC reduction criteria set out in the *Regulation*, and that the AAC reduction criteria had not been applied fairly, impartially and without regard to past disagreements between Powell Daniels and Cascadia.
4. In March, 2003, the Province enacted the *Forestry Revitalization Act*, S.B.C. 2003, c. 17 by which the Government took back 20 percent of the Crown timber allocated to major licensees throughout British Columbia, including Cascadia. At the same time, the Provincial Government announced that 20 percent of the timber harvesting rights of major licensees would be reallocated

for various public policy purposes to British Columbia Timber Sales, to First Nations, and to community forests and woodlots.

5. The 20 percent take back and timber reallocation process implemented by the *Forestry Revitalization Act* (Bill 28) affected Cascadia's Tree Farm Licenses 39 and 44 and Forest Licenses A19225 and A19224, and reduced Cascadia's annual allowable cut from these four licenses by a total of 978,694 m³.

6. The *Regulation* sets out the process by which Cascadia, like other major licence holders, was required to prepare its Forestry Revitalization Proposal (the "Proposal") outlining how it intended to restructure its operations to the reduced allowable annual cut. Before the Bill 28 take back, Cascadia employed 68 replaceable contractors on its four tenures. Contractors impacted by the reductions proposed under the Proposal were entitled to notice, to vote on the Proposal, and, subject to the requirements of the *Regulation*, to arbitrate disputes arising under the Proposal.

The Legislative Framework

7. Section 33.2 of the Regulation provides:

33.2 (1) Subject to subsection (4), after receipt of an order from the minister under section 3(2) of the *Forestry Revitalization Act* for a group of licences, or after June 21, 2004 for an ungrouped licence, a licence holder may make one or more forestry revitalization proposals regarding the replaceable contracts pertaining to those licences to

- (a) vary the amount of work specified in, or to terminate, one or more of those replaceable contracts, or
- (b) change a contract such that it pertains to a different licence.

8. Section 152 of the *Forest Act*, R.S.B.C. 1996, c. 157 defines a "replaceable contract" as follows:

"Replaceable contract" means a contract

- (a) that includes a requirement that the holder of the forest licence, timber licence or tree farm licence, as the case may be, by a prescribed time before expiry of the existing contract, must, if the contractor has satisfactorily performed the existing contract up to the time of the offer, make an offer to the contractor, conditional on the contractor continuing to satisfactorily perform the existing contract, of a replacement contract that
 - (i) provides for payment to the contractor of the amounts agreed by the parties, or failing agreement, of the amounts settled by the method of dispute resolution provided under the existing contract at the time of the offer, and
 - (ii) subject to a requirement as to length of term prescribed under section 157(d)(ii), is otherwise on substantially the same terms and conditions as the existing contract, and
- (b) that conforms to the requirements for replaceable contracts prescribed under section 157; ...

9. If a forestry revitalization proposal is not rejected by the prescribed threshold number of replaceable contractors, under the *Regulation* it is deemed to be accepted. Impacted contractors who objected to the proposal may nonetheless make "fairness objections" under Section 33.42(1) of the *Regulation*, which provides:

- 33.42 (1) If a forestry revitalization proposal in respect of the coastal area is not rejected under section 33.41(2) within 30 days after the last day the proposal is delivered to a contractor,
- (a) the forestry revitalization proposal is deemed to be accepted and each contract entered into by the licence holder in respect of the licenses in the proposal is deemed to be amended or terminated as provided for in the proposal, and
 - (b) if one or more impacted contractors who objected to the proposal have made a fairness objection under section 33.4(5), a dispute is deemed to exist between the licence holder and each impacted contractor who objected to the proposal and who made a fairness objection.

10. Section 33.1(1) of the *Regulation* defines "fairness objection":

33.1 (1) "fairness objection" means the inclusion in an objection to a forestry revitalization proposal under section 33.4 by an impacted contractor of notice that the contractor believes the requirements of section 33.22(h) have not been met in respect of that contractor and the reasons why the requirements have not been met; ...

11. Under Section 33.42(2) of the *Regulation*, only one issue arises on a fairness objection:

33.42 (2) For a dispute deemed to exist under subsection (1),

- (a) the sole issue is whether a forestry revitalization proposal deemed to be accepted meets the requirements of section 33.22(h) with respect to the impacted contractors who have made fairness objections.
- (b) the conciliator may have regard to other forestry revitalization proposals made by the licence holder, and
- (c) if the conciliator concludes that the requirements of section 33.22(h) are not met in respect of one or more of the impacted contractors who have made fairness objections, the licence holder is liable to those impacted contractors for damages in an amount determined by the conciliator in accordance with section 33.7.

[emphasis added]

12. Section 33.22 of the *Regulation* sets out the requirements for a forestry revitalization proposal:

33.22 A licence holder in making a forestry revitalization proposal must do the following:

- (a) make the proposal in writing;
- (b) specify the licences that are included in the proposal;
- (c) list each contractor with a replaceable contract that pertains to a licence included in the forestry revitalization proposal and show the amount of work specified in each contract;
- (d) specify how the licence holder proposes that the amount of work specified in each replaceable contract will be increased or decreased, if at all, and the proposed date of increase or decrease;

- (e) specify those replaceable contracts that the licence holder proposes to terminate, if any, and the proposed date of termination;
- (f) specify any proposed changes to a replaceable contract to cause it to pertain to a different licence and the proposed date of change;
- (g) describe how the forestry revitalization proposal takes into account the AAC reduction criteria;
- (h) apply the AAC reduction criteria fairly, impartially and without regard to any past disagreements between the parties;
- (i) include enough information to allow a contractor acting reasonably to determine if and how the licence holder is complying with s. 33.21; deliver the proposal to each contractor with a replaceable contract that pertains to a licence that is included in the forestry revitalization proposal.

[emphasis added]

13. In s. 1 of the *Regulation*, “AAC reduction criteria” and “AAC reduction proposal” are defined as follows:

“AAC reduction criteria” means each of the following factors:

- (a) achieving a contractor configuration that optimizes the ~~effective utilization of capital within all timber harvesting operations carried out under all licences included by a licence holder in an AAC reduction proposal or a forestry revitalization proposal;~~
- (b) achieving a contractor configuration that optimizes the efficiency of all timber harvesting operations carried out under all licences included in an AAC reduction proposal or a forestry revitalization proposal by a licence holder;
- (c) the demonstrated historical operational effectiveness, ability to carry out timber harvesting operations and compliance with safety, environmental and other applicable laws of each contractor with a replaceable contract pertaining to any licences held by a licence holder;
- (d) minimizing the overall need for geographic relocation by contractors and company operations to operating areas different than those they have traditionally operated in;

“AAC reduction proposal” means a proposal made under Part 5 Division 5 that the amount of work specified in a replaceable contract be varied or a proposal that a replaceable contract be terminated; ...

14. Under Section 33.21(1) of the *Regulation*, the replaceable contract proportion (i.e. the aggregate amount of work allocated under replaceable contracts as a proportion of the total allowable annual cut under the group of licenses held by a licence holder after the Proposal) must not be less than the replaceable contract proportion immediately before the Bill 28 take backs.

15. In Section 33.1(1) of the Regulation, the definitions of “minimum replaceable contract proportion”, and “replaceable contract proportion” are as follows:

33.1 (1) “minimum replaceable contract proportion” means the replaceable contract proportion for

(a) a group of licences immediately before the order of the minister under section 3(2) of the *Forestry Revitalization Act* made in relation to the group of licences, or

(b) an ungrouped licence on March 31, 2003,

... ..

“replaceable contract proportion” means, at any given time for an ungrouped licence or a group of licences, the proportion determined by the formula

A/B

A is the aggregate amount of work, to be performed under all replaceable contracts pertaining to that ungrouped licence or group of licences having regard to the phase contribution amounts for phases under each contract, and

B is the allowable annual cut of that ungrouped licence or the aggregate of the allowable annual cuts of the group of licences;

16. Thus, a licensee may not reduce the proportion of its timber harvesting operations performed by replaceable contractors below the minimum replaceable contract proportion. However, the obligation to maintain the minimum replaceable contract proportion applies to the aggregate amount of work performed under all replaceable contracts pertaining to the group of

licences held, in this case, by Cascadia. The licence holder has the discretion to distribute the Bill 28 volume reductions among its tenures, as it sees fit, provided that it maintains the minimum replaceable contract proportion, and applies the AAC reduction criteria fairly, impartially, and without regard to past disagreements.

17. Section 10 of the *Forestry Revitalization Act* established the B.C. Forestry Revitalization Trust to provide compensation to contractors and their employees impacted by a proposal reducing or terminating their contracts. This scheme provides some compensation to replaceable contractors for lost harvesting rights, losses on equipment rendered redundant, and for severance pay.

18. Under Section 33.7 of the *Regulation*, an impacted contractor who establishes that a forestry revitalization proposal does not meet the requirements of Section 33.22(h) is entitled to receive damages from the licence holder under a statutory formula which takes into account the amount of mitigation funds the contractor receives under the Forestry Revitalization Trust.

19. This Arbitration is concerned solely with the issue of liability, i.e. whether the Proposal meets the requirements of Section 33.22(h) of the *Regulation*.

20. The provisions of the Regulation relating to fairness objections have recently received judicial consideration. *Western Forest Products Inc. v. Hayes Forest Services Limited*, 2007 B.C.S.C. 1469. In that case, the Honourable Madam Justice Lynn Smith found, at paragraphs 83 and 98, that the requirements imposed on licence holders under Section 33.22 do not require the licence holder, when making a forestry revitalization proposal, to consider alternatives which will mitigate the impact of the proposal on individual contractors.

21. In the course of interpreting the *Regulation*, the Court held:

83. ... The *Regulation* restricts the issue that arises when an impacted contractor makes a fairness objection, stating that “the sole issue” is whether the proposal “meets the requirements of section 33.22(h) with respect to the impacted contractors who have made fairness objections” (s. 33.42(2)(a)). The wording of s. 33.22(h) provides that the licence holder must “apply the AAC reduction criteria fairly, impartially and without regard to any past disagreements between the parties”: it does not provide that the licence holder must achieve a result which, insofar as possible,

keeps all contractors involved in the region in question. Finally, I note that the *Regulation* specifically contemplates that one or more of the replaceable contracts under the licence may be terminated.

84. Those features of the wording all seem to support the petitioner's position, which is that the legislature did not intend to require licence holders to consider alternatives which would mitigate the impact of the contract on individual contractors beyond what is inherent in the application of the AAC reduction criteria fairly, impartially and without regard to any past disputes between the parties.

86. *Sullivan and Driedger on the Construction of Statutes* (Ruth Sullivan, 4th ed., Toronto, Butterworths, 2002) at 158 states the presumption against tautology in legislation as follows:

It is presumed that the legislature avoids superfluous or meaningless words, that it does not pointlessly repeat itself or speak in vain. Every word in a statute is presumed to make sense and to have a specific role to play in advancing the legislative purpose.

87. In the context of s. 33.22(h) this presumption implies that the word "fairly" must have a meaning that is different from the meanings of the word "impartially" and the phrase "without regard to any past disagreement between the parties."

88. The *Oxford English Dictionary* (2nd ed., J.A. Simpson and E.S.C. Weiner, eds. Oxford: Clarendon Press, 1989) definition for "fairly" reads, in part, as follows:

Of conduct, actions, arguments, methods: Free from bias, fraud, or injustice; equitable, legitimate.

89. The term "fairly" in the context of s. 33.22(h) is given meaning independent of the other terms if it refers to application of the AAC reduction criteria in a manner which is free from fraud or injustice, equitable, or legitimate. In my opinion it is not necessary, in order for "fairly" to have meaning, to read in criteria beyond the four AAC reduction criteria listed in the *Regulation* or to interpret the *Regulation* as requiring consideration of mitigation alternatives.

90. The purposes of the legislation are to promote stability and economic health in the forest industry and the communities which depend upon it by: (1) providing improved tenure security to logging contractors and subcontractors; and (2) redressing the imbalance of bargaining power between individual contractors and licence holders and achieving greater

fairness between them. These purposes are described by the Court of Appeal in the decisions cited by the respondent and referred to above.

91. ... The scheme requires that when licence holders make forestry revitalization proposals potentially affecting the work done by those holding replaceable contracts, the licence holders must apply the four AAC reduction criteria fairly, impartially and without regard to any past disputes between the parties. Licence holders must give notice to the affected contractors, who may vote to approve or not approve the proposal, and who may file disputes to it if they do not approve. The AAC reduction criteria themselves incorporate consideration of how the proposal would affect contractors, including geographic displacement. The scheme contemplates that the licence holder will make a proposal which takes into account the economic impact of the proposal on contractors as well as on the licence holder.

92. The AAC reduction criteria appear to be focused on these objectives: (1) optimize the effective utilization of capital within timber harvesting operations; (2) optimize the efficiency of timber harvesting operations; (3) recognize the effectiveness and compliance history of contractors; (4) minimize geographic relocation of contractors.

96. The four AAC reduction criteria set out rational considerations licence holders must take into account when making proposals, and the dispute process allows a contractor to dispute the fairness of the manner in which the criteria were applied. In this scheme both the licence holder's interest and the interests of contractors with replaceable contracts must be taken into account.

Western Forest Products Inc. v Hayes Forest Services Limited, 2007 BCSC 1469 (Western).

22. Although Madam Justice Smith overturned my award in *Hayes Forest Services Limited v. Western Forest Products Inc.* (May 31, 2006) on the point that Section 33.22(h) of the Regulation does not require licence holders to consider mitigation alternatives for impacted contractors, the Court expressed no disagreement with my conclusions that Section 33.22(h) applied an objective test, and that the section must be read disjunctively.

23. At Paragraphs 49 and 55 of *Hayes Forest Services Limited v. Western Forest Products Inc.*, *supra*, I said this:

49. I agree that the test here is not perfection, but rather whether Western, in making the Proposal, has applied the AAC reduction criteria in a manner

that a reasonable person would regard as fair, impartial, and made without regard to any past disagreement between the parties.

- ...
- ...
- ...
55. The object of Division 5.1 of the *Regulation* is to provide a process for licence holders to make forestry revitalization proposals, for contractors to evaluate and respond to those proposals, and for the conciliation of disputes respecting those proposals. The *Regulation* endeavours to balance the interest of the licence holder in reconfiguring its operations and contractors so as to best absorb the impact of the twenty percent AAC reduction, with the interests of those contractors who may be faced with the loss or diminution of a valuable asset, their replaceable logging contract. Division 5.1 of the *Regulation* seeks to achieve this balance in part by prescribing requirements for the contents and delivery of the proposal, and by holding the licence holder to an objective standard of fairness. An interpretation of section 33.22(h) under which a fairness complaint was defeated because the contractor was only able to establish that the proposal was unfair or partial, but was not able to show that it was made with regard to past disagreements would defeat the purpose of division 5.1 of the *Regulation* and would therefore be absurd.

Summary of Applicable Principles

24. The *Regulation* contemplates that a licence holder, such as Cascadia, that holds a group of licences may treat them as a single "fibre basket" for the purposes of a forestry revitalization proposal. The licence holder is not obliged to maintain the minimum replaceable contract proportion on a licence-by-licence, or block-by-block basis. Rather, it has a broad discretion to allocate the Bill 28 volume reduction across all of its licences, provided that it does so in a manner that meets the requirements of Section 33.22(h) of the *Regulation*.

25. The *Regulation* contemplates that replaceable contracts may be terminated under a proposal. (*Western, supra*, para. 83).

26. Section 33.22(h) does not require the licence holder to achieve a result which, insofar as possible, keeps all contractors involved in the region in question. (*Western, supra*, para. 83).

27. The Legislature did not intend that licence holders must consider mitigation alternatives. (*Western, supra*, paras. 84, 98).

28. The term “fairly” in Section 33.22(h) refers to the application of “the AAC reduction criteria in a manner which is free from fraud or injustice, equitable, or legitimate” (*Western, supra* at para. 89).

29. The licence holder is not required to meet a standard of perfection, rather the test is whether it has applied the AAC reduction criteria in a manner that a reasonable person would regard as fair, impartial, and made without regard to any past disagreements between the parties.

30. The legislative scheme “contemplates that the licence holder will make a proposal which takes into account the economic impact of the proposal on contractors as well as on the licence holder”: (*Western, supra*, at para. 92).

31. The purpose of the *Regulation* is described by the Honourable Madam Justice Lynn Smith in paragraph 90 of her Reasons in *Western, supra*, cited above. In the case of a forest revitalization proposal, the purpose of the *Regulation* is given effect through the application of the AAC reduction criteria which incorporate consideration of how the proposal would affect contractors, and set out the rational considerations that licence holders must take into account when making proposals. (*Western, supra*, at paras. 92, 93 and 96).

Facts

32. Powell Daniels operated from 1988 to 2005 as a stump-to-dump logging contractor at Powell Lake, in the Stillwater Division of TFL 39. The Claimant held a replaceable logging contract which, at the time it was terminated by Cascadia, entitled Powell Daniels to harvest 203,309 m³ of timber each year.

33. Powell Daniels was an efficient logging contractor, and throughout the seventeen years it operated at Powell Lake, acquired, developed, and deployed equipment, infrastructure and crews well suited to the particular water based nature of its operations at Powell Lake.

34. Powell Daniels’ replaceable logging contract pertained to TFL 39, which in addition to Block 1, the Stillwater Division, included Blocks 2 and 5, the North Island Division, Blocks 3 and 4, the Port McNeil Division, Block 6, the Queen Charlotte Division, and Block 7, Port McNeil Division (Doc Creek).

35. The Stillwater Division contains two areas: Powell Lake, which was the traditional operating area of Powell Daniels under its replaceable contract, and the Stillwater Valley. Another stump-to-dump contractor, Olympic Forest Products Ltd., had operations in the Stillwater Valley, as well as in the Queen Charlotte Division, prior to Cascadia's proposal.

36. Subsequent to the enactment of Bill 28, Weyerhaeuser, which then held TFL 39, TFL 44, and Forest Licences A19225 and A19244, engaged in discussions with various contractors operating in TFL 39 to explore whether they were prepared to voluntarily reduce or terminate their replaceable contracts. These discussions took place at a time when there was some uncertainty about how the Bill 28 volume reductions would be applied, and prior to the promulgation of Division 5.1 of the *Regulation*, which established the regulatory framework for the *Forestry Revitalization Act* AAC reductions.

37. Among the contractors who volunteered to either terminate or reduce their replaceable contracts were Greenstone Logging Ltd., which operated in the North Island Division of TFL 39, Pacific Thinning Ltd., which operated in the Stillwater Division, and Island Pacific Logging and Edwards and Associates Logging Ltd. (Edwards), both of which operated in the Queen Charlotte Division.

38. Edwards held a replaceable logging contract with Weyerhaeuser with a volume entitlement of approximately 275,000 m³ per year. In addition, Edwards and Weyerhaeuser were also parties to a non-replaceable logging contract which provided for an annual harvest of 500,000 m³, less the volume harvested by Edwards pursuant to its replaceable logging agreement. By a logging contract implementation agreement, Weyerhaeuser had engaged Edwards to manage and perform timber harvesting work formerly performed by Weyerhaeuser's company crew in the Queen Charlottes. Edwards performed that work under its non-replaceable logging agreement with Weyerhaeuser.

39. In the fall of 2004, Edwards offered to reduce the cut under its replaceable contract by 60,000 m³. Due to land use controversies in the Queen Charlotte Islands, Edwards was unable to achieve its full volume of 500,000 m³. It saw the Bill 28 process as an opportunity to reduce its employee complement and to take advantage of compensation available for that purpose under the Forest Revitalization Trust.

40. For its own part, Powell Daniels had informal discussions with Weyerhaeuser about potentially reducing its cut by 20,000 m³, if that were necessary to achieve the requisite volume reduction in TFL 39. At the time of these discussions, Weyerhaeuser appears to have been proceeding under the impression that the Bill 28 volume reductions would be implemented on a block-by-block and licence-by-licence basis, similar to the particular volume reductions ultimately set out in the two Orders made pursuant to Bill 28 by the Minister of Forests on December 21, 2004.

41. In any event, none of the discussions which took place between Weyerhaeuser and the replaceable contractors relating to the voluntary reduction or termination of their replaceable contracts resulted in any binding commitment on the part of the licence holder.

42. In May, 2005, Cascadia acquired the four licences previously held by Weyerhaeuser and, during the period July through September, 2005, developed its Proposal.

43. Mr. Jim Jackson, Cascadia's Director of Operations, was responsible for developing the Proposal. He was assisted by a team which included Stan Coleman, the former Unit Manager for TFL 44, Jeff Terman, the Contract Manager for the Stillwater Division of TFL 39, and representatives of Cascadia's other divisions.

44. Unfortunately, Mr. Jackson passed away prior to the hearing of this Arbitration. However, on November 30, 2005 he prepared a memorandum describing Cascadia's approach to the development of the Proposal.

45. I am satisfied that Mr. Jackson's memorandum, although hearsay, is properly admissible under the principled exception to the hearsay rule: *R. v. Smith*, [1992] 2 SCR 915. Here, where the declarant is deceased, the test of necessity is met. Because Mr. Jackson prepared his report in the ordinary course of his duties, and at the request of Cascadia's President in circumstances where accuracy was required, I am satisfied that Mr. Jackson's memorandum meets the threshold of reliability.

46. Once Mr. Jackson and his team, after taking legal advice, determined that Cascadia could, under the *Regulation*, make a proposal under which all four licences were treated as a

single fibre basket, Cascadia identified the basic objectives for its Proposal. Mr. Jackson describes those objectives in his memorandum of November 30, 2005 as follows:

Upon determining our fibre basket approach we set out basic objectives to be accomplished within the terms of the legislation:

They were:

- (a) We would not increase our Bill 13 obligations. We would target the PCA cap within the FRP.
- (b) We would maximize the reduction of the number of Bill 13 contracts. Where possible, we would concentrate on terminations rather than volume reductions.
- (c) We would maintain full phase contractor presence where it interfaced with Company crew operations and provided us cost and operating advantages.
- (d) We would reduce Bill 13 phase contractors in our Company crew operations to position those operations for turnover to full phase contracting if required in the future.

During August and September we evaluated many combinations of contractor reductions and the pros and cons of each option.

During this process we recognized an opportunity we had not anticipated, which was the creation of unallocated cut that we could utilize as "open bid volume" within our tenures. This opportunity provides us the ability to bid out work and create bench making comparisons for future Bill 13 rate negotiations.

This opportunity was then built into the FRP proposal.

Exhibit 5, Volume 2, Tab 36.

47. The "cap", or minimum replaceable contract proportion for Cascadia's Proposal was 42 percent, because prior to the Proposal, 42 percent of the timber harvesting work on the four licences had been performed by replaceable contractors.

48. Mr. Coleman described the guiding principles of the Cascadia team in these terms:

- A Overall, one was we needed to, of course, meet the requirements of the regulation. The other was to improve our business. In other words, this is

a revitalization plan and as we do this restructuring to improve our overall business. The other was we wanted to reduce the number of Bill 13 contractors, in a sense wanted to improve the overall administration handling and then other benefits that can come by reducing some of the contractors. Also, we had what you'd call unallocated wood that we can put out for open bid. So we wanted to protect the unallocated wood that we had through this process as well as investigate to see other opportunities to create some more unallocated wood.

Stan Coleman Disposition, Volume 1, December 6, 2007, pp. 24 – 25.

49. In developing its proposal, Cascadia was confronted with the difficult task of determining how to allocate the Bill 28 volume reduction of almost 1,000,000 m³ among its company operations and some 68 contractors operating under 79 different replaceable contracts on the four tenures.

50. Cascadia developed a spreadsheet to assist the Proposal team in assessing numerous contractor combinations during July, August and September, 2005.

51. Cascadia made its Proposal on October 11, 2005.

52. Cascadia's Proposal, in addition to terminating Powell Daniels' contract, impacted 20 other contractors, whose contracts were either terminated, or in only two cases, reduced. The proposal also impacted Cascadia's company operations. Most notably Cascadia eliminated its Spruce Lake company operation on TFL 44, which accounted for about 25 percent of the total allocation of the Bill 28 volume reduction.

53. In late July, 2005, Mr. Jackson advised Tymatt, a contractor specializing in mechanical falling and processing, that it should consider contacting Greenstone Logging Ltd., one of the contractors that had previously volunteered to have its contract terminated, to determine whether it was interested in selling.

54. On August 30, 2005, Mr. Jackson informed Greenstone's principal, Mr. Tom Olsen, that Cascadia had determined that it was not in its best interest to lose the Greenstone contracting presence in the North Island operation. Mr. Jackson also told Mr. Olsen that if he chose not to sell his business, Cascadia would continue to log with him, but that he should not count on his volunteer status for the Bill 28 buyout.

55. On October 7, 2005, KLM Industries Limited, a company related to Tymatt, entered a share purchase agreement for the acquisition of Greenstone.

56. Cascadia's Proposal retained, rather than terminated or reduced, the replaceable contracts for Greenstone Logging Ltd., Pacific Thinning, Island Pacific and Edwards.

57. Cascadia first notified Powell Daniels that its replaceable contract would be terminated under the Proposal on October 11, 2005. Mr. Monty Hussey, one of the principals of Powell Daniels, testified that he was shocked by the Proposal, and that he felt that the business that he, his partner and employees had developed over 17 years had been taken for no real reason.

Monty Hussey, Direct Examination, Transcript December 12, 2007, p. 18, 16 to p. 20, 15.

58. Mr. Hussey contacted the President of Cascadia and challenged him to look into the Proposal. He told Mr. Sutcliffe that he made a decision by November 16, 2005. On November 21, 2005, Mr. Ternan offered Powell Daniels 50,000 m³ of timber as transitional work. However, by then Powell Daniels was already in the process of removing equipment from Powell Lake. Mr. Hussey's response was that it was too little, too late.

59. Cascadia's Proposal received the requisite two-thirds level of support from replaceable contractors and, pursuant to Section 33.41(3) of the *Regulation*, was deemed to be accepted.

Issue

60. The only issue to be determined in this proceeding is whether Cascadia's Proposal met the requirements of Section 33.22(h) of the *Regulation*, which required Cascadia to "apply the AAC reduction criteria fairly, impartially and without regard to any past disagreements between the parties".

Claimant's Position

61. Powell Daniels submits that:

- (a) its replaceable contract was terminated to create unallocated cut in the Stillwater Division;
- (b) its replaceable contract was terminated to reduce the replaceable contract proportion of 42 percent; and
- (c) Cascadia's decision to terminate Powell Daniels was influenced by a disagreement which arose in April, 2005, when the Claimant refused to barge the equipment of another contractor on Powell Lake.

62. The Claimant argues that in these circumstances, it is necessary to address the following questions.

- (a) Did Cascadia apply the four factors in the AAC reduction criteria in making its decision to terminate Powell Daniels' replaceable contract?
- (b) Did Cascadia balance its own business interests with the interests of its contractors in a fair and impartial manner?
- (c) Was Cascadia's decision to terminate the replaceable contract made without regard to any past disagreements with Powell Daniels?

Claimant's Closing Submissions, para. 30.

63. The Claimant contends that it was not terminated to optimize the effective use of capital, or the efficiency of timber harvesting operations at Powell Lake, where it had developed a specialized and efficient operation.

64. Mr. Ternan's decision to terminate the Claimant was based, at least in part, on Cascadia's objective of creating unallocated cut, which might then be put out to competitive bidding. This would provide Cascadia the opportunity to have work performed, at lower rates, by non-replaceable contractors. It would also provide an opportunity to establish benchmarks for future rate negotiations with the remaining replaceable contractors. Powell Daniels submits that this objective is beyond the AAC reduction criteria. Another reason for Cascadia's decision to

terminate Powell Daniels was its objective of not exceeding the minimum replaceable contract proportion. In order to do this, and by the time Cascadia turned its attention to the Stillwater Division, it had to find about 180,000 m³ of volume to be removed. Powell Daniels argues that meeting the minimum replaceable contract proportion, or “cap” was not an objective falling within the AAC reduction criteria.

65. Further, the Claimant submits that Cascadia could have met the cap by taking the volume volunteered in the Queen Charlotte Division by Edwards and Island Pacific, rather than by eliminating an efficient contractor at Powell Lake who wished to continue in the logging business.

66. The Claimant submits that Cascadia was required, under Section 33.22(h) to balance its own business interests with the interests of its contractors in a fair and impartial manner, and that it failed to act fairly and impartially when it made decisions calculated to improve its own business, and without regard to the interests of its contractors. According to the Claimant, Cascadia, in making its Proposal, was obliged to act impartially as between itself, and its contractors.

67. The Claimant also submits that Weyerhaeuser, through its discussions with contractors who were prepared to voluntarily reduce or terminate their contracts, raised the expectations of contractors, including Powell Daniels, and that Cascadia was obliged to take those expectations into account in making its Proposal. Specifically, the Claimant maintains that if Powell Daniels knew that its replaceable contract was going to be terminated, and that Greenstone Logging Ltd. would not be impacted, it would have made an agreement to acquire Greenstone’s volume. Because Powell Daniels had no notice of the Proposal before October 11, 2005, it was too late to negotiate with Greenstone.

Cascadia’s Position

68. Cascadia submits that the objectives for its Proposal were consistent with the AAC reduction criteria and were aimed at assuring the efficiency and long-term viability of the operations of both the licence holder and its remaining contractors.

69. Cascadia argues that in developing its Proposal it considered numerous options. Ultimately, it put forward a Proposal that balanced its needs with the interests of its remaining contractors, and which met the requirements of Section 33.22(h) of the *Regulation*.

70. The Respondent submits that it was under no obligation to terminate or reduce the contracts of those contractors who had volunteered, particularly when the reductions offered by the volunteering contractors would not have met the objectives of its proposal or benefited Cascadia.

71. Finally, the Respondent submits that no past disagreement influenced its decision to terminate Powell Daniels' replaceable contract.

Discussion.

72. I will begin by considering whether the objectives of Cascadia's Proposal, as outlined by Mr. Jackson, were consistent with the AAC reduction criteria. I will then consider whether Cascadia applied the AAC reduction criteria fairly and impartially. Finally, I will address the question of whether Cascadia's decision to terminate Powell Daniels' replaceable contract was made without regard to past disagreements.

Cascadia's Proposal and the AAC Reduction Criteria

73. The objectives of Cascadia's Proposal were that:

- (a) Cascadia would not increase its Bill 13 obligations, but would aim to maintain the replaceable contract proportion at 42 percent;
- (b) Cascadia, in reducing the number of Bill 13 contracts would concentrate on terminations rather than volume reductions;
- (c) Cascadia would maintain full phase contractors where they interfaced with company operations and provided cost and operating advantages;

- (d) Cascadia would reduce Bill 13 phase contractors in the company crew operations to allow for future contracting out of company operations;
- (e) In addition, Cascadia would take advantage of opportunities to create unallocated volume that might be put out for bid, and to benchmark future Bill 13 rate negotiations.

74. For ease of reference, I repeat here the four AAC reduction criteria.

- (a) achieving a contractor configuration that optimizes the effective utilization of capital within all timber harvesting operations carried out under all licences included by a licence holder in an AAC reduction proposal or a forestry revitalization proposal;
- (b) achieving a contractor configuration that optimizes the efficiency of all timber harvesting operations carried out under all licences included in an AAC reduction proposal or a forestry revitalization proposal by a licence holder;
- (c) the demonstrated historical operational effectiveness, ability to carry out timber harvesting operations and compliance with safety, environmental and other applicable laws of each contractor with a replaceable contract pertaining to any licences held by a licence holder;
- (d) minimizing the overall need for geographic relocation by contractors and company operations to operating areas different than those they have traditionally operated in;

75. In this case, AAC reduction criterion (c), demonstrated historical operational effectiveness, was really a neutral factor, in the sense that all of the stump-to-dump replaceable contractors were established and efficient operators.

76. In my view, Cascadia's objectives were entirely consistent with the AAC reduction criteria. In particular, they were aimed at achieving a contractor configuration "that optimizes the effective utilization of capital within all timber harvesting operations carried out under all licences" included in the Proposal. They were also aimed at optimizing the efficiency of all timber harvesting operations carried out under all licences included in the Proposal. With respect to criterion (d), minimizing the overall need for geographic relocation, any assessment of whether this criterion has been applied as required by Section 33.22(h) focuses not on the result

within a particular block, or operating area, but rather on whether the overall need for geographic relocation has been minimized when viewed globally, across the whole fibre basket.

77. The objective of maintaining the replaceable contractor proportion, rather than increasing Bill 13 obligations was clearly authorized by Section 33.21(1) of the *Regulation* which provides that absent a Ministerial Order under Section 33.21(2), a licence holder must maintain the “minimum replaceable contract proportion”.

78. The objective of maintaining, but not increasing Bill 13 obligations is aimed at achieving efficiency. I accept the evidence of Mr. Coleman that Bill 13 contracts were generally more expensive than non-replaceable contracts, and involved additional administrative commitments for the licensee. I also rely upon Mr. Ternan’s evidence that Bill 13 contract rates are \$4.00 to \$10.00 per cubic meter more expensive than non-replaceable contract rates. Maintaining rather than increasing the replaceable contract proportion is a permissible means of optimizing the efficiency of all timber harvesting operations carried out under all of the licences included the Proposal.

79. Similarly, I am persuaded by the evidence of Mr. Coleman, Mr. Nyman and Mr. Ternan that consolidating Cascadia’s timber harvesting operations among the reduced number of Bill 13 contractors was more efficient, for both Cascadia, and its remaining contractors (who would enjoy economies of scale), than simply reducing the volumes harvested by many contractors.

80. Cascadia implemented this objective consistently throughout its four licences. Of 21 impacted replaceable contractors, only two, Mars and Star, who operated on TFL 44, had their volumes reduced, rather than terminated.

81. Cascadia’s objective of maintaining full phase contractors where they interface with company operations was unique to its North Island Division, as a result of a labour relations settlement made there in 1986. Three of Cascadia’s replaceable contractors, including Greenstone, enjoyed “Window of ‘86” rights which enabled the Respondent to put these contractors to work in priority to its own company crews. This provided Cascadia with flexibility, and the opportunity to achieve efficiencies in the deployment of these contractors. It

was this factor which led Cascadia to retain Greenstone, and two other Bill 13 replaceable contractors who also enjoyed Window of '86 rights in the North Island Division.

82. Again, the reduction of Bill 13 phase contractors in company operations in order to permit future contracting out opportunities was consistent with achieving a contractor configuration that optimizes the efficiency of all timber harvesting operations. Bill 13 contracts linked to a company operation encumbered the ability of Cascadia to contract out work. Another labour arbitration, the Munroe Award, permitted licensees on the Coast to have work performed under non-replaceable contracts, subject to certain conditions. (Exhibit 5, Volume 3, Tab 37).

83. Under Cascadia's Proposal, 16 phase contractors were terminated in order to meet an objective consistent with the AAC reduction criteria: the elimination of a restriction on Cascadia's ability to contract out company operations and thereby achieve operational efficiencies.

84. As Cascadia developed its Proposal, it became apparent that some unallocated cut would be created as a result of getting to the "cap" or minimum replaceable contractor proportion of 42 percent. This unallocated cut offered efficiency to Cascadia's operations because it could be put out to bid under non-replaceable contracts. Furthermore, Cascadia realized that disposing of the unallocated cut by competitive bids provided a means of setting benchmarks for future Bill 13 replaceable contract negotiations. The creation of unallocated cut offered efficiencies by providing Cascadia with additional operational flexibility regarding the harvesting of unallocated volume. Furthermore, it offered some advantage to Cascadia in future market-based rate negotiations with its remaining Bill 13 contractors.

85. As Cascadia submits, when the *Regulation* was amended to include Division 5.1, regulating *Forestry Revitalization Act* volume reductions, it was also amended by the repeal of the existing contract rate dispute provisions, and their replacement by new provisions requiring arbitrators to determine rates "according to what a willing licence holder and a willing contractor acting reasonably and at arms' length in similar circumstances would agree is a fair market rate": *Regulation*, ss. 25.1 and 26.01. When I consider the AAC reduction criteria and Division 5.1 of the *Regulation* in the context of the other amendments made to the *Regulation* at the same time Division 5.1 was enacted, I conclude that the creation of unallocated cut in Cascadia's Proposal,

and the opportunity it presented for increased efficiency of the licensee's operation, including its impact on the determination of fair market rates for Bill 13 contracts, was indeed consistent with the AAC criteria.

Whether Cascadia Applied the AAC Reduction Criteria Fairly and Impartially

86. I find that Cascadia in seeking to achieve the basic objectives of its Proposal, applied the AAC reduction criteria in a manner that was objectively fair, and impartial.

87. In each of its operating divisions, it was guided by the same set of basic objectives although, of course, their application varied with the nature of the operation, and local conditions.

88. Cascadia made its Proposal under a legislative scheme which, as we have seen, entitled it to treat all of its licences as a single fibre basket, and which contemplated that contractors holding replaceable contracts may be terminated. Section 33.22(h) did not require Cascadia to achieve a result which kept all of its contractors in the Stillwater Division, or anywhere else. As the Court held in *Western, supra*, at paragraph 89, the AAC reduction criteria are applied "fairly" when applied in a manner which is free from fraud or injustice, equitable, or legitimate. Furthermore, the balancing of economic interests required by the *Regulation* is achieved through the application of the AAC reduction criteria which, as Madam Justice Smith stated in *Western, supra*, at paragraph 92, "incorporate consideration of how the proposal would affect contractors, including geographic displacement."

89. On the requirement that the criteria be applied impartially, in *Western, supra*, at paragraph 94, the Court said this:

... The arbitrator made no finding that Western had applied the criteria in a different manner when assessing Hayes' operation than it had when assessing the operations of the other contractors.

90. In my view, Section 33.22(h) of the *Regulation* requires that the licence holder apply the AAC reduction criteria impartially among the contractors. That is, the licence holder must not discriminate against, or favour one contractor over another for reasons unrelated to the fair and equitable application of the AAC reduction criteria.

91. The *Regulation* does not require the licence holder to apply the AAC reduction criteria in a manner that is completely impartial, or neutral as between itself and its contractors. Cascadia and its contractors had different and conflicting interests which would render the attainment of impartiality as between them impossible as a practical matter. Furthermore, Cascadia in making its proposal, was responding to the complex burdens imposed by the Bill 28 take back, and was endeavouring to restructure its own operations, and those of its remaining contractors in the manner most likely to ensure their continued economic viability. While the *Regulation* seeks to balance the interests of the licence holder and its contractors, it contemplates that the licence holder will have to make hard decisions, including the termination of some contractors, in order to effectively restructure timber harvesting operations throughout its various licences. That is precisely what happened in this case.

92. On the West Island, Cascadia completely eliminated its TFL 44 company operation which absorbed 250,000 m³ of the Bill 28 volume reductions.

93. Also in TFL 44, Cascadia reduced, rather than terminated two Bill 13 contractors, Mars and Star. It did so taking into account the strains already imposed on the local community by the termination of the company crew, and because Cascadia was able to provide reduced volume to these two contractors on a sustained basis.

94. In the Queen Charlotte Islands, Cascadia chose to eliminate three phase contractors rather than to reduce or eliminate the volumes volunteered by Edwards and Pacific Thinning Limited. Powell Daniels argues that Cascadia ought to have reduced volume in the Queen Charlottes, rather than in the Stillwater Division through the termination of the Claimant's replaceable contract. Edwards sought a partial reduction of its replaceable volume in order to deal with the impact on its operations of land use disputes in the Charlottes, including a blockade of its operations by the Haida, to obtain funds from the Revitalization Trust to pay severance to terminated employees. However, from Cascadia's perspective, reducing Edwards' cut offered no real efficiency, or any economic benefit. Edwards held both a replaceable and a non-replaceable contract with Cascadia. As previously discussed, its amount of work entitlement under the non-replaceable contract was 500,000 m³, less the volume harvested pursuant to its replaceable logging agreement. Therefore, any reduction made to Edwards' replaceable volume under the Proposal would not affect its total volume and corresponding crew and equipment obligations.

In addition, Edwards had received its annual volume entitlements of about 275,000 m³ under its replaceable contract. In all of these circumstances, reducing Edwards' replaceable volume would neither enhance efficiency, or the utilization of capital.

95. Cascadia's decision not to reduce or eliminate the replaceable volume of stump-to-dump contractors in the Queen Charlottes was a legitimate business decision, was consistent with the AAC reduction criteria, and was not objectively unfair.

96. On the North Island, Cascadia's operations included both contractor and company crews. I have previously found that the preservation of the advantage of full phase contractors with "Window of '86" rights, including Greenstone, was a key objective under the Proposal for the North Island, and that this was consistent with the AAC reduction criteria. I am also satisfied that Cascadia's decision to retain rather than terminate Greenstone does not advance Powell Daniels' fairness objection. Mr. Jackson did suggest that Tymatt speak with Mr. Olsen to determine whether he was interested in selling Greenstone. However, he also made it clear to Mr. Olsen that in dealing with Tymatt Mr. Olsen should do whatever he thought was best for his business. Mr. Jackson was "scrupulous" about staying out of the negotiations between Greenstone and Tymatt.

Tom Olsen, Cross-examination, Transcript, December 13, 2007, pp. 273 - 275

97. Greenstone continued to operate in the North Island Division. There is nothing in the evidence to suggest that Cascadia encouraged Tymatt to acquire Greenstone in order to have Greenstone perform work in the Stillwater Division that Powell Daniels, or anyone else had performed before the Proposal.

98. Because many of the decisions Cascadia made with respect to the retention, reduction or elimination of company or contractor operations were shaped by particular circumstances in the divisions to which those operations pertained, when Cascadia's team considered the Stillwater Division, the only way that the Respondent could get to "cap", and maintain, rather than increase its replaceable contract proportion was by terminating either the Claimant, or Olympic Forest Products Inc., the two largest stump-to-dump contractors in that division.

99. Both Olympic Forest Products Inc. and Powell Daniels were efficient contractors who had worked for many years with Cascadia and its predecessors. Olympic had operations in Cascadia's Port McNeil and Queen Charlotte Divisions, as well as at Stillwater. It also owned and operated a log sort yard at Stillwater that Cascadia used for all timber harvested from both its Port McNeil and Stillwater Divisions.

100. At the end of the day, Cascadia, in order to find the additional 180,000 m³ required to reduce its volume to meet the cap had to choose between eliminating either Powell Daniels or Olympic. Cascadia decided to consolidate Olympic's operations at Stillwater. This offered efficiency by centralizing Olympic's operation and reducing the number of contracts Cascadia was required to administer. Olympic's ownership of the log sort was also a factor in Cascadia's decision.

Jeff Terman, Direct Examination, Transcript, December 17, 2007, pp. 32 – 36.

101. This was precisely the kind of difficult decision, resulting in the termination of one experienced and efficient contractor, and the consolidation of the operations of another experienced and efficient contractor, which Section 33.22(h) of the *Regulation* contemplates that licence holders will make under a Proposal.

102. When Cascadia's decision to terminate Powell Daniels' contract is viewed in the context of the Proposal as a whole I am satisfied that the licence holder applied the objectives of its Proposal consistent with the AAC reduction criteria, and that in doing so gave the requisite consideration to the interests of its contractors, and applied the criteria in a manner that was objectively fair and impartial.

Past Disagreements

103. Mr. Hussey testified about a number of incidents involving disagreements between Powell Daniels and Weyerhaeuser, or Cascadia. The Claimant acknowledged that several of these incidents were the kinds of minor disagreement that could be expected to arise in the normal course of a relationship between contractor and licence holder.

104. Powell Daniels relies principally on a single incident. In April, 2005, the Claimant refused to barge equipment owned by Tymatt to work for which it had successfully bid on Powell Lake until Tymatt had repaid a debt, of about \$5,000.00, which it owed to the Claimant. There is no question, that at the time, both Mr. Ternan and Mr. Jackson were disturbed by Powell Daniels' action. They were disturbed because Tymatt and Powell Daniels had been unable to resolve their differences, over a relatively small sum. Their dispute had escalated to the point where, as Mr. Ternan put it, he and Mr. Jackson felt that Powell Daniels was holding Cascadia and Tymatt "for ransom" because the Claimant had the only barge on the lake.

105. Powell Daniels submits that this disagreement was a factor motivating Cascadia's decision to terminate Powell Daniels. The Claimant argues that within two months of the barging incident, Mr. Jackson took charge of the Bill 28 take back process for Cascadia, and that when his team met on July 27, 2005, Mr. Ternan produced a spreadsheet assigning Powell Daniels number one priority on a scale of one to ten for termination.

106. I find that Cascadia made its decision to terminate Powell Daniels without regard to any past disagreements, including the barging incident, which had been resolved well before Cascadia prepared its Proposal. It is correct that Mr. Jackson's team did produce one iteration of its spreadsheet on July 27, 2005, which identified Powell Daniels, along with a number of other contractors across Cascadia's four licenses, as ranked priority one for termination. However, the evidence is that Cascadia quickly abandoned its initial attempt to develop a system prioritizing contractors for termination. Between July 27, 2005 and September 27, 2005, the Cascadia team produced numerous iterations of its spreadsheet showing options for allocation of the Bill 28 volume reductions. Some the spreadsheets modelled options under which Powell Daniels was retained with either an unreduced cut, or with a reduced cut. Others identified the Claimant as one of the contractors who would be terminated. I am not persuaded that there was any connection between the barging incident of April, 2005, and the development of Cascadia's Proposal.

107. Mr. Ternan testified that there was no bad blood between Weyerhaeuser and Powell Daniels, or any other contractor. I accept his evidence, and that of Mr. Erin Badesso and Mr. George Nyman, two other members of the team that worked on Cascadia's Proposal, that past

disputes with Powell Daniels were never even mentioned during their deliberations on the proposal.

108. All of Powell Daniels' disagreements with Cascadia were resolved. None of them ever reached the stage where they were referred to dispute resolution under Powell Daniels' replaceable contract, and the *Regulation*.

109. The Claimant has not established that Cascadia had regard to the bargaining incident, or any past disagreements with Powell Daniels in its application of the AAC reduction criteria.

Award

110. The fairness objection of Powell Daniels is dismissed.

111. Notwithstanding the result, I have concluded that this is an appropriate case for each party to bear its own costs and disbursements of the Arbitration. This case raised challenging questions relating to the application of Section 33.22(h) to Cascadia's complex Proposal. The answers to those questions are not, in all cases, obvious. Powell Daniels was entitled, under the *Regulation*, to challenge Cascadia's Proposal. As a result of the operation of the Bill 28 process, and through no fault of its own, it has lost a valuable asset, its replaceable contract at Powell Lake.

112. It is so awarded.

DATED at the City of Victoria, in the Province of British Columbia, this 24th day of February, 2008.

PAUL J. PEARLMAN, Q.C.
Arbitrator